Vostok Nafta Investment Ltd

Annual Report

2007

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Monthly net asset value calculations
Vostok Nafta publishes a monthly estimated net asset value, issued no later than the 10th of each month. This information is published in the form of a news release as well as on the company's website www.vostoknafta.com

Financial information for the year 2008
The company shall issue the following reports:
Interim report for the first three months:
May 21, 2008
Interim report for the first six months:
August 20, 2008
Interim report for the first nine months:
November 19, 2008
Financial accounts bulletin:
February 11, 2009
Annual report and account:
April 2009
General meeting of shareholders 2008:
May 14, 2008
General meeting of shareholders 2009:
May 2009

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“In ten years we will be happy” – Russia in the coming decade

Vostok Nafta has been an active investor in Russia and neighboring countries for well over a decade. In fact our history goes back to early 1995 – when our founder Adolf H Lundin bought his first shares at the then infant stock exchange in Moscow, and planted the seed to what a little more than a year later became Vostok Nafta. During the years that have passed since the inception of our Company, we have seen Russia transform herself in a multitude of ways.

Last year’s Annual Report featured a text in which Mr. Christopher Granville used the rearview mirror to look back into the ten years that had passed since Vostok Nafta became a publicly listed company. So, we now all know what lies behind us – and what unprecedented values have been created in Russia, and for Vostok Nafta’s shareholders, during the past decade. We know that today’s Russia in many ways is a completely different beast to the Russia of the mid 1990’s, and we are ever thankful for having had the great fortune of being able to closely follow the monumental changes that have taken place within all parts of the Russian society during this time period.

However important the past and the lessons to be learned from it is, now is the time to look ahead and try to see how Russia will once again transform herself in the coming decade. The crystal ball perspective will clearly help us shape our future investment strategy in order for Vostok Nafta to keep delivering the same high rates of return that our shareholders have come to expect.

At the time of writing of this Annual Report, it seems like a surprisingly large part of the horde of global know it-alls are all running in the same direction when proclaiming that we are quickly heading towards a global economic slump. So, is that really true? And where will Russia find itself in this economic puzzle? To help understand the kind of challenges and opportunities Russia, and to some extent the world, will be facing in the coming ten years and beyond, we gathered three of the top experts on Russian politics and macroeconomics in Moscow in late March of 2008 to initiate a round-table discussion amongst them.

Dmitri V. Trenin (“DT”) is deputy Director of the Carnegie Moscow Center, a senior associate of the Carnegie Endowment and chair of the Moscow Center’s Foreign and Security Policy Program. He is the author of several publications on Russia – such as *The End of Eurasia: Russia on the border of Geopolitics and Globalization* (2002) and *Getting Russia Right* (2007).

Al Breach (“AB”) worked in Russia for 11 years from mid 1996 as an economist and research director at investment banks Brunswick UBS/UBS and Goldman Sachs, and, initially, the government think-tank RECEP. He has authored numbers of papers on Russia’s economy and is widely cited.

Christopher Granville (“CG”) is Managing Director of Trusted Sources, an independent research company specializing in emerging markets. He has overall responsibility for the firm’s research product as well as being directly responsible for the research on Russia – which has been the focus of his activity since 1991, first as a British diplomat and then for ten years as an investment strategist for Moscow-based investment banks.

Having these three distinguished gentlemen gathered for a thorough discussion on Russia’s way forward, let’s waste no time and instead jump right into a discussion about the current phase of transformation in the top Kremlin office – and what the succession of power from Vladimir Putin to Dmitry Medvedev will mean for the future of Russia’s political system and the development within the Russian society over the next decade.

CG: What we see now is the mainstream elite of Russia gathering around an idea of modernization, and of how the country must pull together to extract itself from the collapse of the Soviet system and the deep dislocation and hardship that followed on that collapse and lasted for a decade or so. The main political point that I would like to make here is really that the Russian political system is that of a “Big Tent”.

This system differs from the conventional arrangements that have evolved over centuries in Western Europe and North America, where there is a loyal opposition and where the elite are split into clearly defined configurations – classically two, but there can be more. In this system the rotation of power from one set to the other is guaranteed. This is clearly not what we have in Russia, where the main stream elite – the “Big Tent” – are always going to be absorbing the best

ideas. If any of the marginalized opposition players were ever to have a good idea, which they of course will and do have, that would probably be stolen and included in the main stream policy consensus.
This model places enormous burdens on the elite. For the system to work the elite has to be fantastically public spirited, and refrain from the natural instincts of greed – and be able to apply a certain amount of self denial in the face of the vast opportunities for corruption that exists within such a system.
One can easily see a scenario where the present popularity of the government could wane, even if they do everything right – as the public's expectations of higher living standards and real incomes will most likely outpace the actual growth of these factors. As the popularity declines, the temptation to change the constitution and then lose the cornerstones of legitimacy will clearly pose a threat to the whole system.
My own view is that the elite has so far shown signs of adequate patriotism. For all its greed it still doesn't look to be anywhere near the extreme end of the spectrum – where lining your own pockets and forgetting about the country is priority number one. I therefore view these arrangements as being compatible with successful modernization to a greater or lesser extent.

DT: The rotation at the top is absolutely necessary for this system to function, and President Putin was one of the few who clearly understood that from the beginning. His position was unflinching, even though he was in a small minority within the elite and within the country itself when he made clear that he did not want to overstay his welcome. That was my first point. The second thing that struck me with this process was the smoothness of the transition – as conventional wisdom has it that in order to transfer power at that level and at that juncture you have to be ready to see some blood – either virtual or real. So far this has not happened, and there is a good chance it won't happen - instead it looks like the transition of power could actually become a peaceful transition within the system. However, there are still uncertainties ahead, and I believe that both Putin and Medvedev see these uncertainties, as well as everyone else does. This amounts to a real constitutional change, as Putin in a bid to preserve a system that he obviously cares about is now changing the essence of the constitution – while still abiding to the letter of it.
I would use the word 'Regency' to describe the new political period which Russia is stepping into with Medvedev succeeding Putin. This is a period where Putin will play the role of the supporting regent, someone who is supporting Medvedev on his takeoff. I see no reasons for Putin to try to undercut Medvedev or to try to keep him down, as I think he is genuinely interested in Medvedev's success. I get the impression that Medvedev really wants his new job. He is not a politician, but then again – this is not a time for conventional, western style politicians in Russia.
Medvedev clearly sees his mission as the next president to lead the charge in modernizing the country.
My third point would be that both Putin and Medvedev are following, subconsciously or even consciously, the precept of Pjotr Stolypin from the beginning of the past century when he said "Give us 20 years of peace and quiet". If you count from day one of Putin in the Kremlin, which was the 1st of January 2000, and look at the 2020 strategy this is exactly the 20 year period that Stolypin thought was absolutely necessary 100 years ago, and that Medvedev and Putin still thinks is absolutely necessary to turn Russia into a modern country. I think they are guided by a very clear understanding that unless Russia itself takes off, it is likely to go down. The only way you can keep a country of Russia's size, of Russia's diversity, of Russia's geopolitical position, wedged between China and the Muslim world, together is to thoroughly modernize it. This applies to the economy, the social sphere and the political sphere.
The crucial question in the model of the "Big Tent" is how big the tent will be? How accessible it will be to the people from the outside? What are the terms of entry – and how much diversity will be tolerated and encouraged within the tent? In the medium to long term I do see some new structures appearing within the tent, with some factions forming and some groups promoting various interests and ideas.
I agree with Christopher when he says that the burdens on the elite in this system are enormous. Quite frankly, I am not sure that the present elite have the critical mass of ingredients to cope with these burdens. But Russia is a country which is led by a very young elite, and there will be new people coming in to the tent all the time, and in many cases these new

people are extremely well educated, extremely motivated and very successful. They will be able to create a stronger elite than the one that is ruling from inside the big tent today.
My penultimate point is that nationalism is becoming more and more evident in Russia of today. This is reflected by the fact that the people that now lead Russia believe in competition and a lot of them are prepared to compete ruthlessly with each other, because that's how they see the way of the world. They compete as individuals and as companies, but they also compete at a national level, which is of course reflected in Russia's foreign policies – which I am sure we will get a chance to discuss in further detail later on in today's conversation.
The Elites are extremely important within a system like the one of the "Big Tent", but – and this is my last point with regards to this specific topic; it is absolutely crucial to see whether this elite manages to carry the larger society with them, whether they will be able to send the message to the society as a whole that all boats will rise – and that they will rise pretty high. The Russian system is an authoritarian one, but an authoritarian system that has the consent of the governed. If Putin and Medvedev are successful in their efforts to pay more and more attention to the social dimension, the regime will be seen as legitimate – which will give Russia a much better chance to transform and modernize itself.

AB: The point that I would like to make beyond what's been said so far, may be obvious, but I believe it is still an important one. The problem with the model of the big tent is that while it is stable it is not very flexible: policy negotiations go on inside the big tent between the different factions and groups without much transparency, transparency which makes the debate more open, explicit and inclusive; additionally, there is not a well agreed upon electoral system through which to change policies and factions, democracy's great strength. This stability of itself is good in numbers of ways in the shorter-term – it supports both the workings of what is now a decent system and the strong economic momentum. The flip side of this is that the inflexibility can become a real handicap in the longer-term when you need to make alterations that hurt some of the interest groups. The tendency could therefore be towards easier choices: instead of making the necessary tougher choices the elite could take the easy way out, for example by running up budget deficits in one way or another to maintain short-term growth and social stability, or using "administrative means" to deal with inflation. This would make the whole system more vulnerable to changes in the global economy or social dynamics.
For the next ten years then, this stable but rather brittle system of the big tent model looks like being a useful one to address the challenges confronting the country. But the danger is that even if the modernization indeed happens successfully, the system will become more sclerotic over time – and you might end up with a major crisis in a couple of decades or so as the need for more flexibility, transparency and openness kicks in. The challenge thus for Medvedev, Putin and co. is to gradually open up this system so it evolves to a being a more flexible one in the coming decades.

As Dmitri Medvedev was elected president of The Russian Federation in March of 2008, the discussion continued on whether Medvedev is only here to stay for one four year term and then leave over to Putin – who could lead Russia for another two terms until 2020. However, this is an idea that is largely rejected by the participants in our roundtable discussion.

DT: We do not know what kind of a president Medvedev will become – and neither does Putin himself. I am sure that Putin would step forward to carry the burden of saving the system if Medvedev for whatever reason fails to perform. In my mind, that is only an emergency fall-back and not the base-case scenario that Putin has in mind. I would not count on Putin being back in the Kremlin to succeed Medvedev – but he clearly sees himself as a guarantor for the Russian system.

Our discussion has to a great extent come to focus on the topic of stability in the current system of Russian politics and society, while the dominating trend in respect to the global situation rather seems to be that of ever evolving patterns of change. We see how countries that do not recognize that the world is rapidly changing are running the risk of falling behind. The question is then

if Russia will be able to react to the ever changing world around itself, while the above mentioned system of the big tent is still in place?

DT: I see Putin and Medvedev as belonging to two different historical eras, and we are sitting here at a junction of two important periods in Russian history. One era is closing with Putin, while the other is opening with Medvedev. In my opinion Putin was not about change, he was about stabilizing the country after a long period of tremendous changes in Russia. His role in the group of Gorbatchev and Yeltsin was that of a president that could consolidate the principal achievements of the two revolutionary predecessors. If you look at Putin's agenda, it started with making sure that Russia remained in one piece – and has since been about fighting separatism, fighting the charge of the oligarchs and the communists, the liberals as well as the west. Medvedev on the other hand will have to be a modernizing president, as there is no more stabilization to be done. Everything has already been stabilized in Russia, and if you continue to stabilize there will just be stagnation.
From now on it will all depend on whether the people that control the "Big Tent" will be able to capitalize on the talent which exists within the Russian society, if they will be able to exploit that talent for 'The Good of Russia' or not. Medvedev will have to make sure this happens – as stabilization is no longer the name of the game in Russian politics.

I would now like to turn the floor over to you, Al Breach. At the time of this round-table discussion we find ourselves in the middle of a global credit crunch, which some analysts think will turn into a much broader crisis for the global economy. I know that our shareholders would like to learn more about your views on how the global macroeconomic situation – as well as the Russia-specific situation will play out over the coming years.

AB: There are clear historic comparisons to be made when looking at Russia today. "Catch-up growth" – as defined as a rapid, 6+% growth, driven by a combination of strong productivity gains as foreign technologies are imported, rapid accumulation of capital stock and a shift from rural to urban labor have previously been seen in countries like Japan, Korea, post-war Germany, France, Italy etc. and has historically lasted for some 3 decades or so. China, India, Russia and a relatively larger number of other countries looks to be in such a period of rapid growth right now, with at least a decade or more to go. That to me suggests a continued strong global GDP-growth – and at the same time I see how the prices for most commodities will remain at historically high levels.
Sure, there are no doubt so that the current US downturn presents headwinds for this story of global growth – but lower real interest-rates in the short term, reduced capital flows to the US and the strong balance sheets of the countries within the emerging market sphere all suggest that the story will not be knocked off-course. A global slump is possible, but it seems notably unlikely from my horizon.
The above mentioned story of catch-up growth, combined with still undervalued currencies in China, Russia and some other emerging markets countries will most likely mean that the emerging market block will continue to gain in importance when measured as their share of the global GDP. This is of course important for capital markets, as we'll see more capital flowing into these emerging markets and, in general, returns on asset classes in these countries should be higher than those in the developed world. Developed world companies focused on emerging markets will also be key beneficiaries in this scenario.
Looking at Russia specifically, the starting point for the country could not be better. Russia has one of the best (if not the best) state balance-sheets in the world; it is running a big twin surplus (with the budget balancing in 2008 at oil prices of less than USD 50/bbl); it has a decent economic structure (relatively open markets, pretty capitalist structure, etc.); and it has bags of economic momentum for the growth to be sustained. This, combined with the outlook, means that Russia is in an excellent position to enjoy the decade that lies ahead.
Beyond a world-wide slump, the biggest risk for Russia in the period ahead is that the government will shoot the country in the foot, through poor economic policy. Russia now has strong growth momentum; it is theirs to lose. However, ever more state-dominated policies and/or anti-foreign policies could cause a drop in confidence that would give up this momentum. If this would happen at the same time as oil prices fell, the consequences could be felt quicker than is

generally assumed. However, this does not seem very likely – the government has generally remained pragmatic and hard-headed in the economic area. But, the longer the oil price stays, and so the easier growth becomes, the greater the risk of serious errors being within the area of economic policy making.

Russia has an economy that is highly dependant on its natural resource industries, what about the much discussed diversification of the Russian economy – will that be a dominant theme in the decade to come?

CG: I believe that it is important to point out that one should not be neglecting ones key strengths. The idea that extracting oil and minerals from the ground is not good enough for a country is somewhat flawed in my view. These industries are in fact dependent on very advanced technologies and tremendous know-how. The modern world is not all about people manufacturing advanced equipment.

AB: To be fair, the efforts made so far to diversify the Russian economy – which mainly consists of the heavy taxing of the oil and gas sector in order to deliver fiscal stability which then promotes domestic growth such as demand for cars, banking services, telecommunications etc – has in fact been very successful. However, I agree with Christopher fully: with Russia having this unbelievable resource of oil and gas at a time when energy prices are shooting through the roof and at the same time be struggling with managing to achieve even a 1% increase in oil production (latest numbers show it actually falling) is clearly a wasted opportunity. It is interesting to learn the lessons from the Russian metals and mining industry, where you have seen truly globally competitive companies emerging in Russia. Diversification is good if it happens, and it will happen in Russia, but you should let the economy focus on what it is good at and where it has a competitive advantage. Of course we all know this, but oddly enough it quite often seems to be forgotten.

DT: Politics can clearly distort economic thinking. What powers this Russian modernization? Well, it is not about becoming an efficient global player per se, but it is to put Russia back into the category of the big powers. That is exactly what is a real concern to me – that Russia will let politics interfere in too many ways with economically sound reasoning, just to be able to prove that the country is still a super power with national champions able to stand up to the other major players in the business world.

We have been talking a lot about big businesses so far, but what about small businesses – isn't there a clear risk that they will not be allowed to grow and flourish in a Russia where creating national champions seems to be of such a great importance?

CG: As Dmitri so eloquently put it, the modernizing elite will have to bring the rest of the society along with them. And in most successful economies it is small businesses that will create employment and drive substantial growth, with the ensuing creation of a flourishing middle class. The growth of small businesses in Russia is therefore extremely important in order for Russia to prosper – and for the establishment of a healthy middle class across the country.
This is also of very great interest for the investment community, since there are tremendous opportunities to generate earnings and growth within this sector – especially when it comes to private equity.
This is the way that the society can be brought along, and the way the middle class can start to materialize and can start to exercise its rights and to demand not only consumerism, but also voice and ultimately political rights.

AB: I think the picture within this area is a much brighter one than gets generally painted in the western press. There is obvious evidence that small businesses are growing, and growing fast. We have seen a rapid growth in the number of companies and their size etc. And this in spite of problems like poor administration and corruption. We have to remember though that it takes time for the huge liberalizing moves – all the structural reforms that were made in the 1990s and during Putin's first term – to bear fruit. We have seen in the UK that the structural changes of Thatcher have really born fruit in the 1990s and 2000s. That's why I see a lot of momentum in this area going forward, and why many of us see lots of reasons to be encouraged.

It is not only in the non-resource sector that these developments matter: It would be great to see medium size resource companies being able to prosper without being taken over by their larger competitors. There is plenty of scope here for smaller companies to do the things that are below the radar and too irrelevant for a Gazprom or another large company to organize. Productivity increases often come from small businesses rather than from the larger companies, and the growth of small and medium size businesses within this sector is clearly a way for Russia to keep growing the overall size of the output from the natural resource industries.

DT: Just as Putin's grip did not reach very far from Moscow, neither will Medvedev's. The question is therefore of course how the more than 80 'mini Kremlins' around Russia will react to the changes to come. Some of these regional governments will inevitably exhibit a more forward looking attitude to business life than others.

Coming back to this "year of change" in Russian top politics and the fact that Medvedev is about to take over after eight years of Putin in the top Kremlin office, what is it that Medvedev will have to achieve in order to be able to stay in power for more than one term? What is it that he will be judged on at the end of the day and how can he make sure that Russia is reformed – rather than falling into a dangerous state of stagnation?

DT: I hope Medvedev will be judged on how successful he will be in implementing some of the 'slogans' that he has put on the table. He talks about the independence of the court system – which is what people expect from a trained lawyer. And, if four years down the road the court system is still in the same state as it is today, the Russian people will not view him as having succeeded. He will also be judged by how open his system and his presidency will be – how far he will go beyond the usual suspects. How welcoming his administration will be to those offering new ideas and new thinking. There are now a lot of people that see the dawn of a new era in the country – people who have had nothing to do with the government and the Kremlin before, and now they want to join in. These people do not do this for money, but to help the country to do better. There is a tremendous resource of goodwill that Medvedev can benefit from – but he has to act fairly quickly to mobilize the support. If he gets that support and if his administration is seen as a forward looking one, then he will have bridged the gap that existed under Putin between the Kremlin and the educated and successful people of Russia that was not part of the Putin system.

AB: Putin stabilized Russia and got the country in fabulous fiscal and financial order. He also started to create the necessary institutions to distribute that wealth throughout the country. What needs to happen during Medvedev's first term is that we need to see that modernization really happens on the ground – in terms of infrastructure built: big roads, big railways, big modernization of airports etc. That is something that one can for sure look forward to, and this will most likely be a motor for growth in the near term, as well as an important theme in the investment community. There are a lot of reasons to be optimistic here, but this development is of course not without administrative challenges.

As we mentioned above, the Russian Economy is still highly dependant on the natural resource industries and with oil prices hovering above 100 USD/barrel, is there any real risk of a situation where new green technologies emerges and Russia will be left behind?

AB: The obvious risk for the Russian economy, and one of the few reasons I can see why it could not keep growing at high single digit numbers in the years ahead (it seems highly likely that it will do so) - is of a global slump that would pull commodity prices down hard, an eventuality that would then quickly feed through to Russia. I am personally not too worried about a global slump, and the demand for commodities shows few signs of weakening in the emerging world. Also, since Russia has been running such a tight fiscal shop and amassing huge reserves, they have lots of firepower to offset external weakness with these funds. So in sum, I think that this risk has generally been exaggerated.
Could Russia get blind-sided by significant advances in green technologies that would mean that the role of oil and gas in the world suddenly becomes less

important? In the longer term, say 20 years or so, I believe this is a real risk for Russia. The longer oil prices stay at these levels, the stronger the trend towards alternative fuels will be. However, I do not see any reason for us to worry about that in the next ten years or so.

How is the western media's often overly negative stance towards Russia affecting the country's economy – and is the issue of a lack of trust a real concern for Russia?

AB: In a financial nutshell – where Russia is today it is all about growth and about putting money into greenfield and longer term projects. The issue of trust is therefore vital – as an investor you need to have trust in the fact that you will see the fruits of the capital invested coming your way. The bad press that Russia is getting, whether it is merited or not – and I think it is a mixture of the two – is important because it certainly affects peoples willingness to put money into long term investments in Russia.

DT: The Russian authorities are not yet into serious work to think through the reasons for the skeptical attitude that they are confronted with in the west. The fact is of course that Russia has a miserable public relations strategy. A classical case of how you can undermine your own position by paying no attention to international public opinion was the effect of the gas crisis between Russia and Ukraine at the beginning of 2006 – a totally unnecessary self-inflicted wound. Russia stepped into a real foreign policy disaster by neglecting public opinion whole-heartedly.

It is clear to all of us that Russia is viewing herself as one of the true super powers in the world – which has at times led to conflicts with the west and with its neighbors. How can we expect the foreign policies of Russia to change in the coming ten years? How will the picture of Russia in the world and how will the way Russia sees herself change, if at all?

DT: I think that Russia has found a sustainable position in being alone and yet being a modernizing and integrating great power. I do not expect this situation to change. It will be very important what balance between nationalism and integration Russia's foreign policy will hold. Politically, I see a lot of competition going forward, with most of the world – especially with Europe and the United States. This doesn't strike me as a particularly bad scenario though. I would imagine Russia's relations with the rest of the world as being that of a relationship between unaffiliated members that has some interests that are colliding and some interests in common.

So, where will Russia be in ten years from now?

CG: Well, I myself heard President Putin make a joke at a meeting of the World Economic Forum here in Moscow in 2002. He was asked by someone where he saw Russia in ten years. His answer was memorable – at once teasing and ironical while revealing the seriousness of his ambitions for the country. He said: "I think that in ten years we will be happy".

2007 saw the large Gazprom position being separated from the rest of the portfolio through the division of "old" Vostok Nafta Investment Ltd into Vostok Gas Ltd and "new" Vostok Nafta Investment Ltd.

Those shareholders who so desired were able to get better exposure to the non-Gazprom part of the portfolio through the "new" Vostok Nafta than was possible under the old format. The business idea nevertheless stands the same – which is to achieve a high return for our shareholders through mainly portfolio equity investments within Russia and its neighbouring countries. We can undertake public as well as private equity investments. Since inception we have found enough value within the public part of the Russian equity market (although the lines between public and private has often been blurred by low standards of corporate governance) to have the majority of the portfolio invested in listed stocks. However, we have always been conscious not to own companies where we cannot add any value, which means that we have not been sitting on stocks which both institutions and retail investors can own themselves.

Over the past years the public Russian equity market has developed in both quality and depth, which in turn has led to higher valuations – thus making it more difficult to achieve the kind of returns we believe our shareholders expect from us. The quest for higher returns has led us to invest into an increasing number of private equity situations. The deal flow that we are currently analysing is to a higher degree than before encompassing situations that are not yet listed.

The fundamental process by which we carry out our investment work often takes off from a very strong thematic conviction, from which we try to make high return equity investments. Our two dearest themes, which we also share with the "Lundin Group of Companies" at large, is that the oil price is going higher over time and that of the current long commodities super-cycle. Whereas the oil price theme was one that very much dominated the portfolio ten years ago, it is still one which we believe in - but these days we do struggle a bit to find assets that fits into our investment portfolio. This is mainly due to the strong concentration of the region's oil assets into a few large and dominant players. The commodities investment picture allows for more opportunities for us, especially in the semi-public and small-cap world.

The three other macro themes are more "Vostok specific": Russian energy restructuring, Russian infrastructure expansion and "What works in the West works in the East".

Russian energy restructuring is a theme that is of course central to the most important value driver at Gazprom, the de-regulation of Russian gas prices and the complete liberalisation of Russias energy market. This drives not only gas prices, but also thermal coal prices as well as electricity prices. Our preferred exposure to this theme is through the thermal coal companies, but we also have positions in hydro power and uranium mining.

Everyone is investing into new capacity in Russia: domestic industry, foreign corporations, real estate companies and, last but not least – the Russian State which has just announced an enormous programme to upgrade the country's transport network. Being an investor in Russia, one certainly wants exposure to this part of the growing Russian economy. Vostok Nafta is getting this exposure through our investments in cement companies and a company making concrete mixers.

Finally the long-named (and I admit somewhat corny) theme "What works in the West works in the East" is a somewhat dated description (maybe Russian normalisation is a better description?) of our eagerness to invest into management teams with Western experience built around business models that have not yet reached their peaks in Russia. Here we come across sectors and industries where we have less previous experience in comparison to the oil and mining sectors. What happens in our investment process is simply that the hurdle rate goes up and if the investment lives up to it we will make it. Agriculture, media, yellow pages, consumer finance to name a few… a potential high return is what is common to them all.

We have witnessed some turnover in the portfolio during the second half of 2007, and we expect this to continue going forward. Some of our dear macro themes have caught more general attention than others, which has led to a revaluation to fair value of some of our investments. This turnover in combination with us leveraging our company to the 15–20% level that we have traditionally used at Vostok Nafta will help finance the new investments that we expect to conclude during this year.

Enough has been written about the effects on the global economy from the subprime crisis in the US for us

Managing Director's introduction

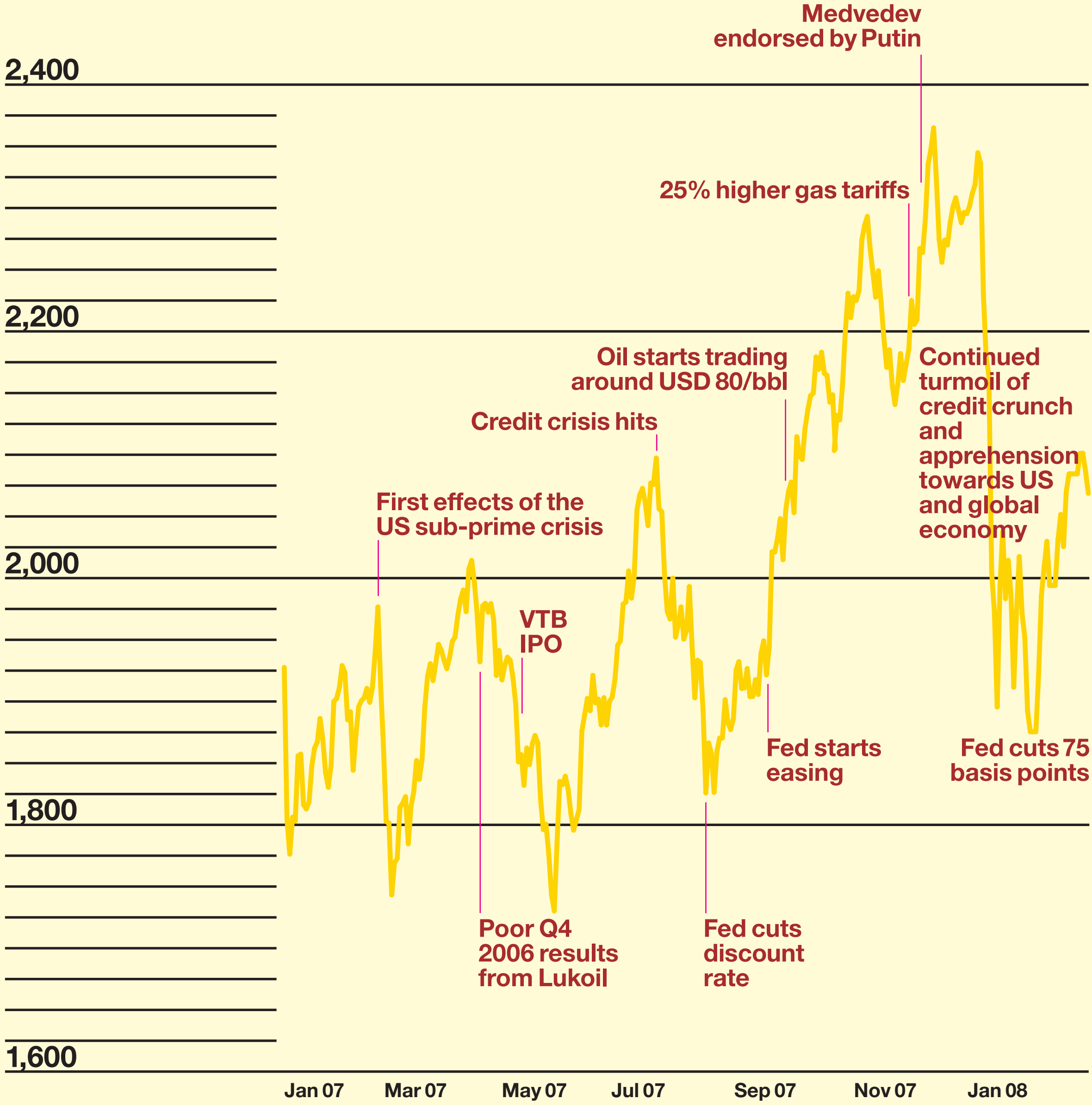
not to need to cover it at any length here. Will it lead to slower, and possibly negative, growth during the next couple of quarters? Yes. Will it lead to a collapse in demand? Not likely. The lately so beaten down theory about business cycles seems to be back in fashion and we are in for a softer patch, which will take its toll on typically cyclical industries which have had some very good years. However with the risk of being inconsistent we do not see a prolonged downturn, if any at all, for the price situation for many commodities – including oil, copper and zinc. This is driven by supply issues in all of these markets, which are to an extent being addressed by investments into new production capacity. However, these investment projects are yet to deliver real production. Demand for oil for example would have to not only stop growing, but also actually contract for existing supply sources to be keeping up. Against this backdrop we do see Russia holding up well. A short term softer commodity pricing outlook (for example oil falling to USD 65–70 per barrel in a momentum driven very bearish short term environment trying to discount an outright collapse in demand) could bring down Russian GDP growth rates to 5%, from the current level of around 8%. This might actually have a positive effect in the difficult fight against inflation in the country. Several years of 7–8% GDP growth rates have brought with it signs of overheating, most notably in the inflation figures (at 12.6% year-on-year in January 2008).

However, domestic savings in Russia, especially of the public kind, are large enough to cushion against the short-to-medium term gloominess in developed markets.

In general terms a higher inflation does erode the margins of commodity exporters, requiring a more selective approach to stock picking within these sectors. Companies with a domestic focus not only on costs, but also revenues will obviously benefit in relative terms. Another clear implication of the heated macro situation in Russia is the strengthening rouble. The reluctance of the Central Bank of Russia to use an appreciating currency as an anti-inflationary tool stems from the competitiveness of the above mentioned sector, but we could very well be looking at more dramatic measures on this front initiated by the new President's administration, most likely coupled with renewed efforts on the structural reform side.

We look forward to the rest of 2008 and beyond. We have the deal flow, the financial capacity and the manpower to live up to our shareholders' high expectations. Adolf Lundin's old target benchmark of "three baggers in two years" is something we still very much live by.

Per Brilioth
Managing Director



RTS Index development, January 2007–February 2008

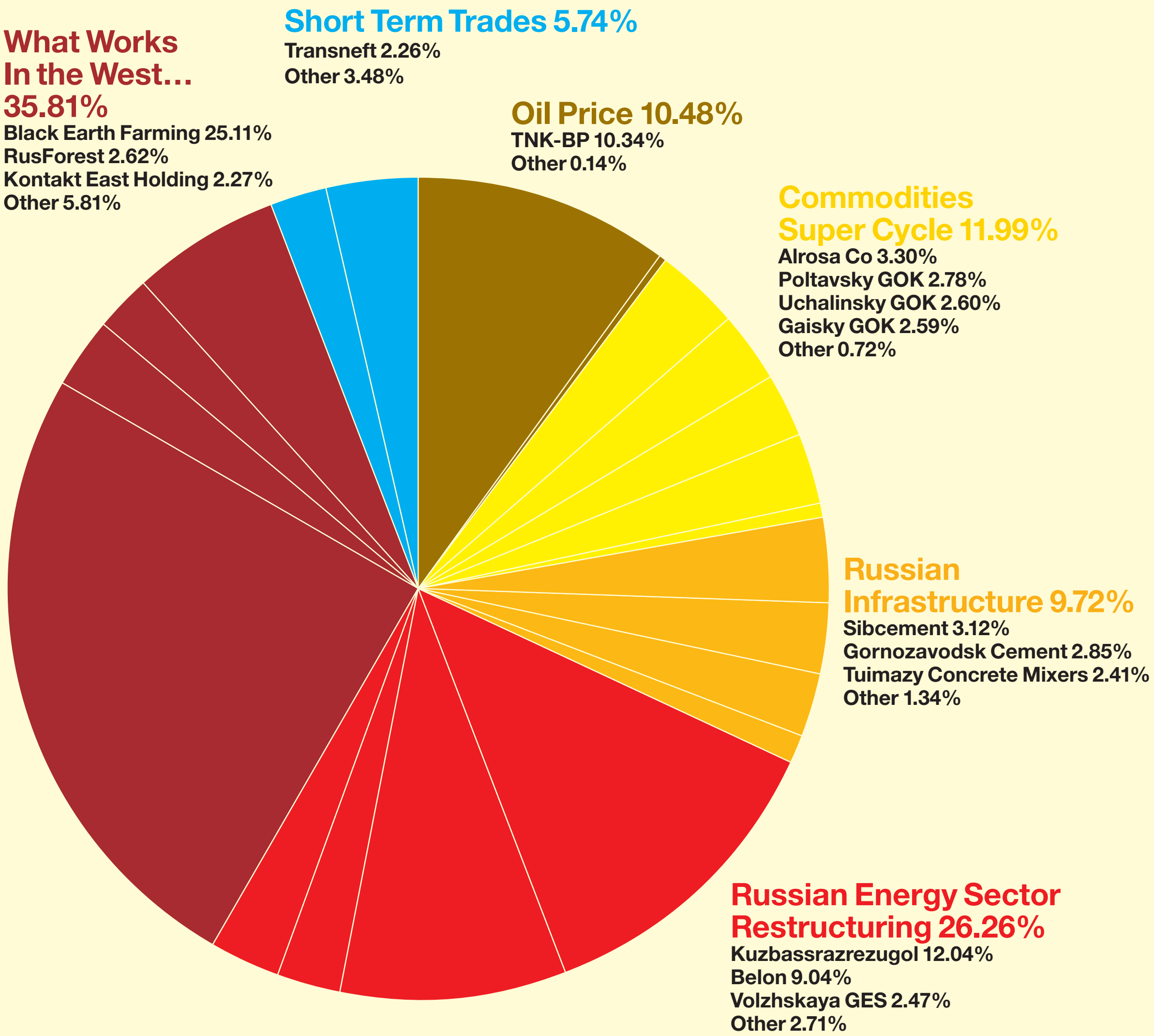
The Group's net asset value as at December 31, 2007, was USD 803.95 mln, corresponding to USD 17.47 per share. Given a SEK/USD exchange rate of 6.4683 the corresponding values were SEK 5,200.22 mln and SEK 113.00, respectively.
The group's net asset value per share in USD increased by 108.72% (excluding effect from proceeds from new share issue: +51.29%) over the period January 1, 2007–December 31, 2007. During the same period the RTS-index increased by 19.23% in USD terms.
During 2007, positive changes in the value of holdings have, together with additions financed by a new share issue and by debt, resulted in a larger portfolio, USD 822.39 mln compared to USD 387.18 mln at the end of last year.

During 2007, net investments in financial assets amounted to USD 151.86 mln. Major investments of the year were the additons of shares in Kuzbassrazrezugol, the purchase of a roughly 0.5% stake in Alrosa, as well as an increased exposure to the Russian power sector through purchases of shares in a series of Russian hydro power plants – Dagestan Genco, Volshkaya GES, Zeiskaya GES and Sayano Sushenskaya GES.
Major sales of the year have been the exits of Raspadskaya, Rosneft, Mechel and Luganskteplovoz.
At the end of December 2007, the three biggest investments were Black Earth Farming (25.11%), Kuzbassrazrezugol (12.04%) and TNK-BP Holding Pref (10.34%).

The Vostok Nafta share portfolio

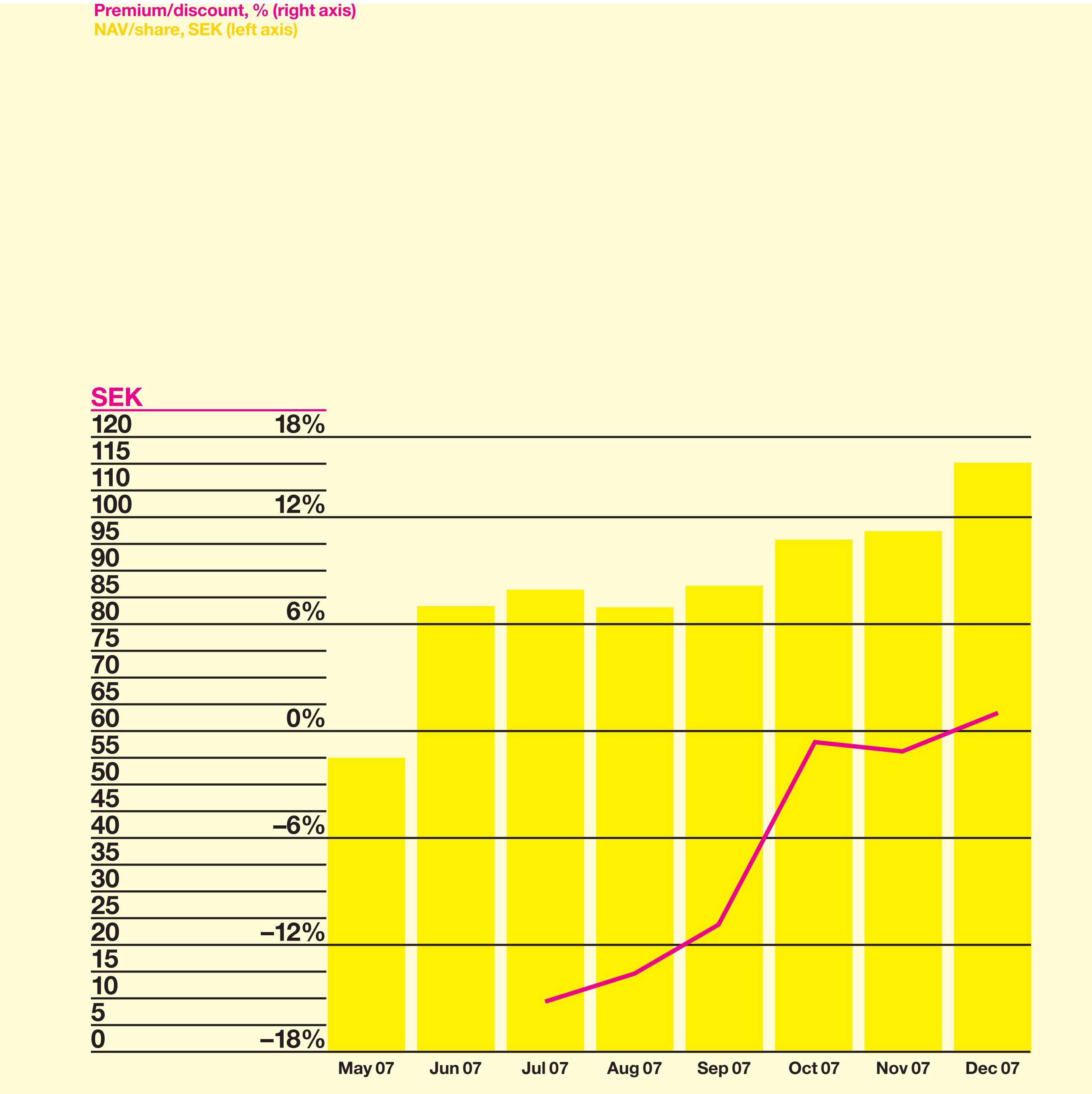
Number of shares	Company	Market price, USD	Market value, USD	Percentage weight	Percentage of outstanding shares
	Oil Price				
233,250	Caspian Services Inc.	3.25	758,063	0.09%	0.46%
5,789,903	Kherson Oil Refinery	0.05	283,705	0.03%	4.40%
2,025	Orsk Refinery Ord	35.00	70,875	0.01%	0.06%
538	Orsk Refinery Pref	29.70	15,979	0.00%	0.05%
45,468,616	TNK-BP Holding Pref	1.87	85,026,312	10.34%	10.10%
100,000	Yakutgazprom	0.15	15,000	0.00%	0.01%
	Total Oil Price		86,169,934	10.48%	
	Commodities Super Cycle				
966	Alrosa Co Ltd	28,000.00	27,048,000	3.30%	0.48%
31,274	Gaisky GOK	680.00	21,266,320	2.59%	5.06%
1,516,055	Poltavsky GOK GDR	15.06	22,831,788	2.78%	1.08%
9,000	Priargunsky Industrial Ord	515.00	4,635,000	0.56%	0.53%
1,200	Priargunsky Industrial Pref	320.00	384,000	0.05%	0.29%
275,000	Shalkiya Zinc	4.00	1,100,000	0.13%	0.49%
1,124,045	Uchalinsky GOK	19.00	21,356,855	2.60%	2.95%
	Total Commodities Super Cycle		98,621,963	11.99%	
	Russian Infrastructure				
39,000	Gornozavodsk Cement	600.00	23,400,000	2.85%	5.03%
1,600,000	Kamkabel	5.07	8,112,000	0.99%	4.12%
151,000	Sibcement	170.00	25,670,000	3.12%	0.50%
1,200,000	Tuimazy Concrete Mixers	16.50	19,800,000	2.41%	14.60%
	Volga – Nash Dom, debt		2,930,000	0.36%	
	Total Russian Infrastructure		79,912,000	9.72%	
	Russian Energy Sector Restructuring				
929,700	Belon	80.00	74,376,000	9.04%	8.08%
72,500,000	Dagestan Regional	0.19	13,775,000	1.67%	1.38%
231,434,053	Kuzbassrazrezugol	0.43	99,053,775	12.04%	3.79%
2,618,241	Kyrgyzenergo	0.06	168,688	0.02%	0.27%
300,000	Sayano Shushenskaya GES	1.80	540,000	0.07%	0.02%
6,167,161	Systemseparation	0.25	1,523,289	0.19%	20.54%
20,903,442	Volzhskaya GES	0.97	20,276,339	2.47%	0.71%
12,570,000	Zeiskaya GES Pref	0.50	6,285,000	0.76%	5.54%
	Total Russian Energy Sector Restructuring		215,998,091	26.26%	
	What Works In the West…				
161,952	Armada	20.50	3,320,016	0.40%	1.35%
26,715,404	Black Earth Farming Ltd	7.73	206,510,073	25.11%	21.47%
272,107	Dakor	26.76	7,282,400	0.89%	4.79%
375,000	Kemerovo Azot	37.25	13,968,750	1.70%	5.51%
2,940,000	Kontakt East Holding AB	4.30	12,636,120	1.54%	31.77%
1,470,000	Kontakt East Holding AB BTA	4.10	6,022,443	0.73%	31.77%
11,004,813	RusForest Ltd		21,521,056	2.62%	50.00%
2,000,000	Sistema	1.64	3,280,000	0.40%	0.02%
	Tinkoff Credit System, debt		6,207,844	0.75%	
	Tinkoff Credit System, WTS		2,000,000	0.24%	
523,800	Waymore Holding (TKS)	22.38	11,720,549	1.43%	5.82%
	Total What Works In the West…		294,469,251	35.81%	
	Short Term Trades				
1,000,000	Bashneft Pref	10.75	10,750,000	1.31%	2.89%
488,000	Gazprom Neft ADR	21.00	10,248,000	1.25%	0.05%
27,800	Tatneft ADR	120.00	3,336,000	0.41%	0.03%
1,200,000	Tatneft Pref	3.60	4,320,000	0.53%	0.81%
9,378	Transneft Pref	1,980.00	18,568,440	2.26%	0.60%
	Total Short Term Trades		47,222,440	5.74%	
	Total		**822,393,679**	**100.00%**	

Vostok Nafta's portfolio as at December 31, 2007



Investment Macro Themes

Vostok Nafta investment portfolio as per December 31, 2007



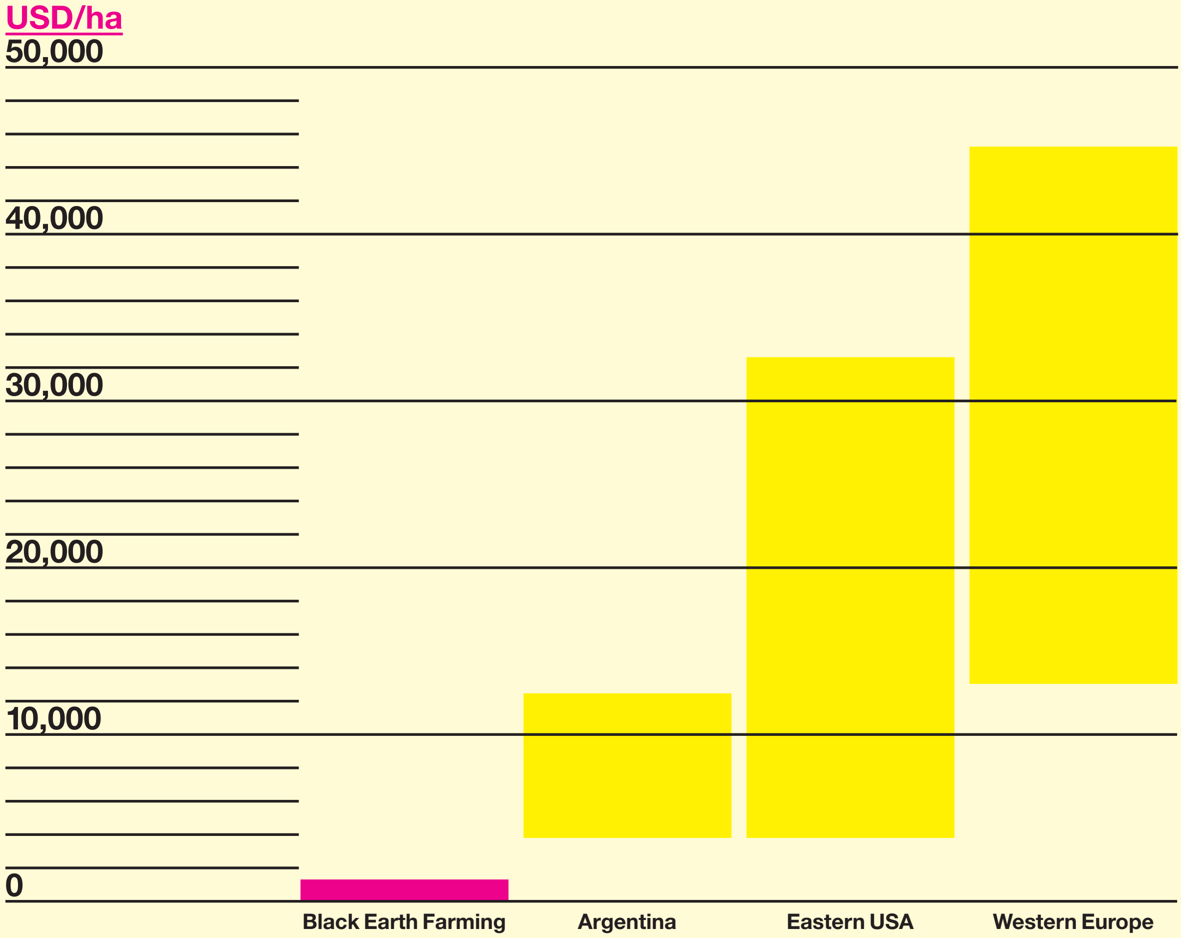
Net Asset Value (NAV) and Premium/Discount Vostok Nafta

NAV May–December 2007,
premium/discount July–December 2007
Source: Vostok Nafta

Black Earth Farming Limited (BEF) was among the first foreign financed companies to make substantial investments in Russian agricultural land assets. BEF has thanks to its early establishment now gained a strong market position in the Kursk, Tambov, Lipetsk, Samara, Voronezh and Ryazan areas of Russia. BEF currently controls over 300,000 hectares of the richly endowed farmland in the Black Earth region, an increase of approximately 178,000 hectares since the beginning of 2007. The land under full ownership contract amounts to 67,200 hectares, and land under long term leases is approximately 16,400 hectares.
During the agricultural year 2005–2006 BEF cropped 5,900 hectares which resulted in a total harvest of 9,000 tonnes of crops, predominantly barley. In 2007 these figures had grown to 53,000 hectares cropped and a marketable harvest of over 100,000 tonnes. The increase y-o-y of the harvest shows the result of BEF's efforts to continuously, and quickly, make the company's existing farmland efficiently harvestable after years of under development. BEF focuses on the production of five major crops, namely: Winter wheat, Rape seed, Corn maize, Sunflower and Barley rape.
To achieve higher productivity and long-term operational efficiency BEF utilizes planned crop rotation schemes, which maximizes the potential of the soil, regional climatic characteristics and efficient use of the company's machinery. These rotations not only spare the soil and increase the harvest, they also minimize the need for chemical pesticides and fertilizers.
Proper soil-management is one of BEF's communicated revenue drivers. BEF has composed a list of six major factors which will play a significant part in the increase of the company's revenues in the upcoming years. These six factors are 1) Selection of crop cultures with high expected profitability, given prevailing prices, as well as other production factors, 2) Increase of the amount of hectares under crops, 3) Increase in crop yields per hectare through proper management of the soil 4) Increase in quality of the harvested product, which generates a price premium, especially by obtaining good seeds 5) Timing of sales – by using storage elevators (BEF recently acquired its first) grain can be stored for longer periods, giving the company an opportunity to sell its produce in times of lower supply and higher prices. The last factor, the general price levels of crops, is completely external and cannot be controlled or influenced by BEF, but depends on regional and local supply and demand balances.
In December 2007, BEF was successfully listed on OMX First North in an offer which was several times oversubscribed. The offer provided BEF with SEK 1,920 million (gross) through an issue of 38,400,000 Swedish Depository Receipts (including an over-allotment option). In conjunction with the IPO, BEF also listed its bonds on the OMX Nordic exchange.
The capital raised will be used to continue acquiring farmland and to develop BEF's farming operations. However, BEF has now moved into a new, more refined, land acquisition stage, whereby new acquisitions are primarily targeted by their proximity to existing assets. This proximity is important in order to create logistics efficiencies and other synergies. Extensive capital investments in modern machinery and equipment are also in progress, coupled with other operation enhancing measures such as thorough soil analysis and the education of the local workforce in modern farming techniques.
To summarise the above discussion: BEF is currently focusing more on improving production costs and margins, than on growing its land bank. During 2008 BEF plans to add an additional 60,000 hectares to its land bank, and more importantly the Company aims to make production more efficient, and increase its gross margin from 27% (in 2007) to over 40%.

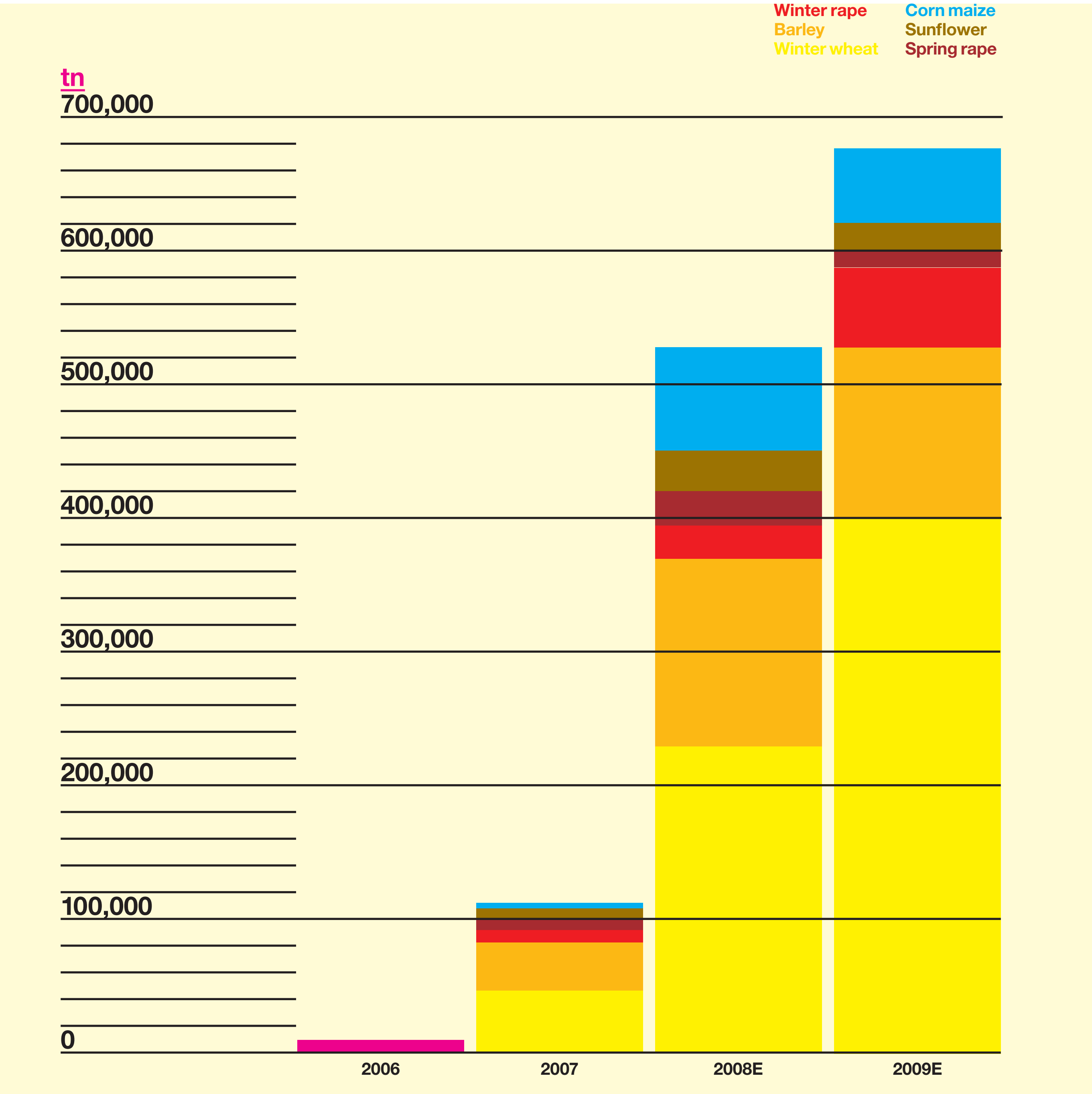
Black Earth Farming

Black Earth Farming

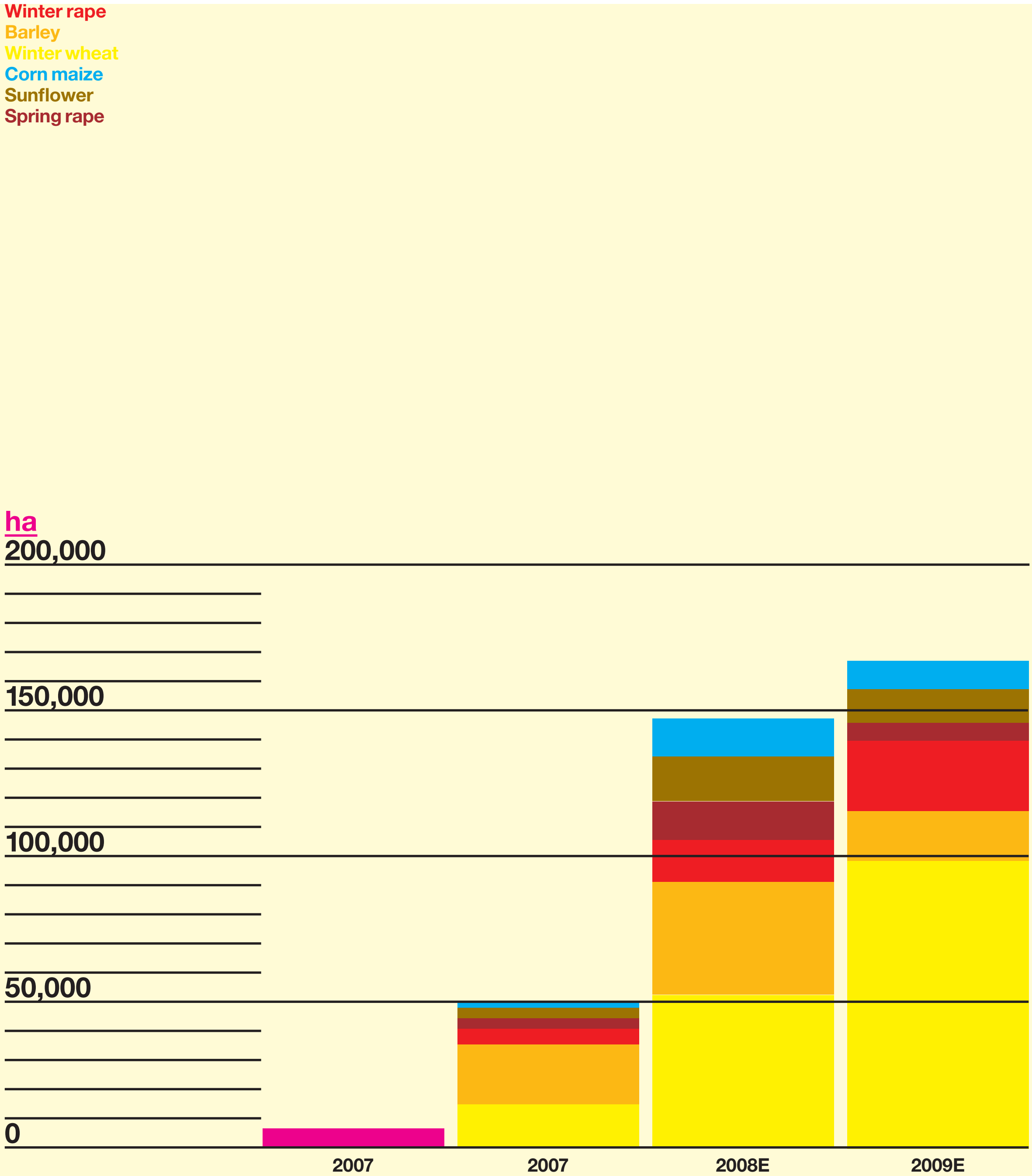


Price ranges for agricultural land, USD per hectare

Sources:
United States Department of Agriculture,
Land Values and Cash Rents 2006,
Federal Statistical Office Germany 2006,
Eurostat 2005 and Cresud 2006



Black Earth Farming harvested tonnes for selected crops



Black Earth Farming harvested hectares for selected crops

EU Biofuels Directive

As part of a wide-ranging policy to fight climate change, the European Commission proposed that the share of biofuels in transport would be raised from its current level of around 2% to 10% by 2020, with a view to reduce Europe's dependency on oil and contribute to the reduction in greenhouse gases emissions. Subsequently, this matter was approved in March 2007 when, at a meeting with the European Council the EU leaders commited to the above mentioned goals.

The previous EU Biofuels Directive set a 2010 voluntary target of 5.75% biofuels in the total transport fuel mix. The new 10% target is already a binding one, however under the condition that biofuel production is sustainable, perhaps as a result of the "second-generation" biofuels becoming commercially viable.

The conditionality of the new 2020 target is linked to mounting concerns that the proliferation of the available "first-generation" biofuels is putting too much upward pressure on food prices, as current technologies for biodiesel and bioethanol production use agricultural crops (such as corn, sugar beet, palm oil and rapeseed) and are doing this in a way that is not very efficient, utilizing only up to 15% of the biomass.

The EC suggested a tentative schedule of growth of the biofuel share in the transport fuel mix (see Figure Case Study I), but some member countries, like Germany and Austria, decided to adopt a more accelerated schedule. However, the ultimate target of a 10% biofuels' share is maintained even in those accelerated schedules, mainly because it is impossible to increase the bio-component in the fuel above 10% without the need to introduce modifications into the power train of automobiles.

The new targets set by EU clearly need a major investment into refining/distilling capacity, but the need to secure a biofuel feedstock is currently perceived as a real challenge.

It is also emerging that the EU countries will be focusing on their own production of biodiesel, while bioethanol will most likely be imported from Brazil, which currently has a clear competitive edge when it comes to production costs.

EU countries' fuel consumption

In order to better understand the future trends, it is well worth looking into the current patterns of fuel consumption in the EU countries (see Figure Case Study II). Currently, overall EU uses more diesel than petrol, mostly because of the widespread use of rail and heavy vehicles in cargo transportation. However there are clear exemptions to this pattern, including the UK and Greece (both island countries, with ecologic reasoning against developing denser road networks) and the Nordic countries (especially Sweden and Finland, where cold winter weather limit the use of diesel engines). Also, it is evident that the new EU members substantially lag the EU-15 countries in fuel use per capita.

The trend currently seen is that even more diesel would be used, if available. First of all, quality and ecologic attractiveness of diesel engines have improved, which has resulted in more diesel cars in private use, a trend with a potential to more than offset fuel-saving from the improved efficiency in rail and heavy commercial transports. With the new EU members expected to move gradually towards the EU-15 per capita consumption level, the only risk to a much bigger weight of diesel in the future fuel mix is that the expected lighter structure of the future oil supply (more gas condensate used) is likely to push middle distillate yields in refining further down – and thus reducing the diesel supply.

This clearly opens up additional future opportunities for EU biodiesel demand/consumption.

EU future diesel demand

We use the following two approaches to calculate diesel demand in 2020 (see Figure Case Study III).

In the first approach, we use the official EU growth figures for the diesel consumption until 2020 (1–2% pa for EU-15 and 3–5% pa for EU-25/15). The resulting estimates for the annual diesel consumption are 207–220 mmtnpa by 2010 and 235–278 mmtnpa by 2020.

In the second approach, we assume that the new EU members reach harmonization with the EU-15 fuel consumption levels and patterns by 2020, namely (quite conservatively, given the currently observable data in Figure Case Study II):

– 800 litres per annum per capita (lpapc), of which 70% is made up of diesel – for countries with warmer climates

– 950 lpapc, of which 50% diesel – for the Nordic countries.

With the further assumption that the population of EU

Case study: Prospects of European biodiesel

stays unchanged around the 2005 levels, the second approach yields a 2020 diesel demand figure of 274 mmtnpa, at the upper end of the range resulting from the first approach.

EU biodiesel production and forecast

We use the estimates of the future overall diesel demand and EU biofuel targets for 2010 and 2020 to make an estimate of the potential future biodiesel demand.

In 2007, EU biodiesel production reached 5 mmtnpa (see Figure Case Study IV). The industry currently faces the task of more than doubling biodiesel output by 2010 (to 12.0–12.6 mmtnpa), and then again double it by 2020 (to 23.5–27.8 mmtnpa).

Arable land in Europe

Various sources give different estimates of the overall arable land in Europe and the comparison of these figures is complicated by the differences in crops under consideration, as well as by the variation in the quality of the soil and plot parameters. The figures for the potentially available agro land are especially hard to estimate.

According to the Eurostat figures (see Figure Case Study V), the arable land bank of the EU currently stands at less than 90 mln ha. However, the EU subsidies policy complicates proper economic assessment of the available land, and the aforementioned estimate could in fact be overly optimistic.

As a result, the addition of arable land in Ukraine and Russia, both quite close geographically to the EU with a good (railway) communication with it, could be essential for supplying Europe with biodiesel, or with the feedstock for its production.

Agro needs for EU biodiesel production targets

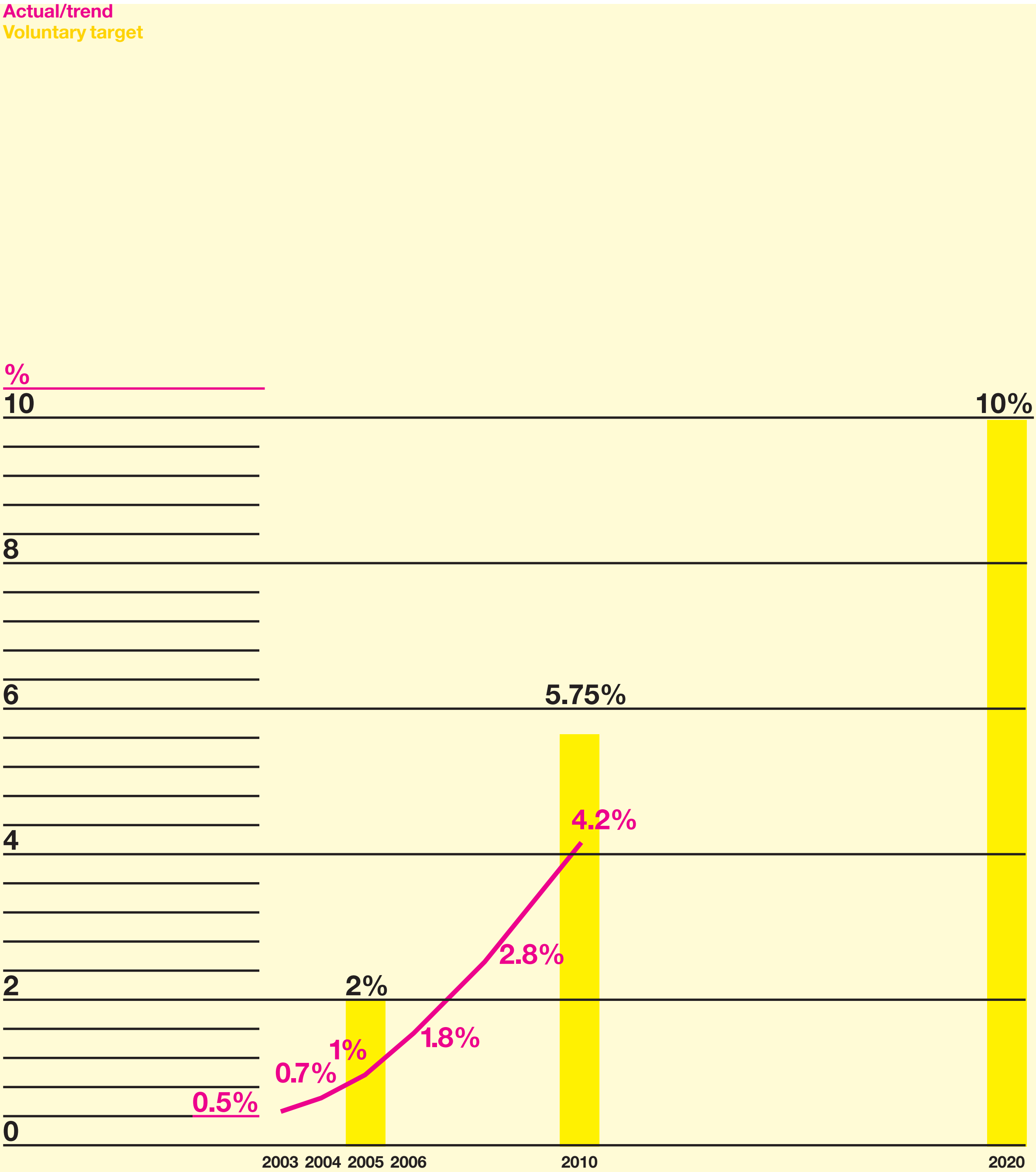
The choice of oil-bearing crops for biodiesel production in the EU is in fact limited (see Figure Case Study VI). Biodiesel made from palm and coconut oils has a tendency to lose liquidity at comparatively modest temperatures and is therefore unsuitable for European cold winters. Plants that are widely used in biodiesel production, such as jatropha and castor are not commonly cultivated in Europe. This leaves rapeseed as the major feedstock for production of European biodiesel, given the culture's relatively high oil yield and low relevance as a part of the food diet.

We use the average yield of biodiesel from rapeseed to calculate the land needed to achieve the EU biodiesel targets by 2010 and 2020. The result is as follows: Biodiesel needs could use up to 12% of EU arable land (10.3–10.8 mln ha) by 2010 and up to 26% (20.2–23.9 mln ha) by 2020. Again, we believe it would be impossible to find such amounts of spare land without incorporating Russia's/Ukraine's agricultural resources into the supply chain of the European biodiesel production.

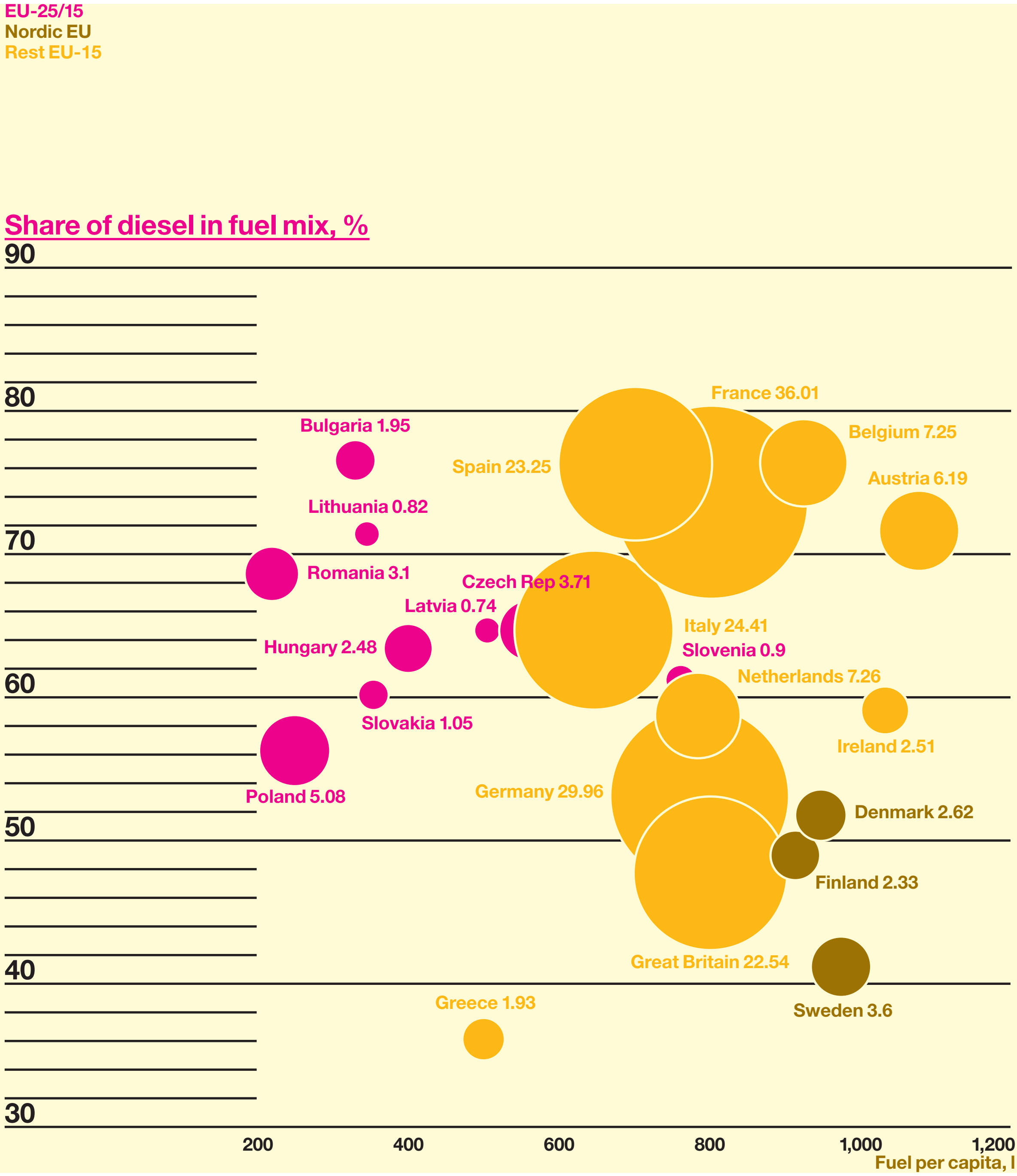
EU biodiesel economics

EU diesel prices were recently moving up very quickly, following the strength in the oil prices globally and the emerging deficit of diesel in Europe. On top of that, the analysis of country-to-country diesel prices (see Figure Case Study VII) explains the observable variation in prices for diesel in line with the country specific levels of taxation. So far, the attempts to harmonize taxation proved to be unsuccessful, but with the EU's current plans to set the minimum tax on diesel at €0.33/l, diesel prices could start at €1.20/l (based on USD 90–95/bbl oil).

Biodiesel is currently exempt from the mineral oil duty and other taxes levied on diesel and its production process has comparatively low energy needs, mainly for transportation and/or oil pressing. This allows for a margin of up to 50–60% from the selling price of biodiesel to go into the feedstock. With the oil content of rapeseed averaging 40% and an oil/biodiesel conversion ratio yielding 90%, USD 375–425/tn could be perceived as a conservative long-term floor level for rapeseed prices. Certainly, further disbalances in supply/ demand of diesel overall, or of biodiesel specifically, could mean that this estimate has substantial risks on the upside.

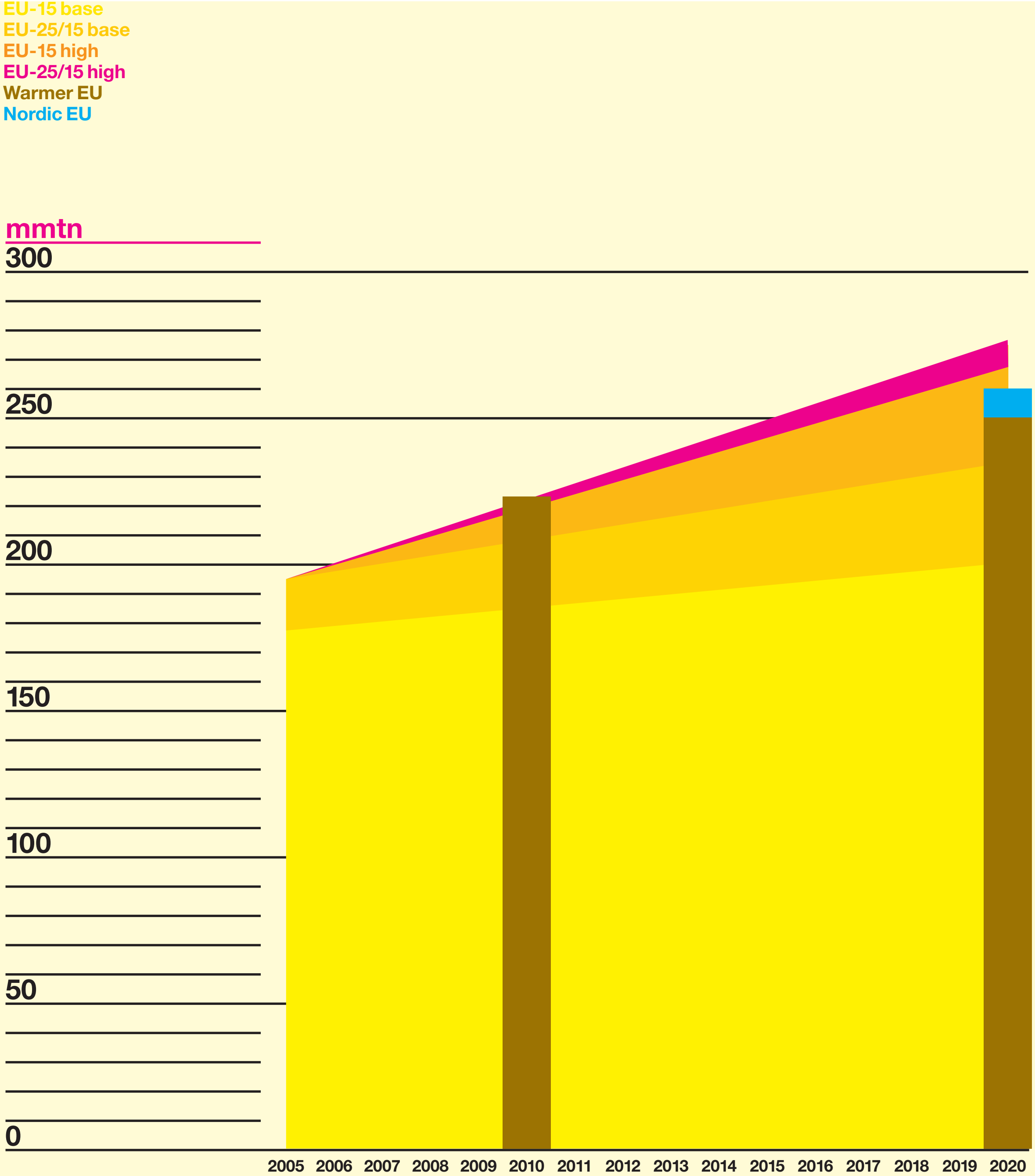


Case Study I: EU countries' share of biofuels in total transport fuel mix, 2003–2020E

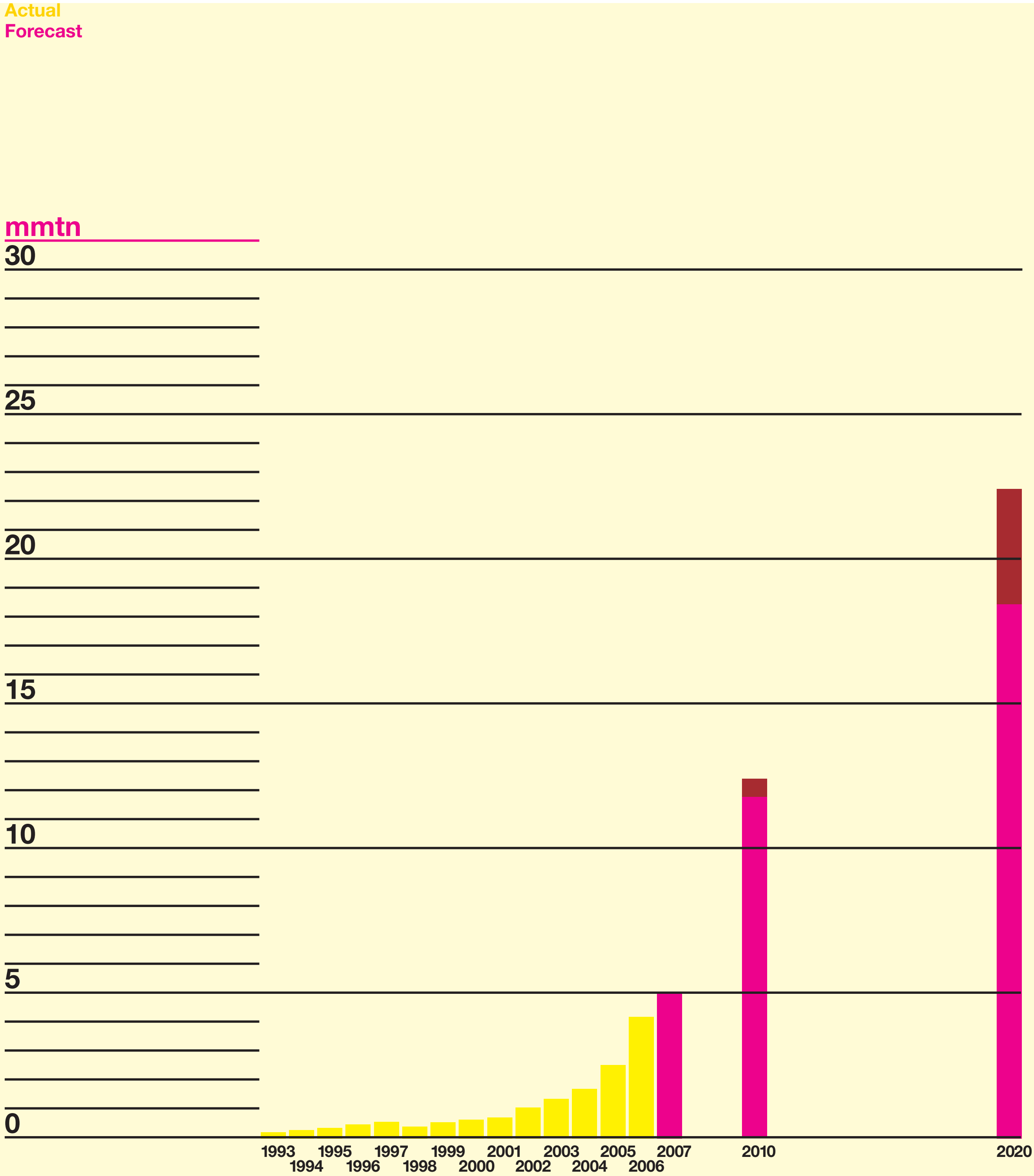


Case Study II: EU countries' transport fuel consumption patterns, 2006

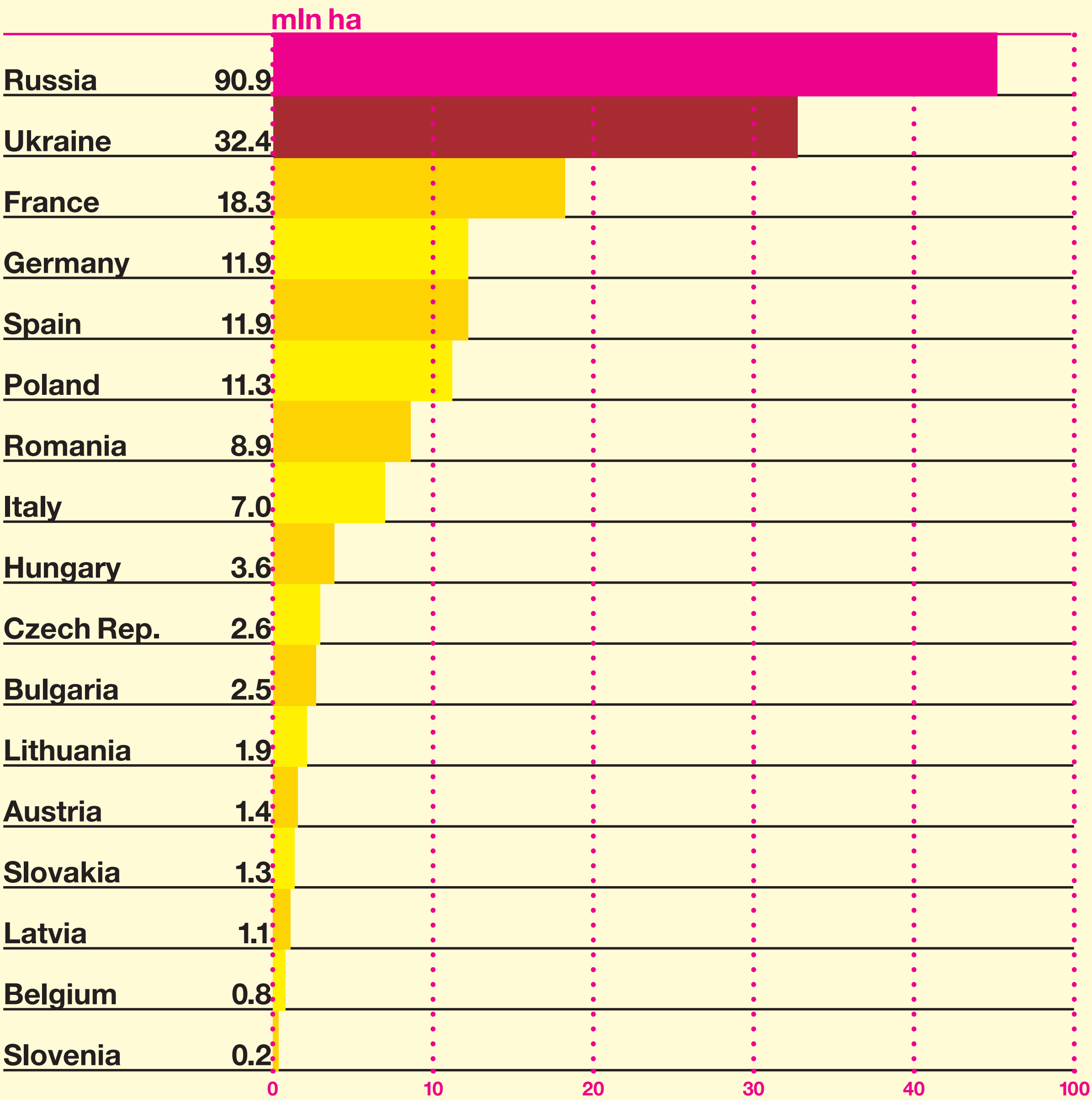
Note:
The size of the bubble and the label represent amount of diesel consumed in the country per annum, in mmtns.



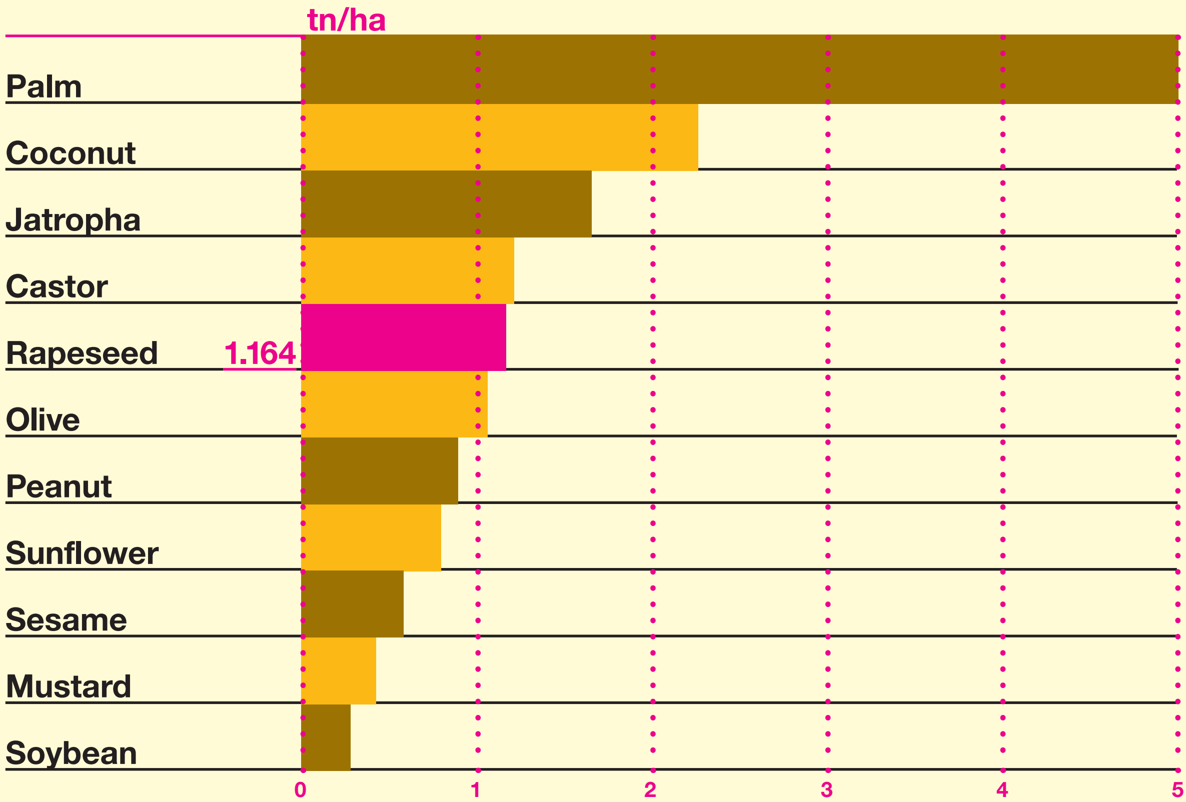
Case Study III: EU future diesel demand, 2005–2020E



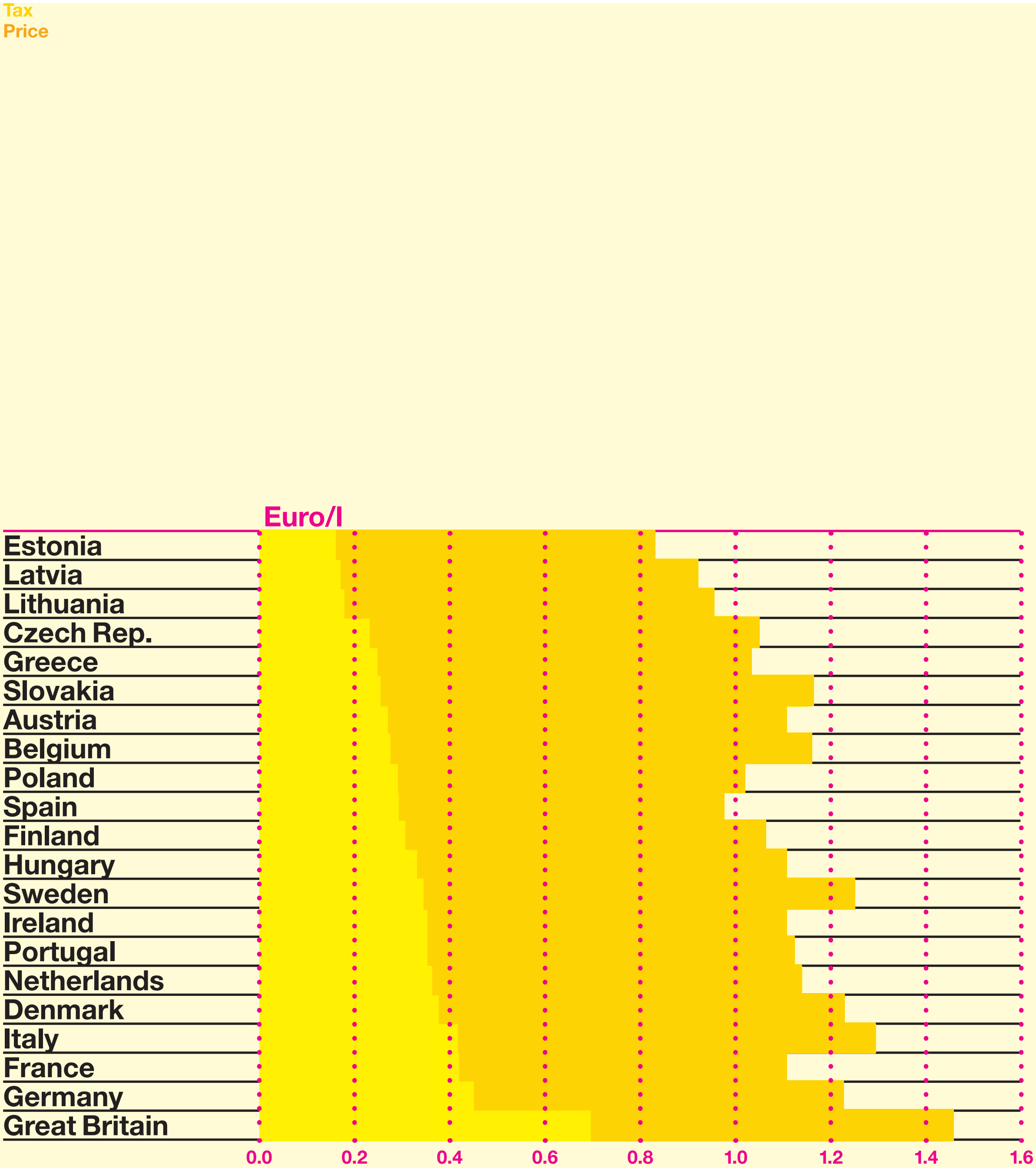
Case Study IV: EU biodiesel production and forecast, 1993–2020E



Case Study V: Arable land in Europe, 2006



Case Study VI: Oil yields for different crops



Case Study VII: European prices and taxes on diesel, 2007

TNK-BP Holding is one of the five Russian oil majors, boasting a reserve base of around 10 bln barrels of 1P reserves under SPE classification, but with a large upside with 3P reserves at over 30 bln boe. Its liquids production stands at 1,550 kbpd. The production is undertaken at some of Russia's oldest fields. The largest one, the huge Samotlor field (the third largest in the world) has a water-cut above 90%. However, the company arguably has the best management team in Russia, having pooled personnel from TNK's Russian operations as well as BP's global base. This is clear in the company's lifting cost, which stands at USD 2.46 per bbl (despite an older asset base) compared to Lukoil's at USD 2.45 per bbl and Rosneft's at USD 2.48 per bbl. TNK-BP's output growth has disappointed lately following asset disposals, however, we expect solid organic growth ahead. TNK-BP holds the reserves and has the management capability to restore growth.

TNK-BP also has downstream activities aimed at generating the highest netbacks for the company. The company owns and operates five refineries, four in Russia and one in Ukraine, with a combined refining capacity of 640,000 bbl per day and the company's retail network which extends across central Russia and Ukraine covers approximately 2,320 petrol stations, of which around 1,600 are under the company's own brand name.

TNK-BP has recently completed the consolidation of the Ryazan refinery after long-lasting negotiations with the minorities of the refining company, and has also been given a green light from the Federal Antimonopoly Service (FAS) to purchase companies operating retail stations in the Moscow and St Petersburg areas. Most of the stations have already been operated under the TNK brand, but the company is aiming at minimizing the number of franchises in order to obtain higher margins by direct ownership, and by increasing its share of the attractive Moscow petrol market.

Alfa Access Renova group (AAR), BP's Russian partner, was subject to a lock-up initiated at the time when they sold down to BP. This lock-up has now been lifted and there have been numerous rumours of whom they might sell their stake to, with Gazprom and Rosneft being the most likely buyers. However, AAR in February issued a joint statement saying that they will remain long-term investors in TNK-BP.

TNK-BP's revenues are estimated, through BP's financial statements 2007, to have grown around 8.9% during 2007 and net income estimates are up almost 21% from 2006 (if 2006 figures are adjusted for the sale of Udmurtneft). Additionally, the company has stated that it plans to increase the oil output in the Orenburg field by 1% in 2008. In 2009–2010, TNK-BP also aims to put several new blocks into operation to secure production rates from Orenburg, which is one of the oldest fields in Russia. The developments in the Orenburg field will not have any significant effects on the Company's total output, which is planned to grow by 33% between 2007 and 2012. TNK-BP's main production increases will instead come from new oil fields, such as Verkhnechonskoe, Russkoe and Uvatskoe.

Outlook for group structure and market participation

The group is now fully consolidated, except for the large Kovykta field (where the group's stake is likely to be sold down to include Gazprom as a partner) and the Slavneft asset (where Gazpromneft is the partner on a 50/50 basis). It is likely that the non-consolidated assets will be folded into the holding company at some point, and even though this won't be for free it should still provide a value creative measure. Currently the holding company has a market capitalisation of around USD 26 bln – and a free float of roughly 5% of the outstanding shares worth around USD 1.35 bln. Minority shareholders in the holding company have primarily been attracted by the high dividend yield of some 12–13%. The sustainability of the dividends is strengthened by the company's transparent dividend policy and gearing target. BP also achieves its financial flows out of the company through the same dividend streams.

In the latest developments around TNK-BP, the Russian authorities in mid-March raided the Moscow offices of BP and TNK-BP. Officials accused a TNK-BP employee of industrial espionage and opened an investigation into tax evasion and possible environmental violations at the company. Most observers see these events as a push from the Russian government to step up the pressure on AAR to sell out to one of the major Russian players. However, TNK-BP's CEO Robert Dudley has stated that the raids and the arrest were one-off incidents, not a broad attack on the company that might lead to a full-blown expropriation by the government.

TNK-BP

Kontakt East Holding AB (KEH) is a Swedish holding company which invests in companies active within search and guidance media in Russia and associated markets. KEH currently has investments in the business segments Directory Services and Consumer eCommerce. Directory Services offers its customers both online and offline directories and is operated through a number of subsidiaries, which together give KEH a leading market position in Russia. Directory Services publishes directories in Moscow, St. Petersburg and eight other Russian districts. Online services are also provided through the web site www.yellowpages.ru, as well as by voice services.

On August 14, 2007, KEH acquired YPI Yellow Pages Limited ("Yell.ru") which had a leading market position within search and guidance media in and around the St. Petersburg and Perm regions of Russia. Yell.ru offered, in likeness with KEH, both online and offline directories within the areas where the company was active. The acquisition therefore further strengthened KEH's position as the market leader in Russia. The integration process, which is in its final stages, should result in considerable synergy effects visible in KEH's future financial results.

During 2007 the order intake for the Directory Services business segment increased by 41% to MSEK 121.3, with the largest growth originating from offline products. Directory Services' total revenues increased by 67% during the year and the organic revenue-growth, adjusted for the acquisition of Yell.ru, was 12%. In 2007, the full year EBITA-loss for Directory Services amounted to MSEK –9.1. However, in 2008, Yell.ru will be fully integrated into KEH and the EBITA-margin for Directory Services is therefore expected to exceed 10% this year and 20% in 2009.

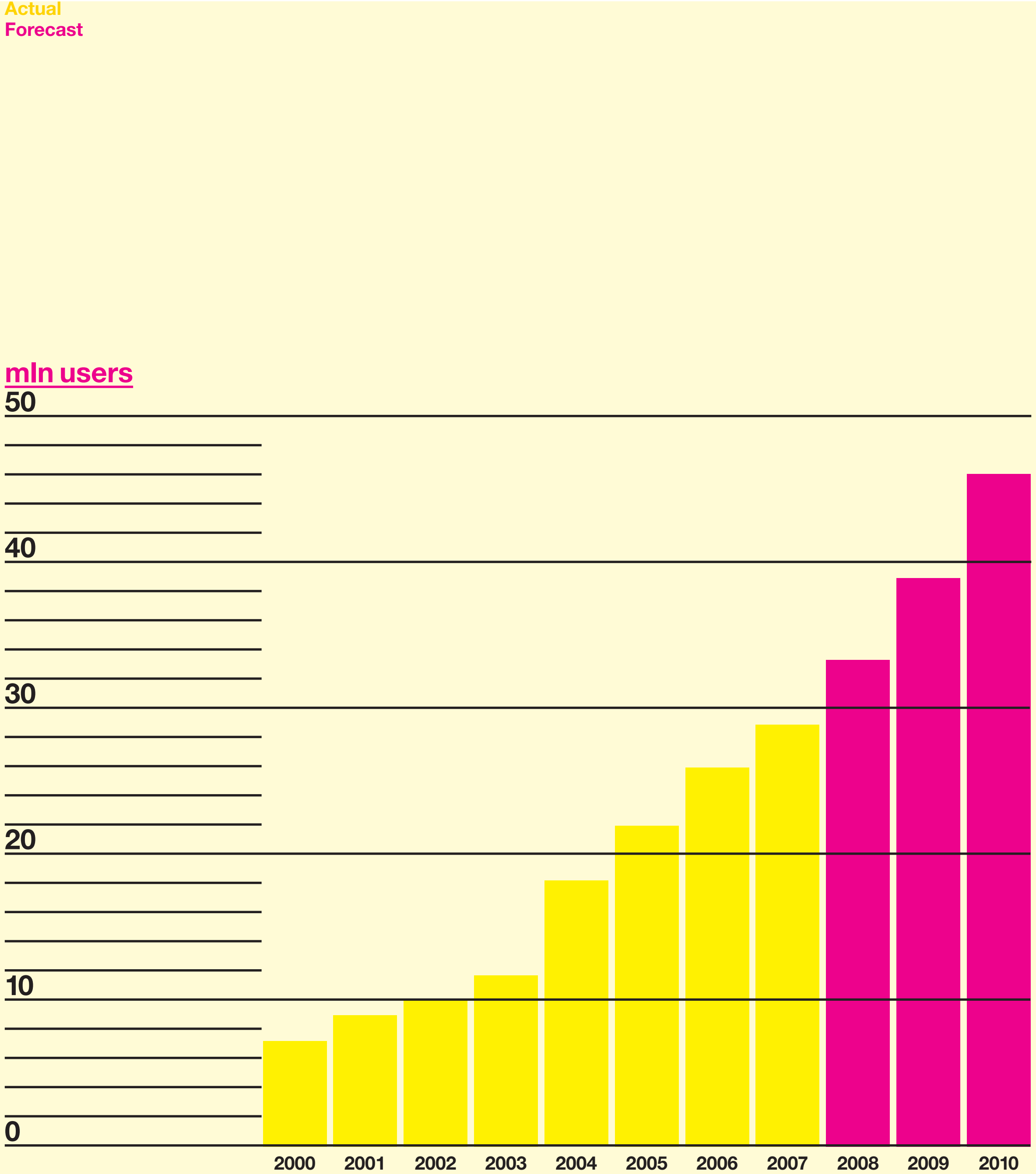
In October, 2007, KEH launched its first consumer e-commerce offering through the subsidiary KEH eCommerce and the website Avito.ru. The site provides an easy and accessible platform for companies and consumers who, through classifieds, wish to buy and sell goods and services over the Internet. In November, KEH announced that it had signed a long term agreement with SUP, a leading Russian online media company. The agreement involved Avito.ru becoming an integrated part of one of Russia's top 10 internet sites, Livejournal. Avito.ru had beforehand established itself as Russia's fastest growing online market place, and through the agreement the site has gained significant additional exposure in terms of users and traffic. Avito.ru currently offers over 80,000 objects for sale and has more than 30,000 registered users.

No operational revenues were generated by Consumer eCommerce during 2007. Initially no fees will be charged for listing items, or holding auctions, on Avito.ru. Revenues will instead be generated by advertisements and fees applicable to extra services provided by the site. Consumer eCommerce has now, as of February 2008, started seeing its first revenues through advertisements on the site.

In late 2007, KEH carried out a fully subscribed new share issue, providing the company with approximately SEK 102 million before issue expenses. KEH has been the leading player within guidance media services in Russia for quite some time, and intends to continue to take a leading role in the consolidation of the market during 2008. In order to do this, further acquisitions of companies operating in major Russian cities may be of interest, and KEH has already announced the acquisition of Publishing House Dialog LLC (Dialog) in Chelyabinsk. Dialog is to be integrated into Directory Services and will strengthen KEH's presence in the southern Urals region of Russia. Additionally, KEH is planning to launch at least one more platform within the Consumer eCommerce business segment during 2008.

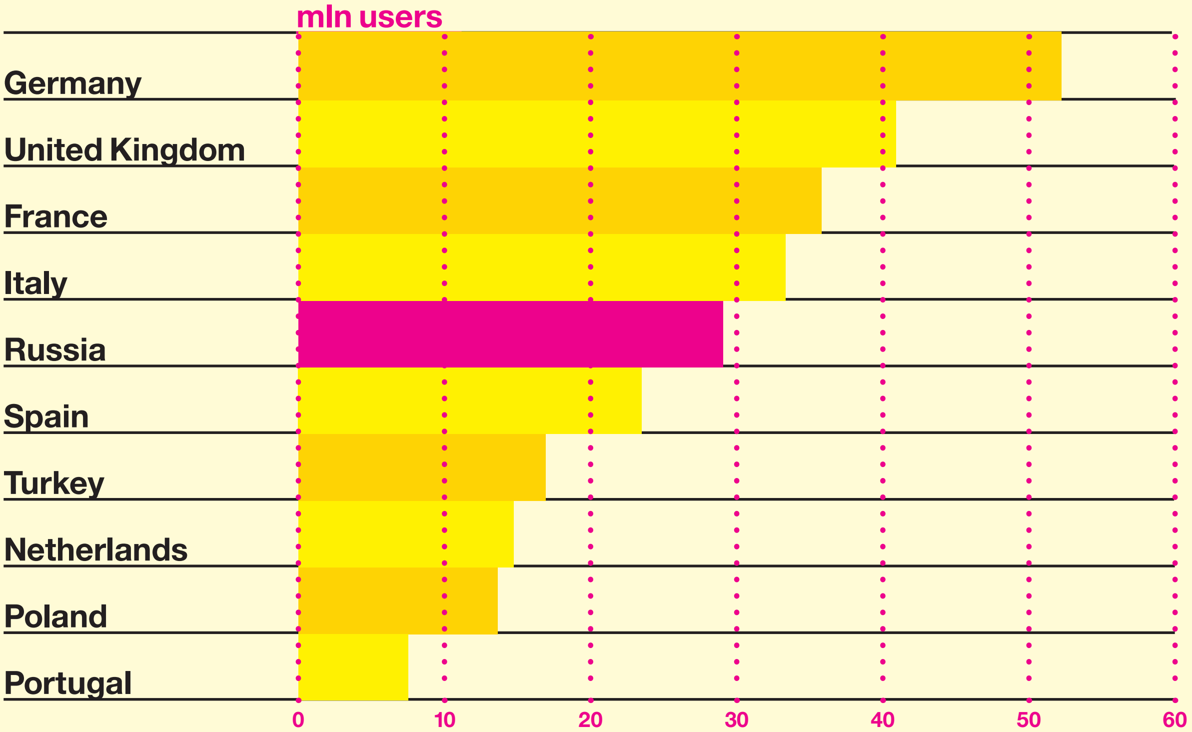
Vostok Nafta sees great potential in both KEH's existing operations and the Russian search and guidance media market in general. A new share issue was a natural step for the Company to facilitate its future growth and to enable investments in further product development and marketing. Therefore Vostok Nafta, as one of two major shareholders, was positive to the new share issue and chose to exercise all subscription rights received.

Kontakt East Holding



Internet in Russia. Russian online users, 2000–2010E

Source:
Russian National Association
of Advertising Agencies



Top ten Internet countries in Europe, December, 2007

Source:
Internet World Stats, March 2008
(www.internetworldstats.com)

Coal

Coal prices, both thermal and coking, are booming, in dissonance with the recurring fears of a US recession and its potential effect on global commodities prices. The reasons for this are several, with short-term issues stacking on top of long-term structural changes:

– on the demand side, continuing economic growth in China and India (together with other Asian countries accounting for more than half of global coal consumption) resulted in pressure on global suppliers of coal, especially after China became a net coal importer in early 2007

– this caused substantial infrastructure bottlenecks in Australian and Indonesian (now the biggest exporter of thermal coal) ports, thus exacerbating the supply side long-term structural problems

– on top of this, several developments in early 2008 put even more short- to medium-term pressure on the coal supply, including:

  – In China, snowstorms limited the ability of power plants to source thermal coal as transportation halted and this resulted in China halting all export activities until April

  – In Australia, heavy rains have flooded coal pits in Queensland, forcing the world's largest exporters of coking coal to declare force majeure

  – In South Africa, also a major exporter of thermal coal, power shortages have forced the temporary closure of coal mines

As a result, spot settlements in 2008 started with prices for hard coking coal of USD 210/tn, with the most recent transactions reaching the levels of USD 275/tn. With 40% of the world's electricity and most of its steel and cement production depending on burning coal, thermal coal prices have risen to as much as USD 130/tn. The analysts are currently upgrading their outlook for thermal coal prices by lifting their annual average forecasts to the USD 125/tn levels. Russia, the world's third-largest coal exporter, is unlikely to boost production to make up for the global shortfalls. However, a widened shortage in China, the major export market for Russian coal producers, is creating a profitable export opportunity for them and putting upward pressure on domestic coal prices too. This means, for example, that the commencement of operations at the Listvyazhnaya preparation plant, allowing Belon to upgrade its thermal coal concentrate to the exportable grade, had an extremely good timing. In any case, Russia's coal production (both thermal and coking) is continuing to grow (see Figure Coal I). We expect this growth to continue, alongside further enhancement of economics in the Russian coal sector.

Belon

Meanwhile, the major recent news about Belon were not the usual reports of growth in output volumes, but of the company getting into a vertical integration with the major Russian steel producer, Magnitogorsk Metallurgical Company (MMK). After the initial acquisition of 10.75% (for USD 60 mln, in Oct 2007), MMK in March 2008 announced the acquisition of a 50% stake in the company, controlling 82.6% of Belon, paying USD 230.4 mln (USD 66/share, compared to the current price of USD 132/share), thus becoming the indirect owner of a 41.3% stake in the company. The new partners will jointly inject USD 500 mln to get a 70% increase in production of coking coal concentrate by 2012.

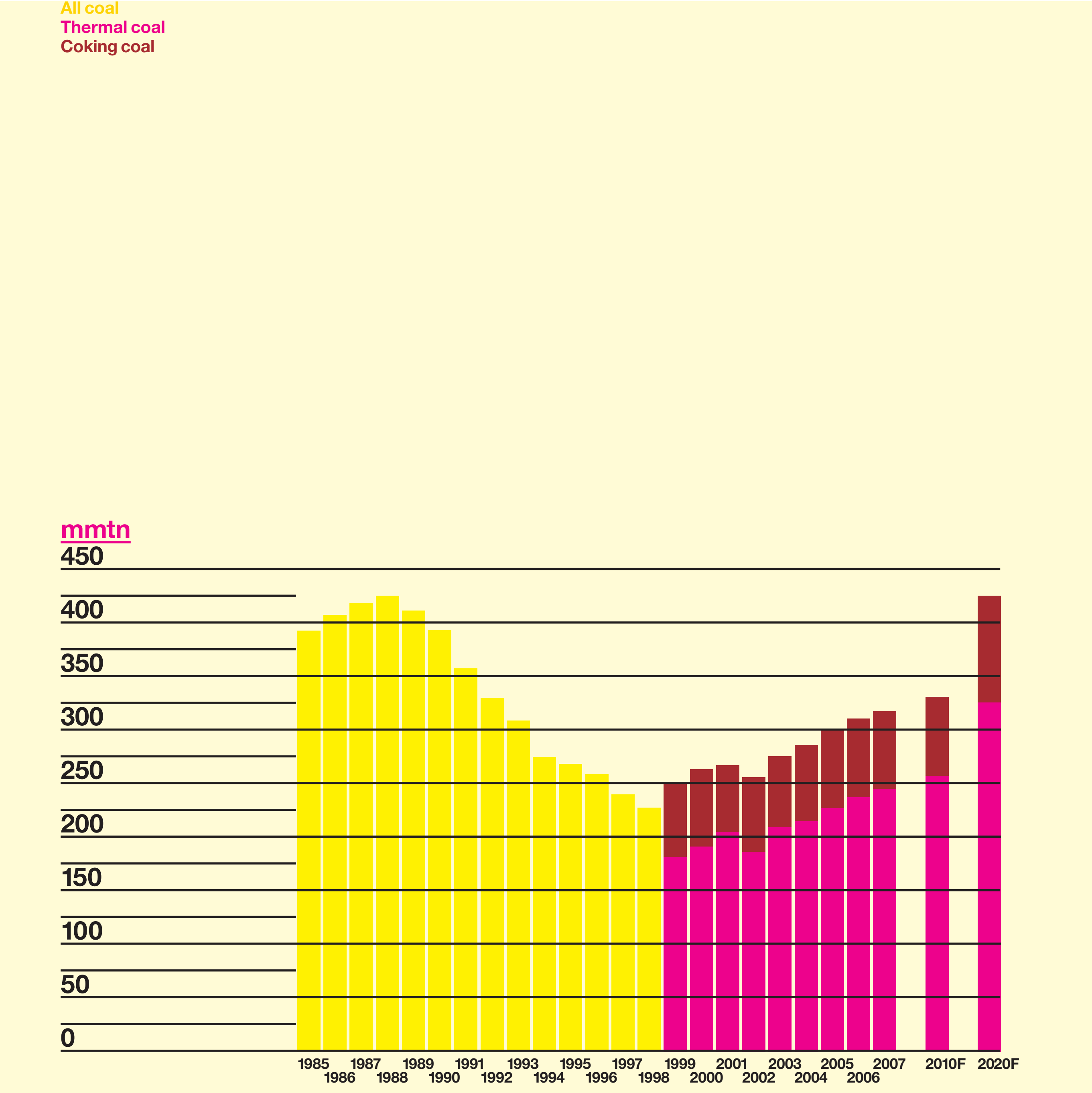
The MoU setting out the key terms and conditions of the transaction was signed in July 2007, hence the relatively low price of the transaction compared to the market. However, the benefits of the joint investment will be apparent to the shareholders of both MMK and Belon. In 2007, Belon produced 2 mln tonnes of coking coal and 2.65 mln ton tonnes s of steaming coal, while in 2008 it expects to produce 3.67 mln tonnes of coking coal and 3.5 mln tonnes of steaming coal. In 2008 Belon will increase shipments of coking coal concentrate to MMK to 2 mln tonnes and to 3.9 mln tonnes in 2009 – at market prices (USD 150/t). By 2012, Belon plans to produce 5.1 mln tonnes of coking coal and 5 mln tonnes of steaming coal, while MMK will require 6 mln tonnes of coking coal.

Kuzbassrazrezugol

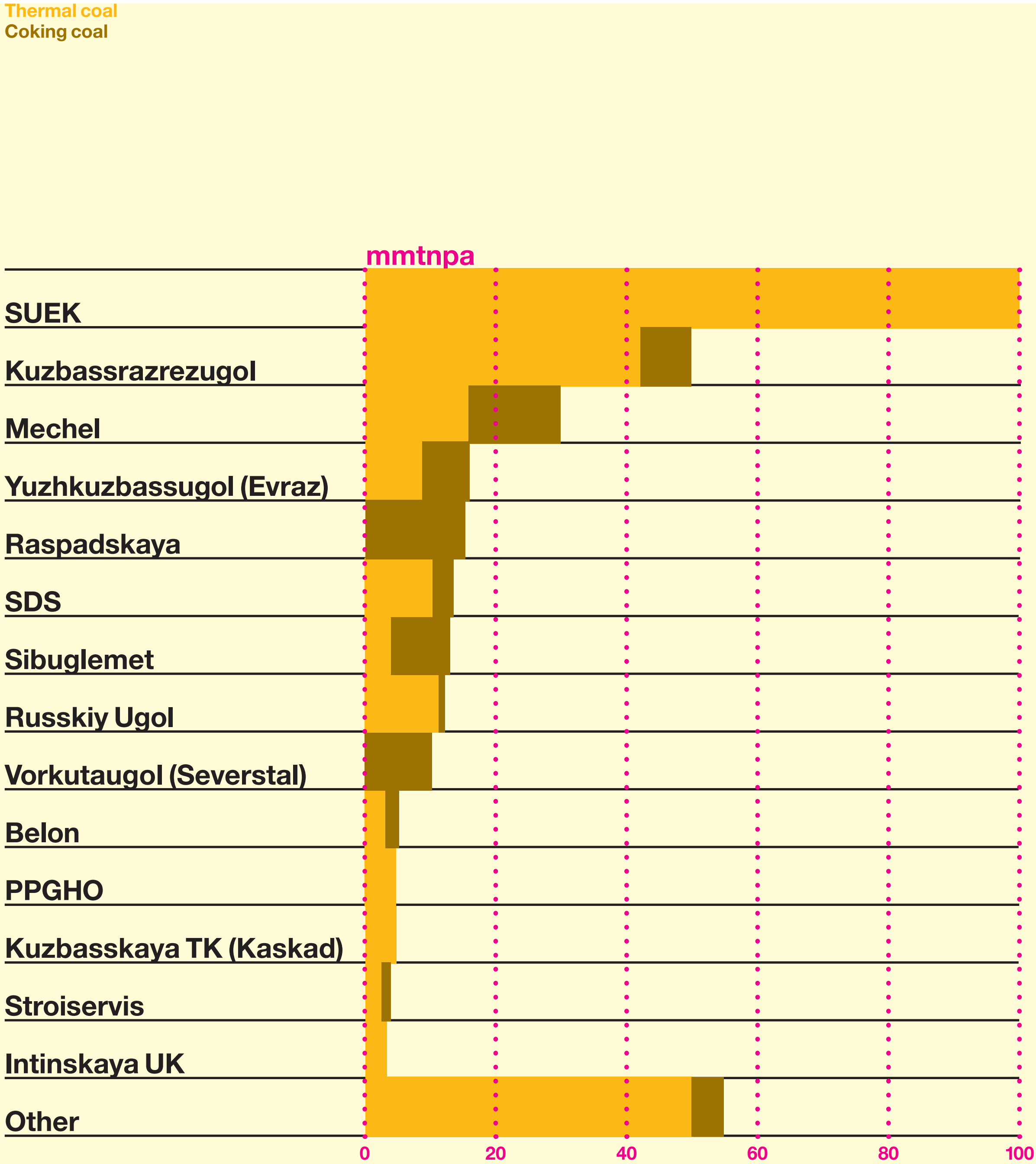
Kuzbassrazrezugol (KZRU), the second largest Russian coal producer (mainly thermal coal, see Figure Coal II), is currently undergoing substantial changes. With the open-pit coal production, the company should be by far the most efficient entity within the Russian coal producers' universe. However, in the last years the company was selling all its production via the trading company KRU Trade, as a result of which its profitability came out less than mouth-

Other holdings

Other holdings



Coal I: Dynamics of coal production in Russia, 1985–2020F



Coal II: Russia's largest coal producers, 2007

Sources:
Rosinformugol,
Company data

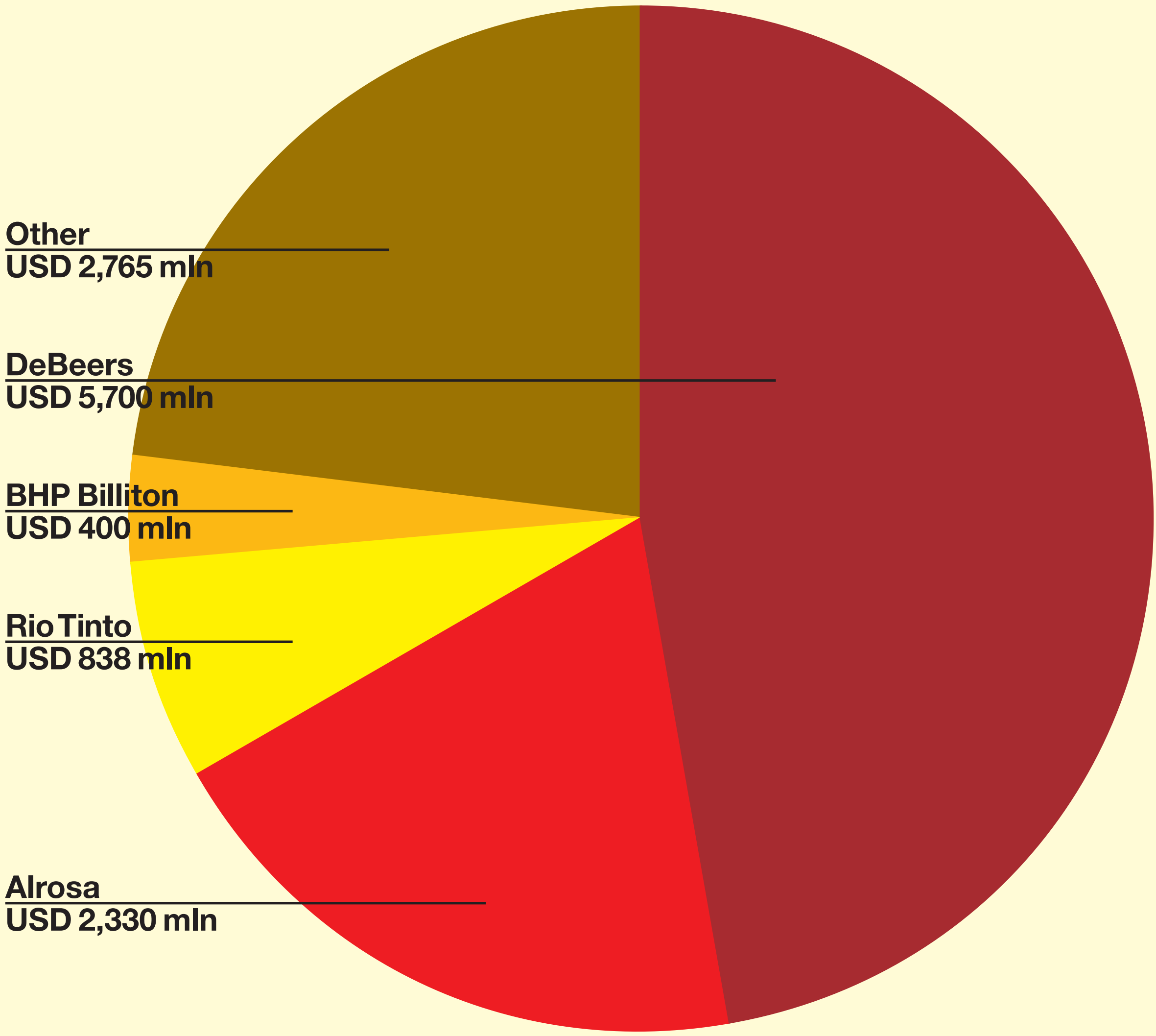
watering to the potential investors. However, we do see matters slowly (but inevitably) starting to change. In the fading days of 2007, KZRU's board approved a decision to issue 4,964,000,391 ordinary shares to convert for the shares of the two holding companies, Kuzbasstrans and Riostail, which previously owned all the machinery of the coal company (276 shovels, 492 heavy trucks, 75 drill rigs, 217 dozers, etc.) In the result of the folding of the two KZRU's holders into the company itself, KZRU started to hold the same amount (4,964,000,391) of its own treasury shares, which were cancelled after the merger had been consummated. Besides the two holders of KZRU shares, several subsidiaries had also been folded into KZRU, which added two more coal pits under direct ownership of the company. As the same amount of shares that had been issued in the early stages has been cancelled at the end of the process, minority holders had preserved their share of ownership in the company, however now with bigger assets.
The completed corporate restructuring helps KZRU to proceed with the plans to raise total coal production to the level of 60 mmtn by 2012 (with 49 mmtn expected to be produced in 2008).

Ural Mining and Metallurgical Company
The Ural Mining and Metallurgical Company (UGMK) is a diversified industrial company controlling enterprises active within mining, metallurgy, refining complexes, machine-building, cable and conductor production as well as within the construction industry. UGMK's products are mainly based around copper and non-ferrous metals.
We are currently invested into two companies controlled by UGMK; Gaisky GOK and Uchalinsky GOK. A trigger for these companies is a potential consolidation of the group companies into UGMK Holding, in likeness with what happened to many other Russian groups in the past. A consolidation would provide investors with the opportunity to increase the value of their holding through the subsequent swap-agreements and the market revaluation of a consolidated entity.

Gaisky GOK
Gaisky GOK is Russia's second largest copper concentrate producer, with a market share of almost 11%, located in the Orenburg region of the Urals. The company is controlled by UGMK Holding (84.5% share ownership) and is a key supplier to its copper producing subsidiaries. Gaisky GOK in turn controls more than three quarters of the ore reserves in the Orenburg region, and the company's total ore reserves are estimated to be around 310 million tonnes, with a reserve life of over fifty years, given current production levels. The reserves have average copper and gold grades of 1.4% and 0.3 g/t, respectively. The ore mined by Gaisky GOK also contains other metals which can be extracted, including zinc, lead and silver. In 2006 the company produced 73,650 tonnes of copper concentrate, its main product. On top of this, Gaisky GOK also produced 9,000 tonnes of zinc concentrate and 50,000 troy ounces of gold in concentrate. Gaisky GOK will increase its production continuously through development of existing deposits, as well as through license acquisitions and new developments. Gaisky GOK plans to develop new open-pit and underground deposits, which should increase the company's production of copper-zinc ore from 5.2 million tonnes in 2003 to 8 million tonnes in 2009.

Uchalinsky GOK
Uchalinsky GOK is the largest zinc mining company in Russia, and the third largest in terms of mined copper ore. The company is controlled by UGMK holding (88.5% share ownership) and functions as a key supplier of zinc and copper concentrates to UGMK's smelting subsidiaries. However, a significant part of the company's production is also supplied to independent smelting companies in Russia. Uchalinsky GOK's ore reserves amount to 110 million tonnes, with zinc and copper grades of 3.0% and 1.15% respectively. Uchalinsky GOK owns its own concentrators and can therefore process its ore into concentrate internally. During 2006 the company produced 118,900 tonnes of zinc in concentrate and 49,530 tonnes of copper in concentrate.

Alrosa
We have during the fourth quarter of 2007 invested into the world's second largest rough diamond producer, Alrosa. The company, which is located in Yakutia, accounts for 97% of Russia's total diamond production, and approximately 25% of global rough diamond production. Alrosa operates alluvial, open



Global production of raw diamonds, 2006

Sources:
Alrosa, Kimberley Process Rough
Diamond Statistics,
IFC Metropol estimates

pit and underground mines with an estimated explored reserve life of 25 years, and seven primary ore treatment production plants with an estimated throughput capacity of 30 million tonnes per year. In 2006 Alrosa produced diamonds for a total value of USD 2,332.2 million and manufactured polished diamonds for USD 141.1 million. Rough diamonds are primarily sold to the jewellery industry, but are also used for the production of industrial abrasives (non-gem diamonds). The company itself cuts and polishes a small share of its production at the subsidiary Brillianty Alrosa. Beside its Russian operations, Alrosa also has a large interest in a diamond production company in Angola.

Alrosa has a CAPEX-plan stated at USD 2.5 billion for its mining operations, and the company's production volumes in Yakutia should remain relatively flat going forward. This is due to the fact that when Alrosa's new underground mining facilities come into operation, open-pit mine production will decrease in the area. However, the company's overall diamond production is expected to rise during the next decade, in large thanks to production increases at the Arkhangelsk division and in Africa.

The short term trigger for the stock will likely be the restructuring of the company. Alrosa currently has the form of a closed joint-stock company, and the largest shareholders are the Russian Federation and the Republic of Sakha (Yakutia). However, the legal form of the company should change to an open joint-stock company by May 2008, and plans have been announced for an IPO in London, Hong Kong or Toronto during 2009, in which the Russian Federation would keep a controlling stake with 50% +1 share. There is also a possibility that the Russian Federation will increase its stake in the company, reducing the share held by the Yakutian government. This could have significant positive effects on Alrosa's profitability, thanks to potential reductions in the yearly royalties paid by the company to the Yakutian government. A longer term revaluation trigger, apart from being an undervalued global diamond producer, is Alrosa's possible role as a consolidator of parts of the Russian mining industry. There have been rumours of everything from Norilsk Nickel to Polyus Gold being acquired by Alrosa. However, such a consolidation is unlikely to happen at the current low market capitalization of USD 6 bln.

Russian cement industry

The Russian cement industry is currently witnessing continually growing demand, and supply levels which can barely keep up. The demand for Russian cement is driven by factors such as the growth in residential and commercial construction, the refurbishment of Russian infrastructure and continued development of hydro power plants and gencos. Simultaneously, import opportunities are relatively limited and the domestic capacity is straining to meet the higher demand. Increasing price levels therefore give cement companies in Russia the opportunity to grow their businesses along with their profits.

Sibirskiy Cement

Sibirskiy Cement is a Russian producer of cement and cement based construction materials. The company owns and manages five separate cement plants, all located in the Siberian Federal District. Sibirskiy Cement is the second largest cement-producer in the country and by far the largest in Siberia. The company has an installed capacity of 6.2 mln tonnes and produced 4.4 mln tonnes in 2006, which can be compared to a production of 2.7 mln tonnes in 2004. Sibirskiy Cement's market share has risen, along with its production, from 4.3% in 2003 to 7.3% in 2006. The company aims at becoming Russia's largest cement producer by constructing additional capacity and investing into equipment modernisation, while at the same time increasing profits.

Sibirskiy Cement also owns a transportation company with over 1,000 cement railcars at its disposal and controls key suppliers of raw materials (limestone, clay and marble). This provides the company with superior control of its cement production and greater flexibility regarding sales and transportation of its finished products.

Gornozavodsk Cement

Gornozavodsk Cement is a medium-sized independent cement producer located in the Perm region of the Urals. The company has two main sources of income, namely Portland Cement used for construction and Oil Well Cement delivered to the Oil and Gas Industry. The location of the company is favorable due to the fact that there is a high demand for cement in the Perm region, and 42% of Gornozavodsk's output was sold there in 2006. Other key regions for the company

Alrosa revenue forecast

	2006	2007E	2008E	2009E	2010E	2011 E	2012 E	2013E	2014E	2015E
Ore output, mn tonnes	31.3	26.2	26.2	26.6	27.0	27.9	28.7	30.2	31.7	31.7
Ore output growth, % y-o-y	n/a	–16%	0%	1%	2%	3%	3%	5%	5%	0%
Revenues, USD mn	3,468	3,643	3,875	4,085	4,285	4,471	4,654	4,849	5,054	5,272
Revenues growth, % y-o-y	n/a	5%	6%	5%	5%	4%	4%	4%	4%	4%
Price for ore, USD per tonne	111	139	148	154	159	160	162	161	159	166
Price growth, % y-o-y	n/a	25%	6%	4%	3%	1%	1%	–1%	–1%	4%

Source: IFC Metropol estimates.

are Sverdlovsk, Udmurtia and Kirovsk which combined received another 42% of the output the same year.
Gornozavodsk has, without large investments, shown strong increases in production recently. This is a trend which will most likely continue, thanks to high production demand and the company's relatively low utilization levels. Gornozavodsk Cement has a total capacity of 2.2 million tonnes per year, and at present 0.5 tonnes of depreciated capacity. Low utilization levels, and the potential of restored capacity, provide the company an opportunity to increase its sales in the Urals and expand its geographical market within Russia. For instance the new development projects for the Oil and Gas sector in Western Siberia will most probably acquire cement from the company.

Tuimazy Concrete Mixers
Tuimazy (TUZA) is the largest producer of concrete mixers and pumps in Russia, accounting for 40% of the market for mixers and nearly 100% of domestically produced concrete pumps. The company is in the process of launching production of auto cranes with the help of the German company Liebherr. Due to capacity constraints at its main competitor – TUZA expects to reach a market share of 50% in 2009.
Construction volumes in Russia are up 25% this year, and double digit growth rates are expected to continue over the next five years. In addition to overall growth there is also a big structural change in the construction sector that requires much bigger use of concrete mixers and pumps – the country is transforming from the old technology of building houses from concrete panels to the new "monolith" technology, where concrete is pumped into the walls on the construction site.
The company has had an historic production compound annual growth rate (CAGR) of 40%+ over the last five years. The management conservatively estimates a production CAGR of 20–25% for the next three years. Moreover, the company is increasing the share of high-margin large capacity mixers and pumps, which leads to further growth of revenues per unit.
TUZA is controlled by KAMAZ, which holds 51% of the shares. KAMAZ views TUZA as a non-core business and does not practice transfer pricing and respects the rights of other shareholders – the government of Bashkiria and financial investors. The free float is nearly 40% and there is an independent director on the board. KAMAZ has the most competitive platform in Russia for car-based mixers, pumps and cranes which has further boosted the competitiveness of TUZA's products. KAMAZ has a country-wide network of distribution and service centres through which TUZA's products are sold and serviced, and there is simply no competitor that can match it. Finally, KAMAZ has a very good and modern management team, which is influencing TUZA's management in a positive way.
During 2007, we have acquired roughly 15% of the outstanding shares with the investment rationale as an attractive way to get exposure to the high growth in Russia's construction sector.

RusHydro
During the third quarter of 2007 we invested into a series of Russian hydro power plants – Dagestan Genco, Volshkaya GES, Zeiskaya GES and Sayano Sushenskaya GES. These companies were, along with 17 other hydros, consolidated into RusHydro through swap agreements during the first quarter of 2008, and the company's shares have been listed on the RTS and MICEX. RusHydro has since gained the largest capitalisation of the companies within the Russian power sector – at around USD 15 bln. In terms of generating capacity RusHydro is, with its 23,700 MW, the largest genco in Russia and the second largest hydro company in the world after Quebec Hydro. The company's free float is currently 21%, but should increase to around 40% following the spin-off from RAO UES this summer.
With a conservatively estimated EBITDA of around USD 3 bln in 2010, the valuation has room to improve. We believe the successful consolidation into a liquid large cap like RusHydro, and the listing of the company's shares on MICEX and the RTS, will serve as a clear trigger for a first step towards full valuation.
The company plans to increase its capacity by 16% through to 2011, and in the long term aims to double its current production levels. Regulators have subsequently allowed a tariff growth of 70% from 2007 to 2008 in support of RusHydro's investment plans. The company is therefore set to reap the rewards of the Russian electricity market liberalisation, rising tariffs and the country's generating capacity deficit. Rus-

Hydro is positioning itself as one of the world's largest renewable energy producers, and is expected to become the major developer of this sector in Russia.

Kemerovo Azot

Kemerovo Azot is a producer of nitrogen fertilizer and caprolactam, located in the Kemerovo region of Siberia. The company has approximately 8,000 employees and is owned to 76% by SIBUR Holding. Kemerovo Azot currently has a 37% domestic market share for caprolactam and a very favorable position on the growing Russian fertilizer market. In 2006 the company produced approximately 766 ktonnes of ammonium nitrate, 471 ktonnes of urea and 854 ktonnes of ammonia. The output is split between two production sites currently working at utilization ratios of almost 100%. However, a three year investment program was approved by SIBUR Holding in 2005, granting Kemerovo Azot 220 million USD to expand its ammonia and urea facilities.

SIBUR holding is Russia's largest petrochemical holding company, of which Gazprom owns a controlling stake. Kemerovo Azot's ownership structure has lead to uncertainty and a relatively low valuation of the company in comparison to many other Russian fertilizer producers. We believe two potential scenarios could trigger a revaluation of Kemerovo Azot i) A dilution of Gazprom's stake in SIBUR holding in conjunction with an IPO, which would increase the liquidity and the transparency of the company, ii) SIBUR holding selling Kemerovo Azot, as a non-core asset, to a strategic investor.

Tinkoff Credit Systems

Tinkoff Credit Systems (TCS) bank is Russia's first purpose-built monoline credit card issuer. Founded by Oleg Tinkov, a well-know Russian entrepreneur and consumer product specialist, TCS commenced its commercial operations in June 2007, and has an aggressive plan to grow into a leading issuer of credit cards for the Russian market.

TCS is run by a talented team of experienced professionals formerly employed by Visa, Master Card, McKinsey and top Russian banks. TCS's operating model depends entirely on a non-branch-based service and its main channel for attracting clients is direct mail (post). The bank's plan is to distribute cards virtually all over Russia targeting primarily urban customers who live busy active lives. To achieve its ambitious goals TCS has acquired best in class technological platforms allowing handling customer acquisitions, servicing and payment collection.

The bank generates interest income charged on the outstanding credit card balance as well as an annual service fee, withdrawal fees and other fees (e.g. late payment fees). Basic rates remain at the level of 36% (average effective percentage rate) both for purchases and cash advances. To achieve payment discipline, in the event of late payment, the percentage rate is increased to 54% and substantial fees are charged. TCS is seeking to reach a market share of 3–5% by 2010. According to the bank's projection the Russian credit card segment will grow from today's USD 7bln to USD 20–25 bln, which allow them to accumulate a credit card loan portfolio of USD 1,500 mln.

Though starting from a low base, Russian bank loans to individuals have grown 12 times over the past 5 years. Nevertheless, Russian consumers continue to be underlevered by global standards. In 2006 consumer loans made up only 7% of the Russian GDP vs. 12% for Kazakhstan and 17% for the UK. When it comes to credit card lending, today only 1 genuine credit card is issued per 20 people in Russia while in Western Europe there are 2–3 credit cards for every person. With a population of 142 million and double digit disposable income growth, Russian consumer lending will continue to be in a strong growth stage.

In September 2007, Goldman Sachs became a TCS's minority shareholder. In December 2007, Vostok Nafta entered into syndicated term loan arrangement whereby it commited to provide RUR 500 million and became entitled to warrants representing 2% of TCS's equity.

Transneft

Transneft is the world's largest crude oil pipeline network operator with around 50,000 kilometres of long-distance pipelines, 386 oil refilling stations and 833 reservoirs, with a storage capacity of around 15 mln cubic meters. The company transports approximately 93% of Russia's total oil production, and piped a total of 459.3 million tonnes of oil during 2006.

Transneft have been very successful at increasing their transport tariffs each year and therefore also the company's profitability. However, long term profitability of the company is still to an extent dependant on

Fertilizer companies, January 2008

Company	Price, USD Common	Price, USD Preferred	Mcap mln USD	EV mln USD	Free float %	P/E 2008	EV/EBITDA 2008	EV/Sales 2008
Acron	55	n/a	2,385	2,607	16.13%	6.4	4.5	1.5
Ammophos	110	n/a	992	954	7.02%	4.5	2.9	1.0
Kemerovo Azot	39	n/a	265	441	15.02%	7.7	6.9	1.2
Dorogobuzh	0.57	0.39	471	563	22.67%	4.2	3.5	1.3
Silvinit	990	665	9,482	9,667	18.86%	14.3	9.8	6.2
Uralkali	6.15	n/a	13,065	13,230	33.10%	12.7	9.3	6.1
Apatit	291	159	2,146	2,406	6.6%	14.7	6	2.2

Source: Renaissance Capital

the government allowing continuous increases of the tariffs. Transneft is, by many, also seen as significantly undervalued both in comparison with the Russian oil majors, but in particular in terms of the replacement costs per kilometre of pipeline. Transneft is trading at around USD 206,000 per kilometre – which is less than a tenth of the cost of some recent pipeline projects, implying that there is room for improvement in the valuation of the company.

Bashneft

Bashneft is an oil company with assets and production concentrated to one region of Russia; the Republic of Bashkortostan. In 2006 Bashneft accounted for 99% of Bashkortostan's oil production, with an output of 86 million barrels and revenues of USD 3.7 billion. In 2007, the company recorded an output volume of 233 kbpd, making it the tenth largest producer in Russia. Bashneft operates predominantly mature fields and could, going forward, benefit from lower mineral extraction taxes (MET) applicable to depleted fields. The potential tax breaks, which are linked to the actual depletion of the fields, could more than halve the company's MET by 2010 and thus have considerable positive effects on the company's EBITDA margin. Many also see Bashneft as a potential acquisition target for one of the oil majors during 2008. A new strategic majority shareholder would most probably provide Bashneft with refining capabilities, increasing the company's profitability further.

Ukraine

The political fight in Ukraine continues. In the last day of September, the pre-term parliamentary elections, called by president Yuschenko, which caused so much controversy and political wrangling during the summer months, were held quietly and relatively orderly (at least without too much challenging in the aftermath of the election). The official results of the new elections still show that the power stays divided between the Orange parties (BYT and OU-PSD) and the party of the ex- president runner-up Yanukovich (PoR) and the power struggle is still very much in balance. The official results of the elections are presented in the table below.
Although the leading coalition in the parliament had finally been formed with a slim majority (two votes) by the end of December, it took several heated sessions of the Rada to elect Yulia Tymoshenko as the new Prime Minister. Despite the New Year holiday season, both the parliament and the Cabinet went to work right after this appointment. However, at the end of January the sessions of the Rada were once again interrupted. In a protest to a letter signed by President Yuschenko, Prime Minister Tymoshenko and the speaker of the Rada (Yatsenyuk), in which they expressed their hope that Ukraine could join the action plan for NATO membership, the opposition PoR started to block the presidium of the Rada and physically obstructed the sessions of the parliament for over a month. Only a looming prospect of yet another new extraordinary general election (with Yulia Tymoshenko's parties being the most likely beneficiaries) managed to push the deputies to look for a compromise and resume the work of the Rada.
So far, Ukraine has a much more dynamic government than the country had in 2007. The agenda of the new government is a national breakthrough, which assumes a large amount of law-making work. However, it is still to be seen whether Yulia Tymoshenko and her followers have learned the lessons of 2005. The first signs are quite mixed, with a dedicated push to write new laws on one hand, and still old games in the revision of several cases of privatisation (Luhansk Teplovoz and Nikopol Ferroalloy Plant as immediate examples) and populism (the move to start payments to depositors of the former USSR savings bank) on the other. The initial signs of the resumed rivalry between President Yuschenko and Prime Minister Tymoshenko also started to show in the form of the president interfering with the moves of the prime minister on the crucial issue of gas supplies (see a more detailed description below), or by calling on the government to revise its privatisation plan only hours after its approval by the cabinet.
Still, privatisation appears to be one of the few credible ways to finance growing budget expenditures, and we see encouraging signs that it is moving ahead. The long-awaited privatisations of the Odessa Portside Plant and Ukrtelecom (much bigger than the expected 67.79% stake) have finally been announced. The government even made a move to accelerate the privatizations and appointed Andriy Portnov, a member of the governing coalition, as acting chairman of the State Property Fund (SPF), while the parliament, whose approval is required for the top SPF job,

Other holdings

Ukraine Parliamentary Election 2007

Party/Block	Total Vote	Change to previous	Seats in Rada
Party of Regions (PoR)	34.4%	+2.2pp	175
Block of Yulia Tymoshenko (BYT)	30.7%	+8.4pp	156
Our Ukraine – People's Self-Defence (OU-PSD)	14.2%	0	72
Communists	5.4%	-1.2pp	27
Lytvyn Block	4.0%	na	20
	88.7%		450

Note: The Socialists, represented in the previous parliament, did not surpass the 3% entry barrier

remains physically blocked by the opposition deputies. Yet, as the head of the SPF cannot be dismissed without the consent of the Rada, President Yushchenko intervened immediately and annulled the move by the government – a small victory for the rule of law in Ukraine.
We have also noticed a lack of political consolidation and/or public consensus on reforms, which will continue to drag on the government's performance. For example, due to the lack of political resolve and differences in opinions within the ruling coalition, the moratorium on land sale has ended, but still the agricultural land reform has been effectively postponed for another year.
The mixture of populist moves and action constraints is coming on the back of deteriorating macroeconomic parameters (especially inflation pressures) globally, so Ukraine, without an active anti-inflationary policy is suffering as well. The latest CPI report confirmed that consumer prices surged again in January, rising 2.9% MoM (following jumps of 2.1% in December and 2.2% in November) and 19.8% YoY, the highest rate since 2000. Food prices again showed the largest growth of 4.3% MoM, while fuel-price inflation slowed to 1.2% during the month – from 3.8% in December and 9.1% in November.
Worth noting is the fact that despite the continued political turmoil in the country for the last three years, the Ukrainian economy shows robust growth (7.3% YoY real GDP growth in 2007). One may get an impression of a causality link between the two developments: local business is growing as the politicians are too busy with their political struggle and therefore not interfering with economic and business matters.

Gas tensions continue

The issues related to the gas imports (quite sizeable at 50–55 bcmpa, and also very costly) are inevitably at the top of the agenda of the new Ukrainian Cabinet. With the year starting, the focus of the renewed attacks from the government was the involvement of RosUkrEnergo and the general principles of gas supplies to Ukraine.
Oleh Dubyna, previously the head of NAK UEC, the Ukrainian state energy holding, became the head of Naftogaz Ukraine and during his first visits to Moscow made a controversial statement that Ukraine would like to substantially increase gas transit tariff for Russian gas heading to Europe – from current USD 1.7/mcm/100 km to USD ~7/mcm/100 km. From the standpoint of Mr. Dubyna, this increase would help Ukraine to cope with the soaring gas prices.
Yet, President Yushchenko spoke out against such a move, claiming that this would trigger the response of a matching rise in transportation tariffs for Ukraine-designated gas crossing Russia and, as a result, would cause higher domestic gas prices for Ukraine. A back of the envelope analysis confirms this: Russia transports around 125–127 bcmpa via a 950–1,100 km long Ukrainian system to Europe, while 50–55 bcmpa of gas from Central Asia is transported ~2,500 km through Gazprom's network to Ukraine. As a result, the transit charges are in parity as long as the transportation tariffs on both sides are linked to one another. For Gazprom such a change in tariffs would be neutral, while Naftogaz Ukraine is perhaps hopeful of improving its finances by pocketing increased transit payments from Russia while passing the increase in transit fees for imported gas to domestic industrial consumers. Given the clear risks of such a move to Ukrainian economic growth, as well as negative effects on the population, President Yuschenko's opposition to this proposal is understandable.
Following the initial setback, Oleh Dubyna turned his offensive on RosUkrEnergo and requested a permission to buy 50 bcm of gas in 2008 directly from Central Asian producers (mainly Turkmenistan). The practical details of this proposal are unclear, as all of the Turkmen gas has already been committed and the transit capacity has been contracted to RosUkrEnergo, so without an agreement with Gazprom regarding the elimination of this intermediary Dubyna's proposals have no future.
Meanwhile, the cold winter in Central Asia and the diversions of gas to meet increased local demand correspondingly reduced the amount of gas flowing via RosUkrEnergo to Ukrainian consumers. Gazprom filled the gap by supplying Ukraine with its own gas without any contracts and therefore priced at USD 314.7/mcm (European levels, as agreed earlier in the general principles). In a move intended to prepare proper discussions during the visit of President Yuschenko and Prime Minister Tymoshenko to Moscow on February 12, 2008, Gazprom issued a press release in which the company insisted on Ukraine

repaying its gas-related debts, now reaching USD 1.5 bln, in full.

In the month that followed, the negotiations on the matter continued with mixed fortunes and with Gazprom finally resorting to cutting its gas supplies to Ukraine twice – each time by 25%. At the same time Ukraine issued a warning saying that it would reduce volumes transited to Europe to compensate for this shortfall. As the conflict started to escalate, Gazprom and Naftogaz Ukraine finally reached an agreement, which laid grounds for a hope that this new round of the old conflict would settle without causing too much damage to the image of both parties – unlike the situation in January 2006. The key points of this agreement were:

1) in 2008, Ukraine will be supplied with no less than 49.8 bcm of Central Asian gas at USD 179/mcm;

2) payment for Central Asian gas delivered to Ukraine in Jan–Feb 2008 will be made to RosUkrEnergo, while payment for Russian gas already consumed during the same period (and priced by Gazprom at USD315/mcm) will be made in kind, with the gas currently stored in Ukrainian underground storage facilities;

3) starting from April 1, 2008, Gazprom's affiliated or subsidiary companies will sell at least 7.5 bcm of gas on the Ukrainian market annually;

4) from 2009, the price of gas for Ukraine will be set in line with the price for Central Asian gas (and the recent negotiations with Central Asian leaders in Moscow show that these prices will be linked to the European gas prices).

The agreement allows the two conflicting parties to find a compromise, but it is still to prove its vitality. The two sides are currently aligned in their desire to eliminate RosUkrEnergo from the Ukrainian gas supply chain, but the alternative supplier have not been specified yet and the previous history of direct gas supplies to Ukraine by Gazprom was unfortunately marred with the recurring acute conflicts.

Ukraine enters WTO

On a positive note, on February 5 Ukraine's president Viktor Yuschenko and the WTO Secretary General Pascal Lamy signed a protocol to admit Ukraine to the World Trade Organization. This successfully completed over 13 years of negotiations. Within two weeks the accession documents were passed to the Rada for ratification, the deadline for which is July 4, 2008. The country will officially become a member 30 days after the ratification of the package, therefore, the country's membership should be in full legal force by the summer. Ukrainian officials estimate that joining the WTO could add 1.5%–2.0% in extra GDP growth per year. The direction of the Ukrainian foreign policy remains definitely pro-European and while Russia is still a crucial trading partner and neighbour, it is the gravity towards Europe that is clearly defining the direction of future development.

Dakor – a sugar producer

Dakor is a sugar producer from Western Ukraine, which uniquely balances agriculture (sugar beet production) with sugar milling capacity. In 2007, the company leased 128,000 ha of land at a total leasing fee of USD 3 mln (ie, USD ~25/ha, while the average leasing cost in Ukraine is moving up to USD 40/ha). Dakor plans to increase its agricultural portfolio to 150,000 ha in 2008. Currently, Dakor operates 4 sugar mills, with a total capacity of 20,000 tpd (5% of the Ukrainian sugar market). The company plans to increase the amount of land leased (owned) and the sugar milling capacity (and perhaps adding refrigerated storage to enable the company to conserve the sugar beets) in order to reach a share of over 10% of the sugar market by 2010.

Dakor's planned 2008 capex of USD 30 mln will be spent as follows: 30% on sugar mills, 10% on elevators, 20% on agro machinery, and 10% on a fertilizer plant.

TKS – a developer from Western Ukraine

During the fourth quarter of 2007, TKS added two more projects (one in Lvov and another in Truskavets), thus enlarging its overall portfolio to 16 projects with a total area of 225,000 m^2 (an increase by 44%). The Lvov project involves construction of a shopping centre (a mall with a supermarket – a total area of 32,000 m^2) and of an office centre (30,000 m^2) by the second quarter 2009. The project is located close to a large residential area and has access to an important traffic route, which makes it easily accessible to private vehicles and public transportation. The Truskavets Ambassador project involves construction of a five-storied three-star serviced apartment complex with 60 bedrooms (currently 60% completed), which will have a developed infrastructure (including a restau-

Other holdings

Dakor current seed/harvest

	2007 '000 ha	2008 '000 ha	Yield tn/ha	Price USD/tn
Sugar beet	21.0	28.0–30.0	41–43	35
Rapeseed	2.5	7.5	2.5	400–420
Winter wheat	15.5	20.0–30.0	4.0	240
Barley	0	20.0–30.0		
Corn	6.0	12.0		

Note: barley volumes for 2008 only if the agreement with Slavutich brewery, currently under discussion, is signed

rant and a spa) and is located close to the main health centers of the resort.
Previously TKS used partnerships with grocery chains Auchan (France) and Furshet (Ukraine, with participation of Auchan) to lease out space in the operated supermarkets. In October, the company signed preliminary lease agreements with Russian retailer Vester, thus securing 8–53% higher rental rates in its four projects in the regional cities of Truskavets, Drogobych, Boryslav and Novovolynsk. This, combined with the portfolio additions, helps to increase TKS net asset value.
By the end of 2007, as the company was drafting its development strategy for 2008 with an eye on a full IPO in 2009, an irreconcilable conflict had emerged between the two major shareholders in the company – Ivan Torskiy and Volodymyr Hovirko. In fact, the conflict got a speedy resolution when Ihor Balenko, the owner of the Ukrainian retail chain Furshet and a long-term partner of both TKS and Ivan Torskiy, bought Volodymyr Hovirko's share. The arrival of Ihor Balenko, with his extensive experience of managing large companies in Ukraine should be positive for the further development of the corporate strategy of TKS. However, the two partners will need to make an effort to avoid a potential conflict of interests stemming from their already diverse business involvements.

Poltava GOK share issue

At its EGM on December 7, 2007, Ukrainian iron pellet producer Poltava GOK had approved an increase in its share capital, aimed at financing the expansion plans.
Given the deficiencies of the Ukrainian laws on capital markets, local companies are allowed to issue capital only at the nominal value of their shares (a legal nonsense providing absolutely no incentives to enhance market capitalisation). As a result, Poltava GOK's issue was highly dilutive and pushed the existing shareholders to participate in the closed subscription to avoid substantial dilution in the value of their holdings in the company.
On top of the total authorised capital of 1,149,384,000 hryvnyas, the company issued 25,350,000 new shares at 9.96 hryvnyas each (around USD 2, while the shares were traded in the market above USD 16), for a total proceeds of 252,486,000 hryvnyas, thus increasing the amount of its outstanding shares by approximately 22%.
The closed subscription had been held in two stages:
1st stage: Dec 28, 2007–Jan 22, 2008, pre-emptive pro rata subscription for the existing shareholders
2nd stage: Jan 23, 2008–Jan 25, 2008, shareholders could buy the non-distributed shares on a first come-first served basis (leaving the majority holder London-listed Ferrexpo a likely beneficiary at this stage)
The proceeds of the share issue were planned to be used for further increase in operations. Following the issue, Ferrexpo, the UK-listed parent company of Poltava GOK, has announced the acquisition of an initial fleet of sixteen 180-tonne capacity dump trucks and related equipment worth USD 55 mln to start stripping works at the company's Yerystovske iron ore deposit. The equipment is scheduled for delivery in November 2008.
In a separate recent development, Ferrexpo has signed a long-term export contract to supply 1.3 Mt of pellets over the next three years to a new customer based close to Ukraine.

Other holdings

Largest shareholders as per December 28, 2007
The shareholder list below as at December 28, 2007, shows the 15 largest owners at that time. The number of shareholders in Vostok Nafta on December 28, 2007 amounted to more than 13,000.

Share information
All the shares carry one vote each. The shares are traded as depository receipts (SDR) in Stockholm, where E Öhman J:or Fondkommission AB is the custodian bank. The shares are not subject to trading in Bermuda. A depository receipt carries the same dividend entitlement as the underlying share and the holder of a depository receipt has a corresponding voting right at shareholders meetings. The holder of a depository receipt must, however, follow certain instructions from the custodian bank in order to have the right to participate in shareholders meetings.

Dividend policy
The Board of Vostok Nafta considers it highly desirable and important to be able to issue dividends to the shareholders. Although no dividend has been proposed for the year, it is the company's intention in the long term to create a well balanced disposition of profits betweend dividends and reinvestments in the company.

Information about the net asset value
Vostok Nafta publishes a monthly estimated net asset value, no later than the 10th of the respective month. This value is issued to the market via press releases and is also distributed via e-mail. In addition it is also available on Vostok Nafta's webpage: www.vostoknafta.com. A more exact net asset value is published in the quarterly reports.

Potential net asset discount
With a view to limiting a possible net asset discount, the Vostok Nafta articles of association contains an opportunity to buy back the company's own shares. Such purchases may be made within the stipulated capital limits, provided that the bought back shares are immediately cancelled.
During the year, no shares were repurchased.

The market
The Vostok Nafta share (SDR) is since July 4, 2007 traded on the OMX Nordic Exchange Stockholm (previously the Stockholm Stock Exchange), Mid Cap segment.

Share turnover
The average daily turnover during the period July 4, 2007 to December 31, 2007, was 141,700 shares. During the quarter October 1, 2007 to December 31, 2007, the average daily turnover was 151,500 shares. Trading has been conducted 100% of the time.

Codes Assigned to Vostok Nafta's Share
Recent and historic quotes for Vostok Nafta's share are easily accessible on a number of business portals as well as via professional financial and real-time market data providers. Below is a list of the symbols and codes under which the Vostok Nafta share can be found.

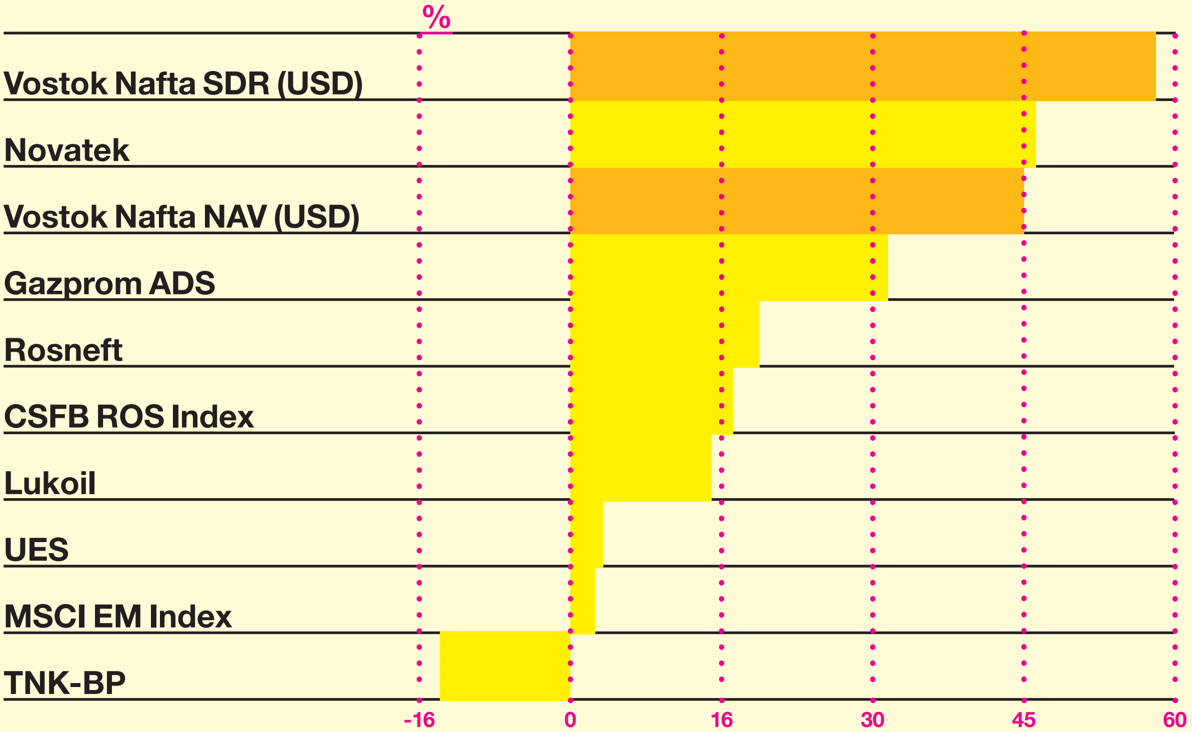
OMX Nordic Exchange ISIN Code	SE0002056721
OMX Nordic Exchange short name (ticker)	VNIL SDB
Reuters	VNILsdb.ST
SAX/Ecovision	VNIL SDB
Bloomberg	VNIL:SS

The Vostok Nafta share

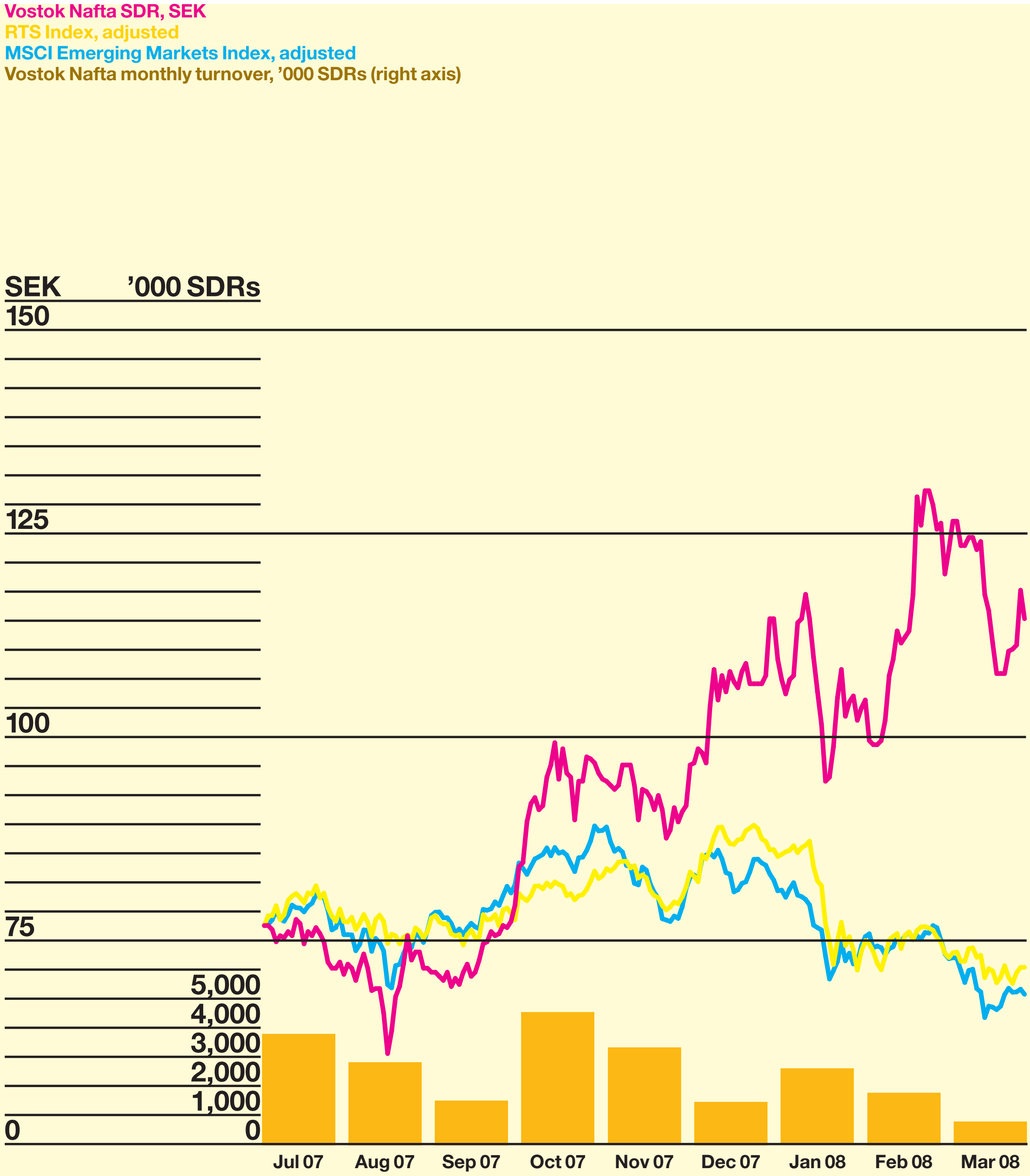
Largest shareholders, Dec 28, 2007

		Number of SDRs	Share of capital and votes, %
01	Lorito Holdings Ltd*	14,000,000	30.42%
02	4th Swedish National Pension Fund	2,233,105	4.85%
03	Fidelity Em Eur, M East & Afr Fund	1,658,655	3.60%
04	AFA Insurance	1,366,904	2.97%
05	Swedbank Robur Funds	830,219	1.80%
06	Investors Bank & Trust	823,770	1.79%
07	Nordea Funds	816,400	1.77%
08	Speaking Partners AB	813,534	1.77%
09	Northern Trust Company	439,373	0.95%
10	Handelsbanken/SPP Funds	423,926	0.92%
11	East Capital Funds	376,850	0.82%
12	Gamla Livförsäkringsaktiebolaget	280,550	0.61%
13	Folksam Funds	274,678	0.60%
14	Skandia Liv	258,825	0.56%
15	SEB Funds	217,790	0.47%
Subtotal 15 largest owners		24,814,579	53.92%
Other foreign owners & nominees		13,949,905	30.31%
Other, approx. 13,000 shareholders		7,256,417	15.77%
Total		46,020,901	100.00%

* Lorito Holdings Ltd. is an investment company wholly owned by a trust whose settler is the estate of Adolf H Lundin.



Development of Russian shares and Vostok Nafta, July–December, 2007



Vostok Nafta share price development

July 4, 2007–March 31, 2008
Source: Bloomberg

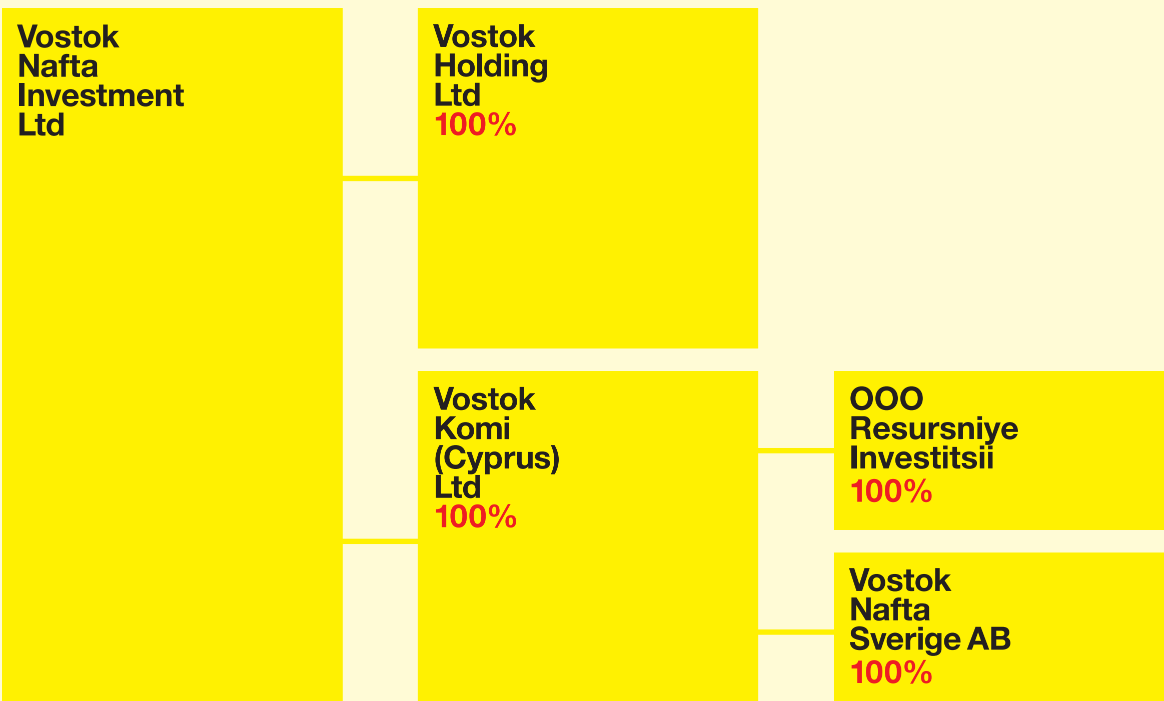
Background
Vostok Nafta Investment Ltd (“Vostok Nafta”; “The Company”) was incorporated in Bermuda on April 5, 2007 with corporate identity number 39861. The Swedish Depository Receipts of Vostok Nafta (SDB) are listed on the OMX Nordic Exchange Stockholm, Mid Cap segment. Ticker: VNIL SDB. There were a total of around 13,000 shareholders at the end of December 2007.
The Vostok Nafta Investment Ltd Group was formed in connection with the restructuring of Vostok Gas Group, which was carried out in 2007. The restrcturing entailed a purchase of Vostok Komi (Cyprus) Ltd and its subsidiary Vostok Nafta Sverige AB from Vostok Gas, and the subsequent transfer of non Gazprom assets from Vostok Gas Group to Vostok Nafta Group.

Group structure
As at December 31, 2007, the Vostok Nafta Group consists of the Bermudian parent company Vostok Nafta Investment Ltd, one wholly owned Bermudian subsidiary, Vostok Holding Ltd; one wholly owned Cypriot subsidiary, Vostok Komi (Cyprus) Ltd; one wholly owned Russian subsidiary, OOO Resursniye Investitsii; and one wholly owned Swedish subsidiary, Vostok Nafta Sverige AB.
Vostok Komi (Cyprus) Ltd is responsible for the group’s portfolio management.
Vostok Nafta (the Group) currently has four employees in Stockholm, one employee in London, and sixteen employees in Moscow.

Operating policy
“New” Vostok Nafta willl continue to invest in accordance with the strategies of “old” Vostok Nafta; with a clear and sustained focus on Russia and its neighbours. However, its mandate is extended in terms of geographical areas and industrial sectors.

Organisation of activities
The Board of Directors meets in person at least twice a year and more frequently when necessary. In addition to this, whenever necessary meetings are conducted by telephone conference. Between meetings, the Managing Director has regular contact with the Chairman of the Board and several other Board members. The Board of Directors adopts decisions on overall issues affecting the Vostok Nafta group.
The Managing Director manages the company’s day-to-day activities and prepares investment recommendations in cooperation with the other members of the Investment Committee. The Chairman also holds an executive position and takes part in the work of the company on a daily basis.
Recommendations on investments are, as stated above, made by the Investment Committee, which operates from London, made up of three representatives from the Board of Directors. Two members of the Investment Committee, i.e. a majority, can together issue recommendations. The Board of Directors of Vostok Komi (Cyprus) Ltd subsequently takes the investment decisions.
Between meetings of the Board of Directors, the Managing Director reports regularly to the Chairman and at least once a month to the Board of Directors.

Company information



Vostok Nafta Group structure

During 2007 a restructuring of Vostok Gas Ltd Group was carried out, whereby the shares in Vostok Komi (Cyprus) Ltd and its subsidiary Vostok Nafta Sverige AB were acquired by Vostok Nafta Investment Ltd. The restructuring of the Vostok Gas Group also entailed a transfer of non-Gazprom related assets to the Vostok Nafta Group and a sale of the shares in RusForest Ltd and RusForest (Cyprus) Ltd to Vostok Komi (Cyprus) Ltd and third party.

The financial statements have been prepared as if the restructuring of Vostok Gas was carried out on September 30, 2003, and comprises the consolidated accounts of the companies that are (or would have been) included in the Vostok Nafta Group; i e Vostok Komi (Cyprus) Ltd, Vostok Nafta Sverige AB, RusForest Ltd and RusForest (Cyprus) Ltd. The restructuring of the Group further implies that items of the income statement and the balance sheet that relate to non-Gazprom assets, which formerly have been recognized in the accounts of other companies of the Vostok Gas Group, are now included in the consolidated financial statements of Vostok Nafta.

The transactions by which Vostok Nafta acquired the companies mentioned above and the non Gazprom related assets, which have been recognized in other companies of the Vostok Gas Group, comprises transactions between companies under common control. These transactions are being recognized to the same values as they were in the selling company, in accordance with the so called predecessor accounting method. For further information, see note 1 in the notes to the Financial statements.

Income statement in brief

(Expressed in USD thousands)	Jan 2007– Dec 2007 (12 months)	Jan 2006– Dec 2006 (12 months)	Oct 2004– Dec 2005 (15 months)	Oct 2003– Sep 2004 (12 months)
Result from financial assets	282,100	61,908	126,066	41,514
Other operating income	10,412	12 541	4 726	2 914
Total income	292,512	74,449	130,792	44,428
Operating expenses	–5,705	–3,441	–3,821	–3,520
Russian dividend withholding tax expenses	–1,499	–1 897	–691	–437
Operating result	285,309	69,111	126,280	40,471
Net financial items	–2,155	610	3 209	7 777
Result before tax	283,154	69,721	129,488	48,248
Tax	–389	–88	–502	–60
Net profit for the period	282,765	69,633	128,986	48,188

Balance sheet in brief

(Expressed in USD thousands)	Dec 31, 2007	Dec 31, 2006	Dec 31, 2005	Sep 30, 2004
Non current fixed assets	545	316	92	–
Non current financial assets	822,394	387,182	185,138	98,473
Current financial assets	–	–	995	995
Cash and cash equivalents	27,528	5,124	7,212	5,118
Other current receivables	8,765	969	16,631	49,966
Total assets	859,232	393,591	210,068	154,552
Equity	803,954	385,043	209,532	154,426
Deferred tax liability	1,358	11	–	–
Current tax liability	106	585	509	80
Other current liabilities	53,814	7,952	27	46
Total equity and liabilities	859,232	393,591	210,068	154,552

Cash flow in brief

(Expressed in USD thousands)	Jan 2007– Dec 2007 (12 months)	Jan 2006– Dec 2006 (12 months)	Oct 2004– Dec 2005 (15 months)	Oct 2003– Sep 2004 (12 months)
Cash flow from/used in operating activities	–162,982	–108,225	76,079	–1,158
Cash flow used in investing activities	–300	–264	–97	–
Cash flow from/used in financing activities	185,673	106,375	–73,880	1,643
Cash flow for the period	22,391	–2,114	2,102	485
Exchange rate differences in cash and cash equivalents	13	26	–8	–207
Cash and cash equivalents at the beginning of the period	5,124	7,212	5,118	4,840
Cash and cash equivalents at the end of the period	27,528	5,124	7,212	5,118

Financial summary

Key ratios

(Expressed in USD thousands if not stated otherwise)	Jan 2007– Dec 2007 (12 months)	Jan 2006– Dec 2006 (12 months)	Oct 2004– Dec 2005 (15 months)	Oct 2003– Sep 2004 (12 months)
GROWTH				
Equity ratio, percent	93.57	97.83	99.74	99.92
RISK BEARING CAPITAL				
Return on equity, percent	47.56	20.88	70.88	37.94
Return on capital employed, percent	46.04	20.88	70.88	37.94
Debt/equity ratio, multiple	6.21	–	–	–
Interest coverage ratio, multiple	77	–	–	–
SHARE DATA				
Net asset value, MUSD	804	385	210	154
SEK/USD	6.4683	6.85	7.94	7.27
Net asset value, MSEK	5,200	2,638	1,667	1,123
Development of net worth in USD, percent	109	84	35	48
RTS Index	2,291	1,922	1,126	632
Development RTS Index, percent	19	71	78	11
Dividends	–	–	–	–
Dividend/share	–	–	–	–
Yield, percent	–	–	–	–
SHARE DATA				
Net asset value per share, USD	17.47	8.34	4.55	3.36
Net asset value per share, SEK	113.00	57.31	36.15	24.39
Number of shares outstanding at year-end	46,020,901	46,020,901	46,020,901	46,020,901
Weighted average number of shares outstanding	46,020,901	46,020,901	46,020,901	46,020,901
– diluted	46,020,901	46,020,901	46,020,901	46,020,901
EMPLOYEES				
Average number of employees during the period	9	10	9	8

Share data

The company was incorporated in 2007 and had until the utilization of the warrants in July 2007 only one share. The number of shares used for showing meaningful per share data for all periods has been the number of shares achieved after the utilization of the warrants. Related capital in connection with the new share issue during 2007 have not, however, been taken into account.

Definitions

Equity ratio, percent Equity ratio is defined as Shareholders' equity in relation to total assets.
Return on equity, percent Return on equity is defined as result for the year divided by average equity.
Return on capital employed, percent Return on capital employed is defined as net result plus interest expenses plus/less exchange differences on financial loans divided by the average capital employed (the average total assets less non-interest bearing liabilities over the year).
Debt/equity ratio, multiple Debt/equity ratio, multiple is defined as interest-bearing liabilities in relation to Shareholders' equity.
Interest coverage ratio Interest coverage ratio, multiple is defined as profit after financial items plus interest expenses in relation to interest expenses.
Development of net worth in USD, percent Change in net worth in USD per share compared with previous accounting year, in percent.
Net asset value Net asset value is defined as shareholders' equity.
Net asset value per share, USD Shareholders' capital divided by the number of shares outstanding at year-end.

Board of Directors

Lukas H Lundin
Chairman

Swedish citizen, born 1958. Member of the board since 2007. Committee assignments in Vostok Nafta: compensation committee, investment committee. Professional and educational background: Senior Director of Lundin Oil AB and president of International Musto Exploration Limited for over 12 years. Mr. Lundin holds a degree in mining engineering from The New Mexico Institute of Mining and Technology. Other significant board assignments: Chairman of Vostok Gas Ltd., Tanganyika Oil Co. Ltd, Suramina Resources Inc., Canadian Gold Hunter Corp., Red Back Mining Inc., Denison Mines Corp and Lundin Mining, member of the boards of Lundin Petroleum AB, Atacama Minerals Corp. and Pearl Exploration and Production Ltd. Holdings in Vostok Nafta: 40,000 depository receipts. Salary and remuneration: TUSD 76. No agreement regarding severance pay or pension.

Al Breach
Board member

British citizen, born 1970.Member of the board since 2007. Professional and educational background: From early 2003, Al Breach worked in the research department of Brunswick UBS/UBS in Moscow, rising to be Managing Director and Head of Research before leaving in October 2007. He has previously been employed as economist by Goldman Sachs with responsibility for the CIS states and as a fund manager at Rothschild Asset Management in London. Al Breach holds an MSc in economics from the London School of Economics and a degree in mathematics from Edinburgh University. Holdings in Vostok Nafta: none. Salary and remuneration: TUSD 29. No agreement regarding severance pay or pension.

Per Brilioth
Managing Director and board member

Swedish citizen, born 1969. Member of the board and Managing Director since 2007. Committee assignments in Vostok Nafta: investment committee. Professional and educational background: Between 1994 and 2000, Per Brilioth was head of the Emerging Markets section at Hagströmer & Qviberg and he has worked close to the Russian stock market for a number of years. Per holds a BA in Business Administration from the University of Stockholm, and a Master of Finance from the London Business School. Other significant board assignments: Chairman of Black Earth Farming Ltd, member of the boards of Vostok Gas Ltd., Kontakt East Holding AB, Bukowskis Auktioner AB and X5 Group AB. Holdings in Vostok Nafta: 80,000 depository receipts and 250,000 options. Salary and remuneration: TUSD 800. Agreement regarding severance pay and pension: Brilioth has the right of twelve months full salary in the event of termination of appointment on the part of the company. Should he himself decide to resign, he must observe six months notice of termination. Brilioth also has a pension plan in accordance with the Swedish ITP standards.

Paul Leander-Engström
Board member

Swedish citizen, born 1966. Member of the board since 2007. Committee assignments in Vostok Nafta: compensation committee, investment committee. Professional and educational background: Co-founder and former Managing Director of Prosperity Capital Management (SE) AB and former partner/co-head of research at Brunswick Warburg Moscow. Paul Leander-Engström holds a Master of Science in Economics and Business from the Stockholm School of Economics and a law degree from Stockholm University. Other significant board assignments: Chairman of the board of directors of Sonores AB and member of the board of Prosperity Capital Management. Holdings in Vostok Nafta: 37,000 depository receipts. Salary and remuneration: TUSD 41. No agreement regarding severance pay or pension.

Torun Litzén
Board member

Swedish citizen, born 1967. Member of the board since 2007. Committee assignments in Vostok Nafta: audit committee. Professional and educational background: Director Investor Relations at Investment AB Kinnevik. Torun Litzén holds a Master of Science in Economics and Business from the Stockholm School of Economics. Other significant board assignments: Vostok Gas Ltd. Holdings in Vostok Nafta: 200 depository receipts. Salary and remuneration: TUSD 43. No agreement regarding severance pay or pension.

Board, management and auditors

Ian H Lundin
Board member
Swedish citizen, born 1960. Member of the board since 2007. Committee assignments in Vostok Nafta: audit committeee. Professional and educational background: Former CEO of Lundin Petroleum, Lundin Oil AB and President and CEO of International Petroleum Corporation. Mr. Lundin holds a Bachelor of Science degree in petroleum engineering from the University of Tulsa. Other significant board assignments: Chairman of Lundin Petroleum AB. Holdings in Vostok Nafta: 40,000 depository receipts. Salary and remuneration: TUSD 43. No agreement regarding severance pay or pension.

William A Rand
Board member
Canadian citizen, born 1942. Member of the board since 2007. Committee assignments in Vostok Nafta: audit committee. Professional and educational background: Director of Rand Edgar Investment Corp. Mr. Rand holds a Commerce degree from McGill University, a Law degree from Dalhousie University and a degree in Masters of Law from the London School of Economics. Other significant board assignments: Vostok Gas Ltd., Lundin Mining Corporation, Lundin Petroleum AB, Canadian Gold Hunter Corp., Suramina Resources Inc., Pender Financial Group Corporation and Dome Ventures Corporation. Holdings in Vostok Nafta: 35,000 depository receipts. Salary and remuneration: TUSD 50. No agreement regarding severance pay or pension.

Robert J Sali
Board member
Canadian citizen, born 1962. Member of the board since 2007. Committee assignments in Vostok Nafta: compensation committee. Professional and educational background: Mr. Sali has been active in the financial world since 1987 at the brokerage firms of Levesque Beaubien Inc. and BMO Nesbitt Burns. In 1999 Robert J Sali established the operation of Dundee Securities Corporation in western Canada, where he directed operations in the Equity Sales and Trading departments. Mr. Sali is currently employed by Dundee Securities Corporation as senior investment adviser. Holdings in Vostok Nafta: 15,000 depository receipts. Salary and remuneration: TUSD 34. No agreement regarding severance pay or pension.

Group management

Per Brilioth: Managing Director. See also heading “Board of Directors” above.
Anders Sjöberg: Chief Financial Officer. Swedish Citizen, born 1970. Employed since 2007. Holdings in Vostok Nafta: 2,200 depository receipts and 30,000 options.
Sergei Glaser: Analyst, member of the management team. British citizen, born 1958. Employed since 2007. Holdings in Vostok Nafta: 47,100 depository receipts and 150,000 options.

Auditors

PricewaterhouseCoopers AB
Klas Brand, born 1956. Authorised public accountant, Lead Partner. Auditor in the Company since 2007. PricewaterhouseCoopers AB, Göteborg, Sweden.
Bo Hjalmarsson, born 1960. Authorised public accountant, Partner. Auditor in the Company since 2007. PricewaterhouseCoopers AB, Stockholm, Sweden.

The Board of Directors and the Managing Director of Vostok Nafta Investment Limited hereby present the annual report for the financial year January 1, 2007–December 31, 2007.

Group structure and operations

Vostok Nafta Investment Ltd ("Vostok Nafta", or "the Company") was incorporated in Bermuda on April 5, 2007 with corporate identity number 39861. A change of name from Vostok Nafta Holding Investment Ltd was made effective in June 2007.

The Vostok Nafta Investment Ltd Group was formed in connection with the restructuring of Vostok Gas Group, which was carried out in 2007. The restructuring entailed a purchase of Vostok Komi (Cyprus) Ltd and its subsidiary Vostok Nafta Sverige AB from Vostok Gas, and the subsequent transfer of non Gazprom assets from Vostok Gas Group to Vostok Nafta Group. For further details; see "The formation of the Group" below.

As at December 31, 2007 the Group consists of one Bermudian parent company, one wholly owned Bermudian subsidiary, one wholly owned Cypriot subsidiary, one wholly owned Russian Subsidiary and one wholly owned Swedish subsidiary. The group's portfolio management activities are performed through Vostok Komi (Cyprus) Ltd.

Vostok Nafta Investment Ltd has a representative office in London, and Vostok Komi (Cyprus) Ltd has a representative office in Moscow.

The formation of the Group

Vostok Nafta Group was formed in connection with the restructuring of the Vostok Gas Group. As a first step in the formation, Vostok Komi (Cyprus) Ltd and Vostok Nafta Sverige AB were acquired for a total consideration of USD 185 thousand. The next step was Vostok Komi's acquisition of non Gazprom assets from Austro (Cyprus) Ltd (a member of the Vostok Gas Group) for a total amount of USD 377.5 million.

Acquired assets were:

– non-Gazprom share portfolio worth of USD 370.7 million

– unsettled trades of USD 1.8 million, and

– cash of USD 5.0 million.

Payment for the acquired assets was made by Vostok Komi through an issue of a promissory note to Austro, amounting to USD 377.5 million.

Simultaneously, Vostok Nafta Investment Ltd sold 46,020,900 warrants to Vostok Gas Ltd for the corresponding amount. Payment for the acquired warrants was made by way of a promissory note to Vostok Nafta, by which Vostok Nafta thus had a receivable from Vostok Gas in the amount of USD 377.5 million. This receivable was used for the subsequent settlement of Vostok Komi's liability to Austro. After the share split in Vostok Gas half of the number of shares issued were redeemed and exchanged for 46,020,900 warrants in Vostok Nafta. One Warrant entitled the holder to subscribe for one newly issued Depository Receipt in Vostok Nafta at a price of SEK 22.

On July 4, 2007, the formation of Vostok Nafta was completed through the listing of the Vostok Nafta SDB on OMX Nordic Exchange Stockholm. The proceeds from the new share issue, net after new share issue costs, amounted to approximately USD 146 mln (SEK 990 mln).

For the accounting principles applied in the formation of Vostok Nafta (as a part of the restructuring of Vostok Gas); see note 1 in the notes to the financial statements, page 67.

"New" Vostok Nafta will continue to invest in accordance with the previous strategies of "old" Vostok Nafta, with a clear and sustained focus on Russia and its neighbours. However, its mandate is extended in terms of geographical areas and industrial sectors. The formation of Vostok Nafta and the capital injected into the Company has also provided a better basis for exploiting the investment opportunities in Russia and the other CIS- states.

Debt financing

On May 4, 2007, Vostok Komi (Cyprus) Ltd has entered into a debt financing agreement. The loan, which amounts to USD 50 mln, will mature until May 4, 2008, and carries a floating interest rate of 200 basis points over LIBOR.

Assets pledged for the loan are the share portfolio.

Result and Portfolio return

During the period January 1, 2007–December 31, 2007, the result from financial assets at fair value through profit or loss amounted to USD 158.41 (25.88)

Administration report

mln. Result from investments in associated companies was USD 123.69 (36.03) mln. Dividend income was USD 10.09 (12.54) mln.
Operating costs were USD –5.71 (–3.44) mln.
Net financial items were USD –2.16 (0.61) mln.
Profit for the year was USD 282.77 (69.63) mln.
Total shareholders' equity amounted to USD 803.95 (385.04) mln on December 31, 2007.
During the period January 1, 2007–December 31, 2007, Vostok Nafta's net asset value per share has increased by 108.72% (excluding effect from proceeds from new share issue: +51.29%). This growth is higher than that of the Russian stock market, reflected in the RTS index, which increased by 19.23% during the same period.
During the period January 1, 2007–December 31, 2007, the net asset value (NAV) has increased from USD 385.04 mln to USD 803.95 mln. The change of the NAV is the result of proceeds from new share issue (+146.35), profit for year (+282.77) and other equity transactions (–10.21).
During the period January 1, 2007–December 31, 2007, net investments in financial assets at fair value through profit or loss amounted to USD 151.86.

Share data
Vostok Nafta was incorporated as a limited liability company with a share capital of USD 1 on April 5, 2007. In July 2007, 46,020,900 new shares were issued in exchange for the same amount of warrants in Vostok Nafta and a cash consideration of SEK 22 per share.
Therefore, at the end of December 2007, the number of outstanding shares in the company was 46,020,901, with a par value of USD 1 per share.
All shares carry one vote each. The Vostok Nafta share (depository receipt) is quoted on the OMX Nordic Exchange Stockholm, Mid Cap segment.

Board meetings
The board of directors of Vostok Nafta comprises eight members. During the financial year six board meetings have been held. The directors represent a number of nationalities. Board meetings are conducted in English. Three of the board members constitute the investment committee. Two of these three members may together make investment recommendations to the Board of Directors of Vostok Komi (Cyprus) Ltd who then takes the formal investment decisions. The Company's Board of Directors has two sub-committees: Audit Committee and Compensation Committee. The work and the composition of the Board and its sub-committees are described in detail in the Corporate Governance Report on page 88.
In compliance with the Code, a nomination committee has been established to to make recommendations to the AGM 2008 regarding:
– Election of Chairman
– Election of board members
– Fees for the Chairman
– Fees for board members
– Fees for board committee work
– Election of auditors
– Auditors fees
– Election of the Chairman at the AGM
– Principles for appointment of the Nomination Committee for the AGM in 2009.

The Nomination Committee has been formed with the following members: Ian H Lundin, Lorito Holdings Ltd and member of the board of Vostok Nafta; Åsa Nisell, Swedbank Robur Fonder; and Lars Öhrstedt, AFA Insurance. At the Nomination Committee's first meeting Ian H Lundin was elected Chairman of the Committee.

Remuneration principles for the senior management
The Board of Directors proposes that the management remuneration principles adopted at the Extra General Meeting held on May 18, 2007 shall continue to apply. At the Extra General Meeting, it was resolved to approve the following management remuneration principles etc; The remuneration to the managing director and other members of the senior management shall consist of fixed salary, variable remuneration, other benefits and pension benefits. Except for the managing directors, the senior management currently includes two individuals. The total remuneration shall correspond to the prevailing market conditions and be competitive. The fixed and variable remuneration shall correspond to the respective individual's responsibility and authority. The variable component should, in the first instance, be covered within the parameters of the company's option plan and shall, where payable in other instances, be subject to an

upper limit in accordance with market terms and specific objectives for the company and/or the individual. The period of notice of termination of employment shall be three to six months in the event of termination by the member of the senior management. In the event of termination by the company, the total of the period of notice of termination and the period during which severance compensation is payable shall not exceed 12 months. Pension benefits shall be either benefit-based or contribution-based or a combination thereof, with individual retirement ages. Benefit-based pension benefits are conditional on the benefits being earned during a pre-determined period of employment. The Board of Directors shall be entitled to deviate from these guidelines in individual cases should special reasons exist.

Corporate governance report

A complete report on Vostok Nafta's application of the Swedish Code of Corporate Governance, together with a Report on the Internal control, is included in this Annual Report. The Corporate Governance Report and the Report on the Internal control have not been subject to review by the Company's auditors.

Personnel

At year-end, Vostok Nafta had one employee in London. Four persons were employed by Vostok Nafta Sverige AB in Stockholm. A staff of 16 people worked at the Representative office of Vostok Komi (Cyprus) Ltd in Moscow. For further information see Note 23 in the Notes to the Financial Statements.

Treatment of retained earnings

The group's total retained earnings amount to USD 611,457 thousand.

The board of directors and the managing director propose that the retained earnings of the parent company USD 335,177 thousand, whereof the year's profit is USD 3,222 thousand, be brought forward, and that no dividends be paid for the year.

The Board of Directors and the Managing Director declare that the consolidated financial statements have been prepared in accordance with IFRS and give a true and fair view of the Group's financial position and results of operations. The financial statements of the Parent Company have been prepared in accordance with IFRS and give a true and fair view of the Parent Company's financial position and results of operations.

The statutory Administration Report and the other parts of the Annual Report of the Group and the Parent Company provides a fair review of the development of the Group's and the Parent Company's operations, financial position and results of operations and describes material risks and uncertainties facing the Parent Company and the companies included in the Group.

Stockholm, April 4, 2008

Lukas H Lundin, Chairman
Al Breach, Director
Paul Leander-Engström, Director
Torun Litzén, Director
Ian H Lundin, Director
William A Rand, Director
Robert J Sali, Director
Per Brilioth, Director and Managing Director

Income statement – Group

(Expressed in USD thousands)	Note	Jan 1, 2007– Dec 31, 2007	Jan 1, 2006– Dec 31, 2006
Result from financial assets at fair value through profit or loss	3,12	158,407	25,877
Result from investments in associated companies	4,13	123,693	36,031
Dividend income	5	10,087	12,541
Other operating income	6	325	–
Total operating income		292,512	74,449
Operating expenses	7,23	–5,704	–3,441
Russian dividend withholding tax expenses		–1,499	–1,897
Operating result		285,309	69,111
Financial income and expenses			
Interest income		1,225	584
Interest expense	19	–3,709	–
Currency exchange gains/losses, net		538	26
Other financial expenses		–210	–
Net financial items		–2,155	610
Result before tax		283,154	69,721
Taxation	8	–389	–88
Profit for the year		282,765	69,633
Earnings per share (in USD)	9	6.14	1.51
Diluted earnings per share (in USD)	9	6.14	1.51

Income statement – Group

Balance sheet – Group

(Expressed in USD thousands)	Note	Dec 31, 2007	Dec 31, 2006
NON CURRENT ASSETS			
Tangible non current assets			
Office equipment	10	545	316
Total tangible non current assets		545	316
Financial non current assets			
Financial assets at fair value through profit or loss	11,12	565,043	292,515
Investment in associated companies	11,13	248,213	94,667
Loan receivables	11,14	9,138	–
Total financial non current assets		822,394	387,182
CURRENT ASSETS			
Cash and cash equivalents	11,16	27,528	5,124
Receivables from related parties	24	4,894	611
Unsettled trades		3,172	–
Tax receivables		98	220
Other current receivables	15	601	138
Total current assets		36,293	6,093
TOTAL ASSETS		859,232	393,591
SHAREHOLDERS' EQUITY (including profit for the year)	17	803,954	385,043
NON CURRENT LIABILITIES			
Deferred tax liabilities	8	1,358	11
Total non current liabilities		1,358	11
CURRENT LIABILITIES			
Interest bearing current liabilities			
Borrowings	19,21	50,438	–
Non–interest bearing current liabilities			
Tax payable		106	585
Liabilities to related parties	24	586	–
Unsettled trades		1,677	7,626
Other current liabilities	20	141	27
Accrued expenses		972	299
Total current liabilities		53,920	8,537
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		859,232	393,591

Balance sheet – Group

Statement of Changes in Equity – Group

(Expressed in USD thousands)	Share capital	Additional paid in capital	Retained earnings including net result for the period	Minority interest	Total
Balance at December 31, 2005	–	–	209,035	156	209,191
Profit for the period	–	–	69,633	–	69,633
Total recognized income for the financial year					
January 1, 2006 to December 31, 2006	–	–	69,633	–	69,633
Transaction between Vostok Gas and Vostok Nafta	–	–	–11,855	–	–11,855
Assets provided through an issue in kind (note 17)	–	–	118,230	–	118,230
Reversal of minority interest					
arising on business combinations	–	–	–	–156	–156
	–	–	106,375	–156	106,219
Balance at December 31, 2006	–	–	385,043	–	385,043
Profit for the year	–	–	282,765	–	282,765
Total recognized income for the financial year					
January 1, 2007 to December 31, 2007	–	–	282,765	–	282,765
Employees share option scheme:					
– value of employee services	–	125	–	–	125
Proceeds from issue of warrants	–	–	476	–	476
Assets provided through an issue in kind (note 17)	–	–	–10,903	–	–10,903
Exercise of issued warrants	46,021	–	–46,021		–
Proceeds from new share issue,					
net of transaction costs (note 18)	–	146,351	–	–	146,351
Currency differences	–	–	97		97
	46,021	146,476	–56,351	–	136,146
Balance at December 31, 2007	46,021	146,476	611,457	–	803,954

Statement of Changes in Equity – Group

Cash flow statement – Group

(Expressed in USD thousands)	Jan 1, 2007– Dec 31, 2007	Jan 1, 2006– Dec 31, 2006
OPERATING ACTIVITES		
Result before tax	283,154	69,721
Adjustment for:		
Interest income	–1,225	–584
Interest expenses	3,709	–
Currency exchange gains	–538	–25
Depreciation	78	40
Result from financial assets at fair value through profit or loss	–158,407	–25,877
Result from investments in associated companies	–123,693	–36,031
Other non–cash items	1,127	–
Change in current receivables	–8,428	4,795
Change in current liabilities	–5,480	18,887
Net cash used in/from operating activities	–9,703	30,926
Investments in financial assets	–356,036	–395,763
Sales of financial assets	219,482	256,622
Increase of loan receivables	–9,126	–
Acquisition of group companies	–6,181	–
Interest received	1,225	2
Tax paid	–668	–
Interest paid	–1,975	–12
Net cash flow used in operating activities	–162,982	–108,225
INVESTING ACTIVITIES		
Investments in machinery and equipment	–303	–264
Sales of machinery and equipment	3	–
Net cash flow used in investing activities	–300	–264
FINANCING ACTIVITIES		
Proceeds from borrowings	49,750	–
Proceeds from new share issue	146,350	–
Transactions between Vostok Nafta and Vostok Gas	–	–11,855
Assets and liabilities provided through an owner's contribution	–10,903	118,230
Proceeds from sale of warrants	476	–
Net cash flow from financing activities	185,673	106,375
Change in cash and cash equivalents	22,391	–2,114
Cash and cash equivalents at beginning of the period	5,124	7,212
Exchange gains/losses on cash and cash equivalents	13	26
Cash and cash equivalents at end of period	27,528	5,124

Cash flow statement – Group

Key financial ratios – Group

	2007	2006
Return on capital employed, % (01)	**46.06**	**20.88**
Equity ratio, % (02)	**93.57**	**97.83**
Shareholders' equity/share, USD (03)	**17.47**	**8.37**
Earnings/share, USD (04)	**6.14**	**1.51**
Diluted earnings/share, USD (05)	**6.14**	**1.51**
Net asset value/share, USD (06)	**17.47**	**8.37**
Weighted average number of shares for the financial period	**46,020,901**	**46,020,901**
Weighted average number of shares for the financial period (fully diluted)	**46,020,901**	**46,020,901**
Number of shares at balance sheet date	**46,020,901**	**46,020,901**

The company was incorporated in 2007 and had until the utilization of the warrants in July 2007 only one share. The number of shares used for showing meaningful per share data for the periods above has been the number of shares achieved after the utilization of the warrants.

01. Return on capital employed is defined as the Group's result plus interest expenses plus/less exchange differences on financial loans divided by the average capital employed (the average total assets less non-interest bearing liabilities over the period).
02. Equity ratio is defined as shareholders' equity in relation to total assets.
03. Shareholders' equity/share USD is defined as shareholders' equity divided by total number of shares.
04. Earnings/share USD is defined as result for the period divided by average weighted number of shares for the period.
05. Diluted earnings/share USD is defined as result for the period divided by average weighted number of shares for the period calculated on a fully diluted basis.
06. Net asset value/share USD is defined as shareholders' equity divided by total number of shares.

Key financial ratios – Group

Income statement – Parent Company

(Expressed in USD thousands)	Note	Apr 5, 2007– Dec 31, 2007
Operating expenses	7	–3,464
Operating result		–3,464
Financial income and expenses		
Interest income		6,735
Interest expense		0
Currency exchange gains/losses, net		–48
Net financial items		6,687
Net result for the financial period		3,222

Income statement – Parent Company

Balance sheet – Parent Company

(Expressed in USD thousands)	Note	Dec 31, 2007
NON CURRENT ASSETS		
Financial non current assets		
Shares in subsidiaries	22	377,695
Receivables from Group companies		150,795
Total financial non current assets		528,490
CURRENT ASSETS		
Cash and cash equivalents		113
Receivables from related parties		6
Other current receivables		261
Total current assets		379
TOTAL ASSETS		528,870
SHAREHOLDERS' EQUITY (including net result for the financial period)	18	527,674
CURRENT LIABILITIES		
Non-interest bearing current liabilities		
Liabilities to group companies		188
Other liabilities		152
Accrued expenses		855
Total current liabilities		1,195
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		528,870

Balance sheet – Parent Company

Statement of Changes in Equity – Parent Company

(Expressed in USD thousands)	Share capital	Additional paid in capital	Retained earn–ings including net result for the period	Total
Profit for the period	–	–	3,222	3,222
Total recognized income for the financial period				
April 5, 2007 to December 31, 2007	–	–	3,222	3,222
Employees share option scheme:				
– value of employee services	–	125	–	125
Proceeds from issue of options	–		476	476
New share issue	0	–	–	0
Exercise of issued warrants	46,021	–	331,479	377,500
Proceeds from new share issue, net of transaction costs, note 18	–	146,351	–	146,351
	46,021	146,476	331,955	524,452
Balance at December 31, 2007	46,021	146,476	335,177	527,674

Statement of Changes in Equity – Parent Company

(Expressed in USD thousand unless indicated otherwise)

Note 1
Introduction

Vostok Nafta Investment Ltd ("Vostok Nafta", or "the Company") was incorporated in Bermuda on April 5, 2007 with corporate identity number 39861. A change of name from Vostok Nafta Holding Investment Ltd was made effective in June 2007.
The Vostok Nafta Group was formed in connection with the restructuring of the Vostok Gas Group. Vostok Nafta will continue to invest in accordance with the previous strategies of former Vostok Nafta; with a clear and sustained focus on Russia and its neighbours. However, its mandate is extended in terms of geographical areas and industrial sectors.
These group consolidated financial statements were authorised for issue by the board of directors on April 7, 2008.

Effects in the accounting of Vostok Nafta from the restructuring of Vostok Gas

During 2007 a restructuring of the Vostok Gas Ltd Group was carried out, whereby the shares in Vostok Komi (Cyprus) Ltd and its subsidiary Vostok Nafta Sverige AB were sold to a new Bermudian company; Vostok Nafta Investment Ltd. The restructuring of the Vostok Gas Group also entailed a transfer of non-Gazprom related assets to the Vostok Nafta Group and a sale of the shares in RusForest Ltd and RusForest (Cyprus) Ltd to Vostok Komi and third party.
The financial statements have been prepared as if the restructuring of Vostok Gas was carried out on September 30, 2003, and comprises the consolidated accounts of the companies that are (or would have been) included in the Vostok Nafta Group; i e Vostok Komi (Cyprus) Ltd, Vostok Nafta Sverige AB, RusForest Ltd and RusForest (Cyprus) Ltd. The restructuring of the Group further implies that items of the income statement and the balance sheet that relate to non-Gazprom assets, which formerly have been recognized in the accounts of other companies of the Vostok Gas Group, are now included in the consolidated financial statements of Vostok Nafta.
The transactions by which Vostok Nafta acquired the companies mentioned above and the non Gazprom related assets, which have been recognized in other companies of the Vostok Gas Group, comprises transactions between companies under common control. These transactions are being recognized to the same values as they were in the selling company, in accordance with the so called predecessor accounting method.
The items of the income statement that have previously been recognized in other companies of the Vostok Gas Group than in the by now completely transferred subsidiaries and which are non-Gazprom related results from financial assets at fair value through profit or loss, results from investments in associated companies, dividend income (including withholding dividend taxes) as well as non-Gazprom related operating expenses.
The items of the balance sheet that have been recognized in other companies of the Vostok Gas Group than in the by now completely transferred subsidiaries and that are non-Gazprom related long term and short term financial assets at fair value through the profit or loss, investments in associated companies, unsettled share trades, and receivables from associated companies.
The transfer of these income statement items, transferred in the format of a total for recognised income and expenses, and assets has been made to shareholders' equity, i.e. as if the transfer of non-Gazprom related income statement items and assets to Vostok Nafta was carried out by way of an owners' contribution. For further information, see Note 17.
The principal accounting policies adopted in the preparation of these financial statements are set out below.

Significant accounting policies

Accounting basis

The consolidated and the parent company financial statements are prepared in accordance with International Financial Reporting Standards, IFRS, as at December 31, 2007. The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets at fair value through profit and loss.

Standards, amendment and interpretations effective in 2007

IFRS 7, 'Financial instruments: Disclosures', and the complementary amendment to IAS 1,'Presentation of financial statements – Capital disclosures', introduces new disclosures relating to financial instruments and does not have any impact on the classification and valuation of the group's financial instruments, or the disclosures relating to taxation and trade and other payables.
IFRIC 8, 'Scope of IFRS 2', requires consideration of transactions involving the issuance of equity instruments, where the identifiable consideration received is less than the fair value of the equity instruments issued in order to establish whether or not they fall within the scope of IFRS 2. This standard does not have any impact on the group's financial statements.
IFRIC 10, 'Interim financial reporting and impairment', prohibits the impairment losses recognised in an interim period on goodwill and investments in equity instruments and in financial assets carried at cost to be reversed at a subsequent balance sheet date. This standard does not have any impact on the group's financial statements.

Standards, amendments and interpretations effective in 2007 but not relevant

The following standards, amendments and interpretations to published standards are mandatory for accounting periods beginning on or after 1 January 2007 but they are not relevant to the group's operations:
IFRS 4, 'Insurance contracts';
IFRIC 7, 'Applying the restatement approach under IAS 29, Financial reporting in hyperinflationary economies'; and
IFRIC 9, 'Re-assessment of embedded derivatives'.

Notes to the financial statements

Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the group

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the group's accounting periods beginning on or after January 1, 2008 or later periods, but the group has not early adopted them:
IAS 23 (Amendment), 'Borrowing costs' (effective from January 1, 2009). The amendment to the standard is still subject to endorsement by the European Union. It requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs will be removed. The group will apply IAS 23 (Amended) from January 1, 2009 but is currently not applicable to the group as there are no qualifying assets.
IFRS 8, 'Operating segments' (effective from January 1, 2009). IFRS 8 replaces IAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131, 'Disclosures about segments of an enterprise and related information'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes. The group will apply IFRS 8 from January 1, 2009.
IFRIC 14, 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction' (effective from January 1, 2008). This interpretation is still subject to endorsement by the EU. IFRIC 14 provides guidance on assessing the limit in IAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The group will apply IFRIC 14 from 1 January 2008, but it is not expected to have any impact on the group's accounts.

Books and accounts

The books and accounts of the Parent are maintained in USD, which is also the functional currency of the Group.

Financial period

The financial year comprises the period January 1–December 31.

Principles of consolidation

Subsidiaries

The consolidated financial statements include the accounts of the parent company and each of those companies in which it owns (directly or indirectly) shares representing more than 50 percent of the voting rights or has the sole right to exercise control over the operations.
The consolidated financial statements are prepared using the purchase method of accounting. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the net assets of the subsidiary acquired is recorded as goodwill. No goodwill was recognized in the consolidated balance sheet as of December 31, 2007 and December 31, 2006, respectively.
All inter-company profits, transactions and balances are eliminated on consolidation.

Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.
Given the nature of the business and the geographical focus of the Group, there is only one segment in the Group.

Functional currency

The functional and presentation currency of the Parent Company and its Bermudian and Cypriot subsidiaries is USD, which is also considered to be the presentational currency of the Group. Transactions in currencies other than USD are therefore translated into USD at the rate of exchange that was in effect at the transaction date.
Monetary assets and liabilities denominated in foreign currencies are translated at rates of exchange prevailing at the balance sheet date. Realized and unrealized exchange gains/losses on receivables and liabilities are reported among financial items. Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognized in profit or loss as part of the fair value gain or loss.
As at the reporting date, the assets and liabilities of subsidiaries that have note the same functional currency as the Parent Company are translated into the presentation currency of the Group at rates of exchange prevailing at the balance sheet date. Their income statements are translated at the average exchange rate for the year. The exchange differences arising on the translation are recognized as a separate component of equity.

Office equipment

Office equipment is stated at cost less accumulated depreciation. Depreciation is based on cost on a straight-line basis of estimated useful life of three and five years. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Financial Assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, and loans and receivables.

Notes to the financial statements

Financial assets at fair value through profit or loss
This category has two subcategories:
– Designated. The first includes any financial asset that is designated on initial recognition as one to be measured at fair value with fair value changes in profit or loss.
– Held for trading. The second category includes financial assets that are held for trading. All derivatives (except those designated as hedging instruments) and financial assets acquired or held for the purpose of selling in the short term or for which there is a recent pattern of short-term profit taking are held for trading.
The Group classifies all its financial assets at fair value through profit or loss in the subcategory designated.
Financial assets carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the income statement. Thereafter they are subsequently carried at fair value. Gains or losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are presented in the income statement within 'Result from financial assets at fair value through profit or loss' in the period in which they arise. Dividend income from financial assets at fair value through profit of loss is recognized in the income statement as "Dividend income" when the Group's right to receive payments is established.

Investments in associated companies
Investments where the Company has the right to exercise significant influence, which is normally the case when the Company holds between 20 percent and 50 percent, are accounted for as investments in associated companies by applying fair value. At the application of fair value, the investments are designated on initial recognition as assets to be measured at fair value with fair value changes in profit or loss. Changes in the fair value are accounted for in the income statement as "Result from associated companies".

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not traded in an active market. They are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. The Group's loans and receivables comprise 'Other short term receivables', 'Receivables from related parties' and 'Cash and cash equivalents' in the balance sheet.
Investments in loans and receivables are recognized at fair value plus transaction costs. Loans and receivables are carried at amortized cost using the effective interest method. Interest on loans and receivables using the effective interest method is recognized in the income statement as 'Interest income' among financial items.
A financial asset or group of assets is impaired, and impairment losses are recognised, only if there is objective evidence as a result of one or more events that occurred after the initial recognition of the asset. An entity is required to assess at each balance sheet date whether there is any objective evidence of impairment. If any such evidence exists, the entity is required to do a detailed impairment calculation to determine whether an impairment loss should be recognised.
The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated cash flows discounted at the financial asset's original effective interest rate. Impairment losses are recognized in the income statement as 'Other financial expenses' among financial items.
Purchases and sales of financial assets are recognized on trade-date – the date on which the Group commits to purchase or sell the asset. Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group have transferred substantially all risks and rewards of ownership.
The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models making maximum use of market inputs and relying as little as possible on entity-specific inputs.

Cash and cash equivalents
Cash and bank include cash, bank balances, and deposits held at call with banks.

Share capital
Share issue costs associated with the issuance of new equity are treated as a direct reduction of the proceeds. Buy back of own shares is, after cancellation of the shares, recorded as a reduction of the share capital with the nominal value of shares bought back, and as a reduction of the additional paid in capital with the amount paid after reduction of transaction costs for the shares in excess of the nominal value.

Borrowings
Borrowings are recognized initially at fair value, net of transaction cost incurred. Borrowings are subsequently recognized at amortised cost: any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest method. Borrowings are classified as current unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Current and deferred income tax
The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the company's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.
Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of

Notes to the financial statements

assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.
Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.
Deferred income tax is provided on temporary differences arising on investments in subsidiaries except where the timing of the reversal of the temporary difference is controlled by the group and it is probable that the temporary difference will not reverse in the foreseeable future.

Employee benefits

Pension obligations

The Group has a defined benefit pension plan, according to Swedish ITP-standards. There is a lack of information to permit the reporting of the Group's proportional share of the defined benefit commitment and of the plan assets and costs associated with this plan. Consequently, the plan is reported as if it were a defined contribution plan, which means that the expenses incurred are reported as a cost.

Share-based compensation

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognizes the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period.
The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and additional paid in capital when the options are exercised.

Revenue recognition

Revenue comprises the fair value of the consideration received in the ordinary course of the group's activities.
For investments held at both the start and end of year, the change in value consists of the difference in the market value between these dates. For investments acquired during the year, the change in value consists of the difference between cost and the market value at the end of the year. For investments sold during the year, the change in value consists of the difference between the sales price received and the value of investments at the start of the year. All changes in value are reported under the heading Result from financial assets at fair value through profit and loss.
Dividend income is recognised when the right to receive payment is established. Furthermore, dividend income is accounted for inclusive of withholding taxes. These withholding taxes are shown either as an expense in the income statement, or as a current receivable, depending on whether or not the withholding tax is refundable.
Other consideration received in the ordinary course of the group's activities is reported as "other income" in the income statement.
Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.
Unless otherwise stated, the accounting principles are unchanged compared to previous year.

Financial risk factors

The Group's activities expose it to a variety of financial risks: market risks (including currency risk and price risk), credit risk, liquidity risk and cash flow interest-rate risk.
Risk management is carried out by management under policies approved by the board of directors.

Foreign exchange risk

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, mainly with respect to the Swedish Krona (SEK), the Russian Rouble (RUB), and Euro (EUR).
At December 31, 2007, if the currency had weakened by 6% against the SEK with all other variables held constant, post-tax profit for the year would have been TUSD 14,838 (2006: 5,198) higher, mainly as a result of foreign exchange gains on translation of SEK-denominated financial assets at fair value through profit or loss. Profit is more sensitive to movement in SEK/USD exchange rates in 2007 than 2006 because of the increased amount of SEK-denominated financial assets at fair value through profit or loss.
At December 31, 2007, if the currency had weakened by 6% against the RUB with all other variables held constant, post-tax profit for the year would have been TUSD 695 (2006: no significant exposure) higher, mainly as a result of foreign exchange gains on translation of RUB-denominated long term and short term receivables.
At December 31, 2007, if the currency had weakened by 6% against the EUR with all other variables held constant, post-tax profit for the year would have been TUSD 1,233 (2006: no significant exposure) higher, mainly as a result of foreign exchange gains on translation of EUR-denominated financial assets at fair value through profit or loss.

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Price risk

The group is exposed to equity securities price risk because of investments held by the group and classified on the consolidated balance sheet as financial asset at fair value through profit or loss.

The majority of the shares in Group's share portfolio are publicly traded and included in the Russian RTS-index. During 2007 the RTS-index increased by 19.23 percent. The price risk associated with Vostok Nafta's portfolio may be illustrated by stating that a 20 percent change in the price of the quoted shares in the Group's porfolio at December 31, 2007 would have affected post-tax profit by approximately MUSD 157.23.

Credit risk

Credit risk is managed on group basis. Credit risk arises from loan receivables, short term receivables, cash and cash equivalents and deposits with banks and financial institutions. For banks and financial institutions, only independently rated parties with a minimum rating of 'A' are accepted.

The majority of financial assets are kept with Deutsche Bank (S&P long term rating (Feb 08): AA)

Liquidity risk

For the Group, prudent liquidity risk management implies maintaining sufficient cash and marketable non-pledged securities. The table below analyses the group's financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

At 31 December 2007	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
Borrowings	51,551	–	–	–

At 31 December 2006	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Over 5 years
Borrowings	–	–	–	–

Cash flow interest rate risk

Since the Group does not possess any substantial interest bearing assets, the Group's revenues and cash flow from operations are almost fully independent of changes in market interest rates. The group's interest rate risk arises from borrowings. Borrowings issued at variable rates expose the group to cash flow interest rate risk.

At December 31, 2007, if interest rates on currency-denominated borrowings had been 1% higher with all other variables held constant, the effect post-tax profit for the year would have been TUSD 333 lower, as a result of higher interest expense on floating rate borrowings. (In 2006 the Group had no cash flow interest rate risk exposure.)

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 benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

The group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including 'current and non-current borrowings' as shown in the consolidated balance sheet) less cash and cash equivalents. Total capital is calculated as 'equity' as shown in the consolidated balance sheet plus net debt.

The gearing ratio at 31 December 2007 was as follows:

	2007
Total borrowings (note 19)	50,438
Less: cash and cash equivalents (note 16)	–24,528
Net debt	25,910
Total equity	803,954
Total capital	829,864
Gearing ratio	3%

Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the group is the current bid price.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. In September 2005, Vostok Nafta initiated legal action against Sakhatransneftegaz, a company owned and controlled by the Government of the Republic of Sakha (Yakutia), in the Moscow

Arbitration court for non-payment of MRUB 189.58, following the Vostok Nafta's sale of approximately 2 million shares in OAO Sakhaneftegaz. The value of the receivable has subsequently been remeasured at the share's ask price, reflecting the company's possibility of repurchasing the shares. During 2007 a court decision was issued, which allow Vostok Nafta to recover MRUB 208.54 of the outstanding receivable (including accrued interest). As at December 31, 2007 it was still uncertain to which degree the receivable was actually recoverable. Therefore, as at December 31, 2007, the recognized value of the receivble was estimated to MUSD 4.57 (2006: MUSD 6.75).

Note 2
General

Incorporation and legal structure

Vostok Nafta Investment Ltd (the Company or the Parent Company) is an investment company with its focus on portfolio investments mainly in the CIS-country block. The Company was incorporated in Bermuda on April 5, 2007, as a tax exempted limited liability company. The Swedish Depository Receipts of Vostok Nafta (SDB) are listed on the OMX Nordic Exchange Stockholm, Mid Cap segment. Ticker: VNIL SDB.
As at December 31,2007 the Vostok Nafta group (the Group) consists of a Bermudian parent company, Vostok Nafta Investment Ltd, one wholly owned Bermudian subsidiary, Vostok Holding Limited, one wholly owned Cypriot subsidiary; Vostok Komi (Cyprus) Ltd, one Swedish subsidiary; Vostok Nafta Sverige AB, and one wholly owned Russian subsidiary, OOO Resursniye Investitsii.
Vostok Komi (Cyprus) Limited was incorporated in Cyprus on September 21, 2000 as a private limited liability company with offshore status. During 2007 Vostok Komi established a representative office in Moscow. Vostok Nafta Sverige AB was incorporated in Sweden as a private limited liability company in 2005. Vostok Nafta Sverige AB's registrered office is at Hovslagargatan 5, 111 48 Stockholm, Sweden.
During 2007, Vostok Komi (Cyprus) Ltd has acquired a Russian subsidiary; OOO Resursniye Investitsii. See also note 25 below.
In November 2007, the Company formed a new Bermudian subsidiary, Vostok Holding Ltd.
The registered office of the Company is in Hamilton, Bermuda (Codan Services Ltd, 2 Church Street, P.O Box HM 666, Hamilton, Bermuda).

Note 3
Result from financial assets at fair value through profit or loss

During 2006 and 2007, result from financial assets at fair value through profit or loss comprises the result from fair value changes of financial assets that have been designated on initial recognition as assets to be measured at fair value with fair value changes in profit or loss.

Note 4
Result from investments in associated companies

During 2006 and 2007 result from associated companies comprises the result from fair value changes of financial assets that have been designated on initial recognition as assets to be measured at fair value with fair value changes in profit or loss.

Note 5
Dividend income

	Group 2007	Group 2006
Dividend income, net of tax, recognized in the income statement	**8,588**	**10,644**
whereof unsettled at balance sheet date	**–**	**–**
Net proceeds from dividends, net of tax, recognized in the income statement during the year	**8,588**	**10,644**

Note 6
Other operating income

	Group Jan 1, 2007– Dec 31, 2007	Group Jan 1, 2006– Dec 31, 2006
Management fee charged to Vostok Gas (note 24)	**268**	**–**
Interest income (note 14)	**57**	**–**
Total	**325**	**–**

Note 7
Operating expenses by nature

	Group Jan 1, 2007– Dec 31, 2007	Group Jan 1, 2006– Dec 31, 2006	Parent Company Apr 5, 2007– Dec 31, 2007
Employee benefit expense (Note 23)	2,764	913	607
Depreciation and write down of office equipment	78	40	–
Operating lease expenses	227	88	101
Other expenses	2,635	2,400	2,756
Total operating expenses	5,704	3,441	3,464

Lease rentals amounting to TUSD 227 (2006: 88) relating to rent of office space in Stockholm, Moscow and London are included in the income statement.

Note 8
Tax

Corporate income tax – general

The parent company, Vostok Nafta Investment Ltd, and its Bermudian subsidiary Vostok Holding Ltd, are exempted and therefore not liable for tax in Bermuda.

Vostok Komi (Cyprus) Limited, is subject to Cypriot corporate tax on taxable profits at the rate of 10%. Under certain conditions interest may be subject to defence contribution at the rate of 10%. In such cases 50% of the same interest will be exempt from corporation tax thus having an effective tax rate burden of approximately 15%. Any gains from disposal of qualified securities are not subject to corporate tax in Cyprus. In certain cases, however, dividends received from abroad may be subject to defence contribution at a rate of 15%.
The Russian subsidiary's profits are subject to Russian income tax at the rate of 24%.
The Swedish subsidiary's profits are subject to Swedish income tax at the rate of 28%.

Income tax expense

	Jan 1, 2007– Dec 31, 2007	Jan 1, 2006– Dec 31, 2006
Current tax	–184	–77
Deferred tax	–205	–11
Taxation	–389	–88

The tax on the Group's result before tax differs from the theoretical amount that would arise using the tax rate of the countries where the Group operates as follows:

	Jan 1, 2007– Dec 31,2007	Jan 1, 2006– Dec 31,2006
Result before tax	283,154	69,721
Tax parent company (0%)	–	–
Expected tax Cyprus (10%)	–27,959	–7,045
Expected tax Russia (24%)	–114	–
Expected tax Sweden (28%)	34	–237
Expected tax, total	–28,039	–7,282
Income not subject to income tax	29,103	7,738
Expenses not deductible	–1,316	–541
Tax losses for which no deferred income tax was recognized	–	–3
Prior year adjustments	–137	–
Taxation	–389	–88

Deferred tax

	Group Dec 31, 2007	Group Dec 31, 2006
Deferred tax liabilities relating to		
– untaxed reserves	**21**	**11**
– unrealized gains on financial assets att fair value through profit or loss	**1,337**	**–**
Total	**1,358**	**11**

The gross movement on the deferred income tax account is as follows:

	Jan 1, 2007– Dec 31, 2007	Jan 1, 2006– Dec 31, 2006
Beginning of the year	**11**	**–**
Acquired deferred tax liability	**1,147**	**–**
Charged to income statement	**205**	**11**
Currency translation differences	**–5**	**–**
End of the year	**1,358**	**11**

Note 9
Earnings per share

Basic earnings per share have been calculated by dividing the net result for the financial year by the weighted average number of shares in issue during the year.
Diluted earnings per share have been calculated by dividing the net result for the financial year by the adjusted weighted average number of ordinary shares outstanding to assume conversion of all dilutive ordinary shares. Share options are the only category of dilutive potential ordinary shares for the company. For the share options, a calculation is made in order to determine the number of shares that would have been acquired at fair value (determined as the average annual market share price of the Company's shares) based on the monetary value of the subscription rights to outstanding share options. The number of shares calculated as above is compared with the number of shares that would have been issued assuming the exercise of the options.
Until the warrants in Vostok Nafta were exercised in July 2007, the Company had only one share. In order to provide meaningful data per share for the entire periods, the number of shares has been the number of shares achieved after the exercise of the warrants.

	Dec 31, 2007	Dec 31, 2006
Profit attributable to the equity holders of the company	**282,765**	**69,633**
Weighted average number of ordinary shares on issue	**46,020,901**	**46,020,901**
Earnings per share, basic	**6.14**	**1.51**
Adjustment for dilution effect of incentive options	**–**	**–**
Weighted average number of ordinary shares for diluted earnings per share	**46,020,901**	**46,020,901**
Earnings per share, diluted	**6.14**	**1.51**

Note 10
Office equipment

	Group Dec 31, 2007	Group Dec 31,2006
Opening cost	361	97
Additions	303	264
Disposals	–3	
Exchange differences	59	–
Closing cost	720	361
Opening accumulated depreciation	–45	–5
Depreciation for the financial period	–119	–40
Exchange differences	–10	
Closing accumulated depreciation	–174	–45
Net book value as at year end	545	316

Depreciations amounting to net –78 (–40) for the Vostok Nafta Group are recognized among operating expenses in the income statement (see also note 7).

Note 11
Financial instruments by category

The accounting policies for financial instruments have been applied to the line items below:

December 31, 2007 – Group

Assets as per balance sheet	Loans and receivables	Assets at fair value through the profit and loss – designated	Total
Financial assets at fair value through profit or loss	–	565,043	565,043
Investments in associates	–	248,413	248,413
Loan receivables	9,138	–	9,138
Cash and cash equivalents	27,528	–	27,528
Total	36,666	813,256	849,922

Liabilities as per balance sheet	Other financial liabilities	Total
Borrowings	50,438	50,438
Total	50,438	50,438

December 31, 2006 – Group

Assets as per balance sheet	Loans and receivables	Assets at fair value through the profit and loss – designated	Total
Financial assets at fair value through profit or loss	–	292,515	292,515
Investments in associates	–	94,667	94,667
Cash and cash equivalents	5,124	–	5,124
Total	5,124	387,182	392,306

Liabilities as per balance sheet		Other financial liabilities	Total
Borrowings	–	–	–
Total	–	–	–

Note 12
Non-current financial assets at fair value through profit or loss

	Group Dec 31, 2007	Group Dec 31, 2006
Beginning of the year	292,515	178,491
Additions	331,406	342,197
Proceeds from disposals	–217,285	–254,050
Change in fair value	158,407	25,877
End of the year	565,043	292,515

	Number of shares held, Dec 31, 2007	Fair value (USD), Dec 31, 2007	Ownership share, %	Number of shares held, Dec 31, 2006	Fair value (USD), Dec 31, 2006	Ownership share, %
GROUP						
Alchevsk Steel	–	–	–	160,652,377	7,510,499	1.49%
Alrosa Co Ltd	966	27,048,000	0.48%	–	–	–
Armada	161,952	3,320,016	1.35%	–	–	–
Bashneft Pref	1,000,000	10,750,000	2.89%	–	–	–
Belon	929,700	74,376,000	8.08%	919,700	33,339,125	9.20%
Caspian Services Inc.	233,250	758,063	0.46%	233,250	886,350	0.55%
Centerenergo	–	–	–	500,000	658,750	0.07%
Dagestan Regional	72,500,000	13,775,000	1.38%	–	–	–
Dakor	272,107	7,282,400	4.79%	–	–	–
European Minerals WTS	–	–	5.06%	3,400,000	–	–
Gaisky GOK	31,274	21,266,320	5.06%	30,114	15,358,140	4.88%
Gazprom Neft ADR	488,000	10,248,000	0.05%	–	–	–
Gornozavodsk Cement	39,000	23,400,000	5.03%	39,000	13,143,000	5.03%
Kamkabel	1,600,000	8,112,000	4.12%	800,000	1,680,000	3.99%
Kemerovo Azot	375,000	13,968,750	5.51%	–	–	–
Kherson Oil Refinery	5,789,903	283,705	4.40%	5,156,903	2,052,447	3.92%
Kuzbassrazrezugol	231,434,053	99,053,775	3.79%	70,005,000	30,452,175	1.15%
Kyrgyzenergo	2,618,241	168,688	0.27%	2,618,241	44,510	0.27%
Luganskteplovoz	–	–	–	10,578,336	4,691,492	4.83%
Mechel ADR	–	–	–	493,700	12,539,980	0.12%
Orsk Refinery Ord	2,025	70,875	0.06%	2,025	50,625	0.06%
Orsk Refinery Pref	538	15,979	0.05%	538	13,450	0.05%
Poltava GOK GDR	1,516,055	22,831,788	1.08%	1,516,055	15,160,550	1.31%
Priargunsky Industrial Ord	9,000	4,635,000	0.53%	–	–	–
Priargunsky Industrial Pref	1,200	384,000	0.29%	–	–	–
Raspadskaya	–	–	–	11,000,000	20,295,000	1.41%
Rosneft Oil Co	–	–	–	3,415,583	31,252,584	0.04%
Sayano Shushenskaya	300,000	540,000	0.02%	–	–	–
Shalkiya Zinc	275,000	1,100,000	0.49%	–	–	–
Sibirski Cement	151,000	25,670,000	0.50%	–	–	–
Sistema	2,000,000	3,280,000	0.02%	–	–	–
Tatneft ADR	27,800	3,336,000	0.03%	–	–	–
Tatneft Pref	1,200,000	4,320,000	0.81%	–	–	–
Tinkoff Credit Systems WTS	–	2,000,000	2.00%	–	–	–

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	Number of shares held, Dec 31, 2007	Fair value (USD), Dec 31, 2007	Ownership share, %	Number of shares held, Dec 31, 2006	Fair value (USD), Dec 31, 2006	Ownership share, %
TNK–BP Holding Ord	–	–	–	326,448	829,178	0.00%
TNK–BP Holding Pref	45,468,616	85,026,312	10.10%	38,712,416	89,038,557	8.60%
Transneft Pref	9,378	18,568,440	0.60%	–	–	–
Tuimazy Concrete Mixers	1,200,000	19,800,000	14.60%	–	–	–
Uchalinsky GOK	1,124,045	21,356,855	2.95%	397,317	5,761,097	1.04%
Waymore Holding Ltd	523,800	11,720,549	5.82%	–	–	–
Volzhskaya GES	20,903,442	20,276,339	0.71%	–	–	–
Yakutgazprom	100,000	15,000	0.01%	100,000	25,000	0.05%
Yuzhni Kuzbass	–	–	–	271,312	7,732,392	0.57%
Zeiskaya GES Pref	12,570,000	6,285,000	5.54%	–	–	–
Total non current financial assets						
at fair value through profit or loss, Group		565,042,852			292,514,901	

On December 21, 2007, Vostok Nafta has entered into a syndicated term loan arrangement with Tinkoff Credit Systems, whereby Vostok Nafta commited to provide RUB 500 million and at the same time became entitled to warrants representing slightly below 2% of TCS's equity. The fair value of the warrants, which were designated on initial recognition as a financial asset to be measured at fair value with fair value changes in profit or loss, was, both as at the date of acquisition and as at December 31, 2007, USD 2,000,000.

Risk factors in Russia

The economy of the Russian Federation continues to display characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible outside of the country; a low level of liquidity in the public and private debt and equity markets; and relatively high inflation. Exchange restrictions and controls exist relating to converting Russian Roubles into other currencies. These factors must be understood and taken into consideration by Vostok Nafta and Russian investors in general. Since Vostok Nafta has the bulk of its assets invested in Russia, the shareholders of Vostok Nafta also need to be aware of these risks.
Operations on the Russian securities market are affected by its underdeveloped infrastructure, particularly the stage of development of its registration and settlement systems and the current status of the developing regulatory and legal framework in Russia. The political stabilization beginning in 2000 and continuing into 2007 has been a positive contributing factor for the further development of the political and legal environment.
The prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory and political developments, which are beyond the Company's control.
Given the risks outlined above, any decision to invest in Vostok Nafta shares should be taken only after careful consideration.

Note 13
Investment in associated companies

	Dec 31, 2007	Dec 31, 2006
Beginning of the year	94,667	6,647
Additions	32,051	53,566
Proceeds from disposals	–2,198	–1,577
Change in fair value or share of income	123,693	36,031
End of the year	248,213	94,667

The shares specified below are investments in associated companies. Black Earth Farming Ltd, Kontakt East Holding AB and Systemseparation AB are listed companies; hence, the fair value option is applied for the value assessment of these investments. RusForest Ltd is still unlisted and in the process of adapting to requirements placed on publicly listed companies, why the investment is recognized at acquisition cost as this at balance sheet date is estimated to correspond to fair value.

Name 2007	Number of shares held	Interest held, percent	Fair value	Revenues	Profit/ loss	Assets	Liabilities
Black Earth Farming Ltd	26,715,404	21.5	206,510	21,256	–21,505	490,127	92,328
Kontakt East Holding AB	4,410,000	31.8	18,659	19,918	–5,555	51,059	17,311
RusForest Ltd*	11,004,813	50.0	21,521	54,402	1,156	53,409	32,886
Systemseparation AB	6,167,161	20.5	1,523	3,036	–1,390	6,339	1,086

Name 2006	Number of shares held	Interest held, percent	Fair value	Revenues	Profit/ loss	Assets	Liabilities
Black Earth Farming Ltd	23,460,000	30.6	63,362	501	–8,371	123,860	1,211
Kontakt East Holding AB	2,940,000	35.0	17,598	10,859	–1,291	25,349	5,706
RusForest Group							
of Companies*	–	40.0	11,414	32,988	–66	26,868	13,424
Systemseparation AB	5,926,991	19.5	2,293	1,723	–2,863	7,263	974

*During 2007 a restructuring of the RusForest group was carried out, whereby Vostok Gas sold 100% of the shares in RusForest Ltd to Vostok Nafta (50%) and Varyag Capital Ltd (50%). From Vostok Gas, RusForest Ltd acquired 100% of the shares in Rus-Forest (Cyprus) Ltd, which in turn acquired the shares in the Russian forestry companies, in which Vostok Nafta and Varyag Capital Ltd held a 40% stake each. Following the restructuring, Vostok Nafta still holds, however indirectly, a 40% ownership share of the Russian forestry companies.

In the table above revenues, profits/losses, assets and liabilities of RusForest Ltd and RusForest Group of companies are the aggregated revenues, profits/losses, assets and liabilities of the Russian forestry companies, which were included in the Rus-Forest Ltd Group and RusForest Group of companies as at December 31, 2007 and December 31, 2006, respectively, The financial information has been gathered from the companies' financial reports which have been prepared according to Russian Accounting Standards.

Note 14
Loan receivables

	Dec 31, 2007	Dec 31, 2006
Beginning of the year	–	–
Additions	9,126	–
Interest income	57	
Exchange differences	–45	–
End of the year	9,138	–

Counterparty	Credit rating Dec 31, 2007	Nominal value Dec 31, 2007	Nominal value Dec 31, 2006	Carrying value Dec 31, 2007	Carrying value Dec 31, 2006	Terms of interest	Maturity
Tinkoff Credit Systems	–	6,151	–	6,208	–	16.50/18.50%	Dec, 2009
Murrayföretagen AB	2*	2,930	–	2,930	–	10%	Dec, 2007

* The credit rating is according to the credit rating system of UC AB. After the end of the period, the credit rating was changed to 'K', following the bankruptcy of Murrayföretagen AB. As at the date of the issue of the Annual Report, the effect of the bankruptcy on the value of the loan to Murrayföretagen AB was not known.

In December 2007, Vostok Nafta has entered into a syndicated term loan arrangement with Closed Joint Stock Company Tinkoff Credit Systems Bank (TCS), whereby Vostok Nafta commited to provide a total of RUB 500 million, of which RUB 201 million has been transferred to the counterparty as at December 31, 2007. Through the agreement Vostok Nafta also became entitled to warrants representing slightly below 2% of TCS's equity. The warrants were at inception recognized as financial assets through profit or loss with a fair value of TUSD 2,000, which reduced the carrying value of outstanding loans. The loan carries an interest rate, which is fixed to 16.50% for the first year and 18.50% for the second year up to maturity. Interest income on the loan is being recognized in the income statement over the maturity of the loan, using the effective interest method. During 2007, interest income in relation to the loan has been recognized in the amount of TUSD 57.

Note 15
Other current receivables

	Group Dec 31, 2007	Group Dec 31, 2006	Parent Company Dec 31, 2007
Prepayments and accrued income	125	93	16
Sundry debtors	476	45	245
Total	601	138	261

Note 16
Cash and cash equivalents

Cash, cash equivalents and bank overdrafts include the following for the purposes of the cash flow statement:

	Group Dec 31, 2007	Group Dec 31, 2006
Cash and bank	27,528	5,124
Total	27,528	5,124

Note 17
Shareholders' equity

The transactions by which Vostok Nafta acquired non-Gazprom related assets, which have been recognized in companies of the Vostok Gas Group, comprise transactions between companies under common control. These transactions are being recognized at the same values as reported by the selling company, in accordance with the so called predecessor accounting method. The items of the income statement that have previously been recognized in other companies of the Vostok Gas Group than in the by now completely transferred subsidiaries and which are non-Gazprom related realized and unrealized profits and losses from financial assets at fair value through profit of loss, results from investments in associated companies, dividend income (including withholding dividend taxes) as well as non-Gazprom related operating expenses.
The items of the balance sheet that have been recognized in other companies of the Vostok Gas Group than in the by now completely transferred subsidiaries and that are non-Gazprom related long term and short term financial assets at fair value through the profit or loss, investments in associated companies, unsettled share trades, receivables from associated companies and cash and cash equivalents.
The transfer of these income statement items, transferred in the format of a total for recognised income and expenses, and assets has been made to shareholders' equity, i.e. as if the transfer of non-Gazprom related income statement items and assets to Vostok Nafta was carried out by way of an owners' contribution.
In other words, the item "Assets and liabilities provided through owners' contribution" includes the net assets transferred to Vostok Nafta which had not been reported in Vostok Nafta's income statement and which is primarily comprised of net investments in financial assets, unpaid dividends (net after coupon tax), changes in unpaid share transactions and unpaid administration expenses.

	Total	2007	2006	2005	2004	2003
Income statement items						
Result from financial assets at fair						
value through profit or loss and						
from associated companies	222,973	–748	61,909	126,066	35,746	–
Dividend income, net of tax	22,128	5,057	10,644	4,035	2,392	–
Operating expenses	–10,944	–733	–3,434	–3,561	–3,216	–
Total income statement items	234,157	3,576	69,119	126,540	34,923	–
Assets and liabilities provided						
through owners' contribution						
Net investments in financial assets	157,964	–15,720	139,141	–39,401	3,863	70,081
Unpaid dividends						
(net after coupon tax)	–22,128	–5,057	–10,644	–4,035	–2,392	–
Changes in unpaid share transactions	–3,437	9,411	–12,933	3,278	–3,193	–
Unpaid administration expenses	10,863	733	3,435	3,479	3,216	–
Other	81	–270	–769	1,120	–	–
Total Assets and liabilities provided						
through owners' contribution	143,343	–10,903	118,230	–35,559	1,494	70,081
Total	377,500					

Note 18
Share capital and additional paid in capital

Parent Company	Number of shares held	Share capital	Additional paid in capital
At incorporation of the company, Apr 5, 2007	1	0	–
Employees share option scheme:			
– value of employee services			125
Exercise of issued warrants	46,020,900	46,021	–
Proceeds from new share issue, net of transaction costs	–	–	146,351
At December 31, 2007	46,020,901	46,021	146,476

The total authorized share capital is USD 100,000,000. As at December 31, 2007, 46,020,901 shares have been issued and fully paid. As at the same date, the number of outstanding shares was 46,020,901 at a par value of USD 1 each. Transaction costs for shares issued during the period April 5, 2007–December 31, 2007, was TUSD 4,052, which has been deducted from shareholders' equity. Additional paid in capital is defined as the difference between the net proceeds from the issue of share capital and the par value of that share capital. Each ordinary share carries one vote.
There are currently 710,000 ordinary shares available under the employee share option scheme. Each option entitles the holder to one new share (SDR) in Vostok Nafta Investment Ltd. For more information on the options, please see Note 23.

Note 19
Borrowings

Current	Group Dec 31, 2007	Group Dec 31, 2006
Bank borrowings	50,438	–

Specification of bank borrowings (TUSD)	Credit facility as per Dec 31, 2007	Utilized credit facility as per Dec 31, 2007	Unutilized amount as per Dec 31, 2007		Terms of interest
Lender					
Deutsche Bank	50,000	50,000	–	May 2008	LIBOR+200 bps
Total bank borrowings	50,000	50,000	–		

Transaction costs in the amount of TUSD 250 will be released to the income statement over the period of the borrowings using the effective interest method. As at December 31, 2007, fair value of the borrowings amounted to TUSD 49,931 (2006: –).

At the same date, accrued interest on the borrowings amounted to TUSD 507 (2006: –). The carrying amount of the Group's current borrowings approximate their fair value.
Assets pledged for the borrowings; see note 21.

Note 20
Other current liabilities

	Group Dec 31, 2007	Group Dec 31, 2006	Parent Company Dec 31, 2007
Other current liabilities	141	27	152
Total	141	27	152

Note 21
Pledged assets

As per December 31, 2007, assets are pledged as collateral for the bank borrowings amounting to TUSD 50,000. The assets pledged are the listed shares in the share portfolio.

Total pledged assets represent a fair value of MUSD 895.90 (2006: –).
Neither the Group nor the Company had any contingent liabilities as per December 31, 2007.
Neither the Group nor the Company had any contingent liabilities or assets pledged as per December 31, 2006.

Note 22
Shares in subsidiaries

Parent Company	Country	Number of shares	Nominal value of ordinary share capital In issue, USD	Share of capital and votes, %	Book value Dec 31, 2007, TUSD
Vostok Komi (Cyprus) Ltd	Cyprus	150,000	150,000	100	377,685
Vostok Holding Ltd	Bermuda	10,000	10,000	100	10
Total					377,695

All the companies are included in the consolidated financial statements from the time of acquisition. The difference between the cost and the market value of the physical net assets acquired has been capitalized according to the accounting principles of the group.

Note 23
Employee benefit expense

	Group Jan 1, 2007– Dec 31, 2007	Group Jan 1, 2006– Dec 31, 2006	Parent Company Apr 5, 2007– Dec 31, 2007
Wages and salaries	2,093	691	436
Social security costs	446	186	44
Share based compensations	125	–	125
Pensions costs	60	31	–
Other employee benefit expenses	40	4	3
Total employee benefit expense	2,764	913	608

Staff costs

	Group Jan 1, 2007– Dec 31, 2007	Group Jan 1, 2006– Dec 31, 2006	Parent Company Apr 5, 2007– Dec 31, 2007
Salaries and other remunerations to the management and the board of directors of the parent and its subsidiaries*	1,519	375	424
Salaries to other employees	759	316	137
Total salaries	2,278	691	561

* Decisions regarding remuneration to managers are made by the company's compensation committee made up of three of the board members. The managing director has the right to 12 months salary in the event of the termination of appointment on part of the company. He must himself observe 6 months notice of termination. The rest of the management has a notice period of one month, which also applies to the company in the event of termination on part of the company. No notice period applies to the Board of Directors. The average number of persons employed by the Group, excluding members of the Board of Directors, during the year was 9 (10), of which 6 were men (9).

Group, 2007	Base salaries/ board fees	Variable compensation	Other benefits	Pension expenses	Share based compensations	Other remunerations	Total
Lukas H Lundin	76	–	–	–	–	23	99
Al Breach	29	–	–	–	–	–	29
Paul Leander Engström	41	–	–	–	–	–	41
Torun Litzén	43	–	–	–	–	–	43
Ian H Lundin	43	–	–	–	–	–	43
Wiliam A Rand	50	–	–	–	–	–	50
Robert J Sali	34	–	–	–	–	–	34
Fabienne Pfyffer	–	–	–	–	3	–	3
Per Brilioth	294	506	–	51	–	–	851
Other management (2 persons)	213	61	–	9	43	–	326
	823	567	–	60	46	23	1,519

Notes to the financial statements

Parent Company, 2007	Base salaries/ board fees	Variable compensation	Other benefits	Pension expenses	Share based compensations	Other remunerations	Total
Lukas H Lundin	76	–	–	–	–	–	76
Al Breach	29	–	–	–	–	–	29
Paul Leander Engström	41	–	–	–	–	–	41
Torun Litzén	43	–	–	–	–	–	43
Ian H Lundin	43	–	–	–	–	–	43
Wiliam A Rand	50	–	–	–	–	–	50
Robert J Sali	34	–	–	–	–	–	34
Fabienne Pfyffer	–	–	–	–	3	–	3
Other management							
(1 person)	62	–	–	–	43	–	105
	378	–	–	–	46	–	424

1. No termination or post-employment benefits have been paid out during the year.
2. The managing director has a pension plan according to Swedish ITP standards. There is a lack of information to permit the reporting of the Group's proportional share of the defined benefit commitment and of the plan assets and costs associated with this plan. Consequently, the plan is reported as if it were a defined contribution plan, which means that the expenses incurred are reported as a cost. The pension is not tied to the managing director's employment and is based on the managing director's base salary.

Incentive programme

The Extra General Meeting held on August 29, 2007 decided in accordance with the proposal from the Board of Directors to adopt an incentive programme in Vostok Nafta Investment Ltd which entitles present and future employees to be allocated call options, which entitle the holder to acquire shares represented by Swedish Depository Receipts in Vostok Nafta Investment Ltd.

The incentive programme shall be governed by the following terms and conditions:

– The exercise price for the options shall correspond to 120 percent of the market value of the Swedish Depository Receipts at the time of the granting of the options.

– The options may be exercised not earlier than two years and not later than three years from the time of the granting.

– For employees resident outside of Sweden the following conditions shall apply. No premium shall be paid for the options and the options may only be exercised if the option holder at the time of exercise is still employed within the group. If an option holder ceases to be an employee of or, as the case may be, consultant to any member of the Group for any of the reasons set out below, then his or her options will not lapse but may be exercised to the extent notified to the option holder on the date of grant provided all applicable performance conditions being relevant at date of cessation are satisfied or waived. The reasons are; ill-health, injury, and disability; retirement; early retirement by written agreement with the option holder's employer; his or her employing company ceasing to be under the control of the Company, or, as a result of a transfer of the undertaking in which the option holder works, transfer to a company which is neither under the control of the Company nor a member of the Group; any other reason specified by the Directors in their absolute discretion.

– For employees resident in Sweden the following conditions shall apply. The options are offered to a purchase price corresponding to the market value of the options at the time of the offer. The options shall be fully transferable and will hereby be considered as securities. Among other things this entails that the options are not contingent upon employment and will not lapse should the employee leave his or her position within the group.

– Options may be issued by Vostok Nafta Investment Ltd or by other group companies.

Preparation and administration

The Board of Directors, or a designated committee appointed by the Board of Directors, shall be authorised to determine the detailed terms and conditions for the incentive scheme in accordance with the approved principal conditions and guidelines. The Board of Directors may in connection thereto make necessary adjustments to satisfy certain regulations or market conditions abroad. The Board of Directors shall also be authorised to resolve on other adjustments in conjunction with material changes affecting the group or its business environment, which would mean that the authorised conditions for the incentive scheme would no longer be appropriate.

Allocation

The incentive scheme is proposed to include granting of not more than 1 million options. Allocation of options to the Managing Director shall not exceed 500,000 options and allocation to

each member of the executive management or to other key employees shall not exceed 200,000 options.
The allocation of options shall be decided by the Board of Directors, or by the Compensation Committee, whereby inter alia the performance of the employee and his or her importance to the group will be considered. In connection with allocation of options to employees resident outside of Sweden as well as resident in Sweden, the following criteria shall inter alia be considered: the employee's ability to manage and develop the existing portfolio, identify new investment opportunities and evaluate conditions of new investments, and also return on capital or estimated return on capital in various object of investments. The employees will not initially be offered the maximum allocation of options and a performance related allocation system will be maintained since allocation of additional options within the mandate given by the general meeting will require fulfilment of stipulated requirements and targets. The Compensation Committee shall be responsible for the evaluation of the performance of the employees. The outcome of stipulated targets shall, if possible, be reported on afterwards.
Directors who are not employed by the group shall not be able to participate in the scheme.

Possible future bonus for employees resident in Sweden

In order to stimulate the participation in the scheme, the company has the intention to arrange for a subsidy in the form of a bonus payment which after tax corresponds to the option premium. Half of the bonus is intended to be paid in connection with the purchase of the options and the remaining half in connection with the exercise of the options. The latter bonus payment is subject to the requirement that the holder is still an employee of the group at the time of exercise of the options. If the options are not exercised, the latter bonus payment will not be paid. For employees in Sweden, the participation in the scheme will thus include a risk-taking element.

Purpose

The purpose of the proposed incentive scheme is to create conditions to retain and recruit competent employees to the group as well as promote long-term interests of the company by offering its employees the opportunity to participate in any favourable developments in the value of the Company. The Board of Directors is of the opinion that the adoption of an incentive scheme is particularly justified as a consequence of employees of the Company not being subject to any variable bonus scheme.
On August 30, 2007 it was decided to issue 710,000 of the authorized 1,000,000 options under the company's incentive program to a group of employees.

Personnel options	Issued 2007*	Total Dec 31, 2007
Management		
Managing Director	**250,000**	**250,000**
Sergei Glaser	**150,000**	**150,000**
Anders Sjöberg	**30,000**	**30,000**
Other	**280,000**	**280,000**
Total	**710,000**	**710,000**
Strike price, SEK	**84.66**	
Market value per issue at the time of issue, SEK**	**11.34**	
Maturity	**August 30, 2007–**	
	August 30, 2010	

* The strike price for the options has been calculated as 120% of the average last paid of the ten trading days leading up to the day of issue in line with the rules of Vostok Nafta's Option plan.
** The market value of the options issued in 2006 has been calculated with the help of the Black & Scholes options valuation model. The significant inputs into the model were share price at the grant date; exercise price shown above; standard deviation of expected share price returns, based on an analysis of historical share prices; option life disclosed above; and Swedish market interest rate at the grant date.

Notes to the financial statements

Movements in the number of share options outstanding and their weighted average prices are as follows:

	Average exercise price in SEK/share	Options Dec 31, 2007	Options Dec 31, 2006
At opening balance day	–	–	–
Granted	84.66	710,000	–
Forfeited	–	–	–
Exercised	–	–	–
At closing balance day	84.66	710,000	–

Out of the 710,000 options (2006: –) no options (2006: –) were exercisable.

Share options outstanding at the end of the year have the following expiry date and exercise prices:

	Exercise price, SEK	Share options 2007	Share options 2006
August 30, 2010	84.66	710,000	–
At the end of the financial year		710,000	–

Note 24
Transactions with related parties

During the fiscal year the Group has participated in transactions with the following main groups of related entities:
– Vostok Gas Ltd Group (VGAS): In connection with the Restructuring of Vostok Gas, assets for a total amount of USD 377.5 million were provided to Vostok Nafta. Payment for the provided assets was made by way of a promissory note to Austro, amounting to USD 377.5 million. Interest income from the note, which carried an interest rate of 9 %, amounted to USD 1.2 million. Thereafter, Vostok Gas purchased 46,020,900 Warrants from Vostok Nafta for the corresponding amount. Payment for the acquired Warrants was made by way of a promissory note to Vostok Nafta, by which Vostok Nafta thus had a receivable from Vostok Gas in the amount of USD 377.5 million. This receivable was used for the subsequent settlement of the liability to Vostok Gas. In addition to the transferred assets, Vostok Gas has sold Vostok Komi (Cyprus) Ltd and its subsidiary Vostok Nafta Sverige AB to Vostok Nafta for a total consideration of TUSD 185. Other transactions with Vostok Gas are specified below.
– The Lundin family and the Lundin group. Members of the Lundin family – late Adolf H Lundin (AHL), Lukas H Lundin (LHL) and Ian H Lundin (IHL) – have actively participated in the management of the company and have received remuneration for their provided services.
– Management and directors; see note 23.
– Associated companies; Black Earth Farming Ltd, Kontakt East Holding AB, RusForest Ltd (and subsidiaries).
– Key personnel and companies owned by key personnel of the Company.

Major related party transactions have been:

Income, TUSD	2007	2006
Management fees provided to Vostok Gas Ltd during April and May 2007	268	–
Office rental income, associated companies	90	6
Interest income on loans to associated companies	36	58
Interest income on loans to key personnel and companies owned by key personnel	8	2

Notes to the financial statements

Expenses for shared services have during 2007 been charged to Vostok Gas in the amount of TUSD 231 (2006: –).

Expenses, TUSD	2007	2006
Management fees AHL	–	142
Management fees LHL	23	90
Management fees IHL	–	8
Board fees LHL	76	2
Board fees IHL	43	2
Management services, key personnel in associated companies	55	12

Receivables and liabilities, TUSD	2007	2006
Receivables from Vostok Gas	–	340
Receivables from associated companies	3,777	271
Receivables from key personnel in associated companies	674	–
Receivables from companies owned by key personnel of the company	447	–
Liabilities to Vostok Gas	586	–

Note 25
Business combinations

During the period Vostok Komi (Cyprus) Ltd has acquired 100% of the participatory interest in OOO Resursniye Investitsii. Date of acquisition was July 3, 2007 and total consideration amounted to TUSD 6,181, which was entirely paid in cash. The acquired business has contributed with TUSD 279 to the Group's net profit for the period from July 3, 2007 to December 31, 2007. If the acquisition had occurred on January 1, 2007 the Group's post tax profits would have been TUSD 284,982. These accounts have been calculated using the Group's accounting policies and by adjusting the result of the subsidiary the reflect the fair value adjustments tio financial assets had applied from January 1, 2007, together with consequential tax effects.

The assets and liabilities as of July 3, 2007 arising from the acquisition are as follows:

	Fair value	Carrying value
Financial assets valued at fair value via the income statement	7,333	2,555
Other assets	3	3
Deferred tax liability	–1,147	–
Other liabilities	–8	–8
Net assets	6,181	2,550

Purchase consideration settled in cash	6,181
Cash and cash equivalents in subsidiary acquired	–0
Cash outflow on acquisition	6,181

Note 26
Events after the end of the period

As at December 31, 2007, the Group has a loan outstanding to Murrayföretagen AB in the amount of TUSD 2,930. After the end of the period, Murrayföretagen AB has gone into bankruptcy. As at the date of the issue of the Annual Report, the effect of the bankruptcy on the value of the loan to Murrayföretagen AB was not known.

Note 27
Adoption of annual report

The annual report has been submitted by the Board of Directors on April 4, 2008, see page 58. The balance sheet and profit and loss accounts are to be adopted by the Company's shareholders at the Annual General Meeting on May 14, 2008.

To the shareholders of
Vostok Nafta Investment Ltd

We have audited the accompanying consolidated and parent company financial statements of Vostok Nafta Investment Ltd, appearing on pages 59–86, which comprise balance sheets as at December 31, 2007 and 2006, and income statements, statements of changes in equity and cash flow statements for the years then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Vostok Nafta Investment Ltd as of December 31, 2007 and 2006, and of its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Stockholm, April 8, 2008
PricewaterhouseCoopers AB

Klas Brand
Authorised public accountant
Lead Partner

Bo Hjalmarsson
Authorised public accountant
Partner

Independent Auditors' Report

Corporate Governance Code Application
Vostok Nafta is a limited liability company registered in Bermuda. In the absence of a Bermudian Code of Corporate Governance, Vostok Nafta applies the Swedish Code of Corporate Governance (“the Code”). The Company will apply the Code in full or, where applicable, explain deviations from it. The principles of corporate governance in Vostok Nafta are described below. This report has not been subject for review by the Company’s auditors.

Shareholders meetings
The Annual General Meeting (“AGM”) is the highest decision-making body of Vostok Nafta, in which all shareholders are entitled to attend in person or by proxy. The Annual General Meeting of Vostok Nafta is held in Stockholm, Sweden, in the Swedish language, once per year, no later than six months after the end of the financial year.
The task of the Annual General Meeting is to report on the financial results and take decisions on corporate matters, including payment of dividend and amendments to the Articles of Association. The Annual General Meeting also appoints members of the board of directors and auditors, and establishes the remuneration to the board of directors and the auditors.
During 2007, Vostok Nafta held two extra general meetings on May 18 and August 29. The extra general meeting held on May 18, 2007 resolved upon the remuneration to the board of directors and auditors, and approved the guidelines regarding remuneration to the management. At the extra general meeting held on August 29, 2007 it was, among other things, resolved to approve the board of directors proposal regarding the Company’s incentive scheme. The same meeting also approved the transfer of call options at market value in connection with investments in portfolio companies in accordance with the board’s proposal (with an adjustment put forth by Lorito Holding Limited).

Appointment and Remuneration to the Board of Directors and the Auditors
Shareholders in the Company have the right to nominate members of the board of directors, and auditors, to the Annual General Meeting. The AGM elects members of the board of directors for a term of one year and auditors for a period of one year. The shareholders also propose remuneration to the board of directors and auditors, which is to be resolved by the AGM. In accordance with the Code, the Company has established a nomination committee which prepares proposals for the election of and remuneration to members of the board of directors and auditors for the Annual General Meeting. The nomination committee is to consist of three members, of whom one is appointed among the board of directors and two members are to be appointed by the Company’s major shareholders. The nomination committee before the Annual General meeting 2008 consists of Ian H Lundin – member of the board, Åsa Nisell – Swedbank Robur Fonder and Lars Öhrstedt – AFA Insurance.

The Board of directors

The 2007 Board of directors
Through the sole member’s written resolution, made on April 10, 2007, pursuant to the Bye-laws of the Company it was resolved that the Company shall have eight Directors. The directors elected where: Al Breach, Paul Leander-Engström, Torun Litzén, Lukas H Lundin, Ian H Lundin, Per Brilioth, William A Rand and Robert J Sali. For a detailed presentation of the current Board, until the Annual General Meeting 2008, se section “Board, management and auditors” in the formal annual report.

Board meetings
The board of directors is to meet at least twice a year in person and more frequently when necessary. In addition, meetings are to be conducted by telephone if considered necessary. The Managing Director has regular contact with the Chairman of the board of directors and several other members of the board of directors.
During the financial year ended 31 December, 2007, six board meetings have been held, whereof two where held with personal attendance.

Work and Responsibilities
The Board of Directors adopts decisions on overall issues affecting the Vostok Nafta group. However, the Board of Directors’ primary duties shall be the organization of the Company and the management of the Company’s operations including:

Corporate Governance Report

– Decisions regarding focus of the business and adoption of Company policies;
– Supply of capital;
– Appointment and regular evaluation of the work of the Managing Director and Company management;
– Approval of the reporting instructions for the Company management;
– Ensuring that the Company's external communications are open, objective and appropriate for target audiences;
– Ensuring that there is an effective system for follow-up and control of the Company's operations and financial position vis-à-vis the established goals;
– Follow-up and monitoring that the operations are carried out within established limits in compliance with laws, regulations, stock exchange rules, and customary practice on the securities market.

Chairman of the Board of Directors

The Board of Directors has appointed a chairman amongst themselves. The chairman shall not be employed by the Company and shall not receive any salary nor be eligible for participation in the Company's incentive program. In Vostok Nafta, the Chairman holds an executive position and takes part in the work of the Company on a daily basis. Lukas H Lundin was elected chairman of the board as of the first meeting of the board of directors held on April 10, 2007.

Sub Committees of the Board

The board of directors has established three sub-committees: the audit committee, the compensation committee and the investment committee.

Audit committee

The function of the Audit Committee is to review on behalf of the Board, the Company's quarterly (Q1 and Q3) interim financial statements, review and make recommendations to the Board in relation to the Company's six month and yearly accounts, review audit fees, ensure maintenance of, and compliance with, the Company's internal control systems and liaise with the Group's external auditors as part of the annual audit process.

Audit committee in 2007

The audit committee consists of three of the board members, namely William A Rand, Torun Litzén and Ian H Lundin. In 2007, three meetings were held by the audit committee.

Compensation committee

The function of the Compensation Committee is to receive information on and determine matters regarding compensation to the Group Management. The guiding philosophy of the Committee in determining compensation for executives is the need to provide a compensation package that is competitive and motivating, will attract and retain qualified executives, and encourage and motivate performance.

Composition of the Board of Directors, elected on April 10, 2007, including meeting attendance 2007

Name	Elected to the board	Position	Connection to the company	Audit committee	Compensation committee	Investment committee	Attendance board meetings	Board fee, TUSD
Lukas H Lundin	2007	Chairman	Main owner		x	x	100%	76
Al Breach	2007	Member	Independent				67%	29
Per Brilioth	2007	Member	Management			x	100%	–
Paul Leander-Engström	2007	Member	Independent		x	x	83%	41
Torun Litzén	2007	Member	Independent	x			100%	43
Ian H Lundin	2007	Member	Main owner	x			100%	43
William A Rand	2007	Member	Independent	x			100%	50
Robert J Sali	2007	Member	Independent		x	x	100%	34
Number of meetings				3	2		6	

Compensation committee in 2007

The compensation committee consists of three of the board members, namely Lukas H Lundin, Robert J Sali and Paul Leander-Engström. In 2007, two meetings were held by the compensation committee.

Investment committee

The function of the Investment Committee is to make suitable investment recommendations to the Cypriot subsidiary Vostok Komi (Cyprus) Ltd. These recommendations must at all times be in line with the overall strategy of the Company as decided by the Board of Directors and communicated from time to time to the Investment Committee. A majority of the Investment Committee i.e. two directors can together make recommendations to the Board of Vostok Komi (Cyprus) Ltd, which will then resolve the matter.

Investment committee in 2007

The investment committee consists of three of the board members, namely Lukas H Lundin, Per Brilioth and Paul Leander-Engström.

Management

The Managing Director, who is a member of both the Board of Directors as well as of group management, manages the Company's day-to-day activities and prepares investment recommendations in cooperation with the other members of the Investment Committee.

Group management in 2007

Per Brilioth: Managing Director. Employed since 2007.
Sergei Glaser: Analyst and member of group management. Employed since 2007.
Anders Sjöberg: Chief Financial Officer. Employed since 2007.
For a detailed presentation of the management, see section "Board, Management and Auditors" in the formal annual report. The Investor Relations function of Vostok Nafta is managed by Robert Eriksson, who is "Head of Investor Relations" of Vostok Nafta. Robert Eriksson devotes a significant part of his time to Vostok Nafta, while simultaneously being engaged in Investor Relations activities for a number of other companies within "The Lundin Group of Companies".

Compensation to the board and management

The extra general meeting held on May 18, 2007 resolved that the remuneration to the board of directors shall, in total, amount to USD 322,000, of which USD 57,000 shall be paid to the chairman of the board and USD 29,000 shall be paid to each of the members of the board. For work in the Audit Committee, USD 21,000 shall be paid to the chairman and USD 14,000 to each of the members. For work in the Compensation Committee, USD 8,000 shall be paid to the chairman and USD 5,000 to each of the members. For work in the Investment Committee, USD 11,000 shall be paid to the chairman and USD 7,000 to each of the members. It was resolved that no fee shall be paid to the Managing Director.
The extra general meeting held on May 18, 2007 also approved the guidelines regarding remuneration to the management. The remuneration to the managing director and other members of the senior management shall consist of fixed salary, variable remuneration, other benefits and pension benefits. Except for the managing director, the senior management currently includes two individuals. The total remuneration shall correspond to the prevailing market conditions and be competitive. The fixed and variable remuneration shall correspond to the respective individual's responsibility and authority. The variable component should, in the first instance, be covered within the parameters of the Company's option plan and shall, where payable in other instances, be subject to an upper limit in accordance with market terms and specific objectives for the Company and/or the individual. The period of notice of termination of employment shall be three to six months in the event of termination by the member of the senior management. In the event of termination by the Company, the total of the period of notice of termination and the period during which severance compensation is payable shall not exceed 12 months. Pension benefits shall be either benefit-based or contribution-based or a combination thereof, with individual retirement ages. Benefit-based pension benefits are conditional on the benefits being earned during a pre-determined period of employment. The board of directors shall be entitled to deviate from these guidelines in individual cases should special reasons exist.
In advance of the annual general meeting in 2008, the compensation committee shall present a detailed

proposal for management remuneration principles for the coming year including a determination of the management positions that shall be subject to the remuneration principles.

Incentive programme

The Extra General Meeting held on August 29, 2007 decided in accordance with the proposal from the board of directors to adopt an incentive programme in Vostok Nafta Investment Ltd which entitles present and future employees to be allocated call options, which entitle the holder to acquire shares represented by Swedish Depositary Receipts in Vostok Nafta Investment Ltd.

The incentive programme shall be governed by the following terms and conditions:

– The exercise price for the options shall correspond to 120 percent of the market value of the Swedish Depositary Receipts at the time of the granting of the options.

– The options may be exercised not earlier than two years and not later than three years from the time of the granting.

– For employees resident outside of Sweden the following conditions shall apply. No premium shall be paid for the options and the options may only be exercised if the option holder at the time of exercise is still employed within the group. If an option holder ceases to be an employee of or, as the case may be, consultant to any member of the Group for any of the reasons set out below, then his or her options will not lapse but may be exercised to the extent notified to the option holder on the date of grant provided all applicable performance conditions being relevant at date of cessation are satisfied or waived. The reasons are; ill-health, injury, and disability; retirement; early retirement by written agreement with the option holder's employer; his or her employing company ceasing to be under the control of the Company, or, as a result of a transfer of the undertaking in which the option holder works, transfer to a company which is neither under the control of the Company nor a member of the Group; any other reason specified by the directors in their absolute discretion.

– For employees resident in Sweden the following conditions shall apply. The options are offered to a purchase price corresponding to the market value of the options at the time of the offer. The options shall be fully transferable and will hereby be considered as securities. Among other things this entails that the options are not contingent upon employment and will not lapse should the employee leave his or her position within the group.

– Options may be issued by Vostok Nafta Investment Ltd or by other group companies.

Preparation and administration

The Board of Directors, or a designated committee appointed by the Board of Directors, shall be authorised to determine the detailed terms and conditions for the incentive scheme in accordance with the approved principal conditions and guidelines. The Board of Directors may in connection thereto make necessary adjustments to satisfy certain regulations or market conditions abroad. The Board of Directors shall also be authorised to resolve on other adjustments in conjunction with material changes affecting the group or its business environment, which would mean that the authorised conditions for the incentive scheme would no longer be appropriate.

Allocation

The incentive scheme is proposed to include granting of not more than 1 million options. Allocation of options to the Managing Director shall not exceed 500,000 options and allocation to each member of the executive management or to other key employees shall not exceed 200,000 options.

The allocation of options shall be decided by the Board of Directors, or by the Compensation Committee, whereby inter alia the performance of the employee and his or her importance to the group will be considered. In connection with allocation of options to employees resident outside of Sweden as well as resident in Sweden, the following criteria shall inter alia be considered: the employee's ability to manage and develop the existing portfolio, identify new investment opportunities and evaluate conditions of new investments, and also return on capital or estimated return on capital in various object of investments. The employees will not initially be offered the maximum allocation of options and a performance related allocation system will be maintained since allocation of additional options within the mandate given by the general meeting will require fulfilment of stipulated requirements and targets. The Compensation Com-

mittee shall be responsible for the evaluation of the performance of the employees. The outcome of stipulated targets shall, if possible, be reported on afterwards.
Directors who are not employed by the group shall not be able to participate in the scheme.

Possible future bonus for employees resident in Sweden

In order to stimulate the participation in the scheme, the company has the intention to arrange for a subsidy in the form of a bonus payment which after tax corresponds to the option premium. Half of the bonus is intended to be paid in connection with the purchase of the options and the remaining half in connection with the exercise of the options. The latter bonus payment is subject to the requirement that the holder is still an employee of the group at the time of exercise of the options. If the options are not exercised, the latter bonus payment will not be paid. For employees in Sweden, the participation in the scheme will thus include a risk-taking element.

Purpose

The purpose of the proposed incentive scheme is to create conditions to retain and recruit competent employees to the group as well as promote long-term interests of the company by offering its employees the opportunity to participate in any favourable developments in the value of the Company. The Board of Directors is of the opinion that the adoption of an incentive scheme is particularly justified as a consequence of employees of the Company not being subject to any variable bonus scheme.

Issuance

On August 30, 2007 it was decided to issue 710,000 of the authorized 1,000,000 options under the company's incentive program to a group of employees.

Transfer of call options

The Extra General Meeting held on August 29, 2007 also decided in accordance with the proposal from the board of directors to approve the transfer of call options, during the period up to the next Annual General Meeting in Vostok Nafta Investment Ltd, by group companies to members of the executive management and other employees related to investments in non-listed portfolio companies to create opportunities for employees to take part in future rise in value. Directors of the Company who are not employed by the group shall not be entitled to participate in the scheme.
The following guidelines shall apply in connection with transfer of call options:
– The options shall entitle the holder to acquire shares in the portfolio company at a certain exercise price corresponding to 110–150 percent of the market value of the shares in the portfolio company at the time of the transfer of the options.
– The term of the options shall be not longer than five years.
– The options shall be sold at market value. The price for the options shall be determined by an independent valuation institute or auditing firm in accordance with the Black & Scholes valuation model. Investment in the options thus implies a risk-taking element for the employee.
– The number of options should amount to not more than a number that corresponds to ten percent of the underlying shares in a portfolio company owned by a company in the group.
– The Company shall be entitled to repurchase the options at market value if the holder ceases to be an employee of the group.
– If the shares in a portfolio company are sold or listed prior to the last day for exercise of the options, the options shall be exercised at the latest in connection with the trade sale or the listing of the shares. If the options have been exercised prior to the company's sale of the shares in the portfolio company, the employee shall be obliged if so required to sell the shares in connection with the company's disposal.
In case of special circumstances, the Board of Directors shall be entitled to deviate from the guidelines above.
By offering employees to acquire options in respect of shares in portfolio companies, employees will be given the opportunity to participate in a future increase in value similar to the opportunities open for persons acting for private equity entities. The Board of Directors is of the opinion that this proposal significantly improves the possibility to retain and recruit competent personnel to the group.

Issuance

As of yet no call options have been transferred to any employees within the group. This is to a large extent due to the longer lead times associated with investments in non-listed portfolio companies.

Auditors

Auditors in 2007

Through the sole member's written resolution, made on April 10, 2007, the audit firm PricewaterhouseCoopers AB, Sweden was appointed as auditor for the period up to the next AGM.

Klas Brand, born 1956. Authorised Public Accountant, Lead Partner. Auditor in the Company since 2007. PricewaterhouseCoopers AB, Gothenburg, Sweden.

Bo Hjalmarsson, born 1960. Authorised public accountant, Partner. Auditor in the Company since 2007. PricewaterhouseCoopers AB, Stockholm, Sweden.

During the year the auditing firm has not had any other assignments from Vostok Nafta in addition to auditing work specified in the section "Independent Auditors' Report" on page 87, and the review of the new, revised historical financial statements presented in the prospectus relating to the restructuring of Vostok Nafta Investment Ltd.

Internal control

The board of directors has overall responsibility for setting up effective internal control systems. Responsibility for maintaining and carrying out effective control has been delegated to the Managing Director. Internal control is a process which should be applied to ensure that goals such as effective and profitable operation are attained, financial reporting is reliable and laws and ordinances are followed. The board of directors has also, as described above, set up an audit committee which is responsible for continuously reviewing the Company's control in relation to financial reporting.

The board of directors is responsible for the Company's organisation and administration of the Company's activities, which includes internal control. Internal control in this context regards those measures taken by Vostok Nafta Investment Ltd ("Vostok Nafta" or the "Company") board of directors, management and other personnel, to ensure that bookkeeping, asset management and the Company's economic condition in general are controlled in a reliable fashion and in compliance with relevant legislation, applicable accounting standards and other requirements for publicly listed companies. Vostok Nafta has also appointed an Audit Committee, consisting of three members of the board, charged with the special responsibility to review and discuss internal and external audit matters.

This report has been established in accordance with the Swedish Code of Corporate Governance, sections 3.7.2 and 3.7.3, which govern internal control over the financial reporting. In addition this report has been prepared in accordance with the guidance provided by FAR SRS, the institute for the accounting profession in Sweden, and the Confederation of Swedish Enterprise. This report does not constitute part of the formal Annual Report and has therefore not been reviewed by the Company's auditors.

Vostok Nafta is an investment company and hence the Company's main activities is the management of financial transactions and the Company's internal control over financial reporting is focused primarily on ensuring an efficient and reliable process for managing and reporting on purchases and sales of securities and holdings of securities. The board of directors has decided not to implement any particular review function (internal audit) in addition to the internal control functions already in place.

The system of internal control is normally described in terms of five different areas that are a part of the internationally recognised framework which was introduced in 1992 by The Committee of Sponsoring Organizations in the Treadway Commission (COSO). These areas, described below, are control environment, risk assessment, control activities, information and communication and monitoring.

The management continuously monitors the Company's operations in accordance with the guidelines set out below. Monthly reports are produced for internal use, which later act as the basis for a quarterly review by the board of directors. During the year the board of directors and management have also examined possible additions to the internal control functions already in place within the organisation. The main goal was to enhance control functions relating to the Company's financial risk management, covenants to lenders and counterparty and custody risks.

Control environment

The control environment, which forms the basis of internal control over financial reporting, to a large extent exists of the core values which the board of directors communicate and themselves act upon. Vostok Nafta's ambition is that values such as, precision, professionalism and integrity should permeate the organization. Another important part of the control environment is to make sure that such matters as the organisational structure, chain of command and authority are well defined and clearly communicated. This is achieved through written instructions and formal routines for division of labour between the board of directors on the one hand, and management and other personnel on the other. The board of directors establishes the general guidelines for Vostok Nafta's core business, which is purchases and sales of securities and holdings of securities. To ensure a reliable and easily overseeable procedure for purchases and sales of securities the Company has established a sequential process for its investment activities. A specific Investment Committee has been instituted whose members are appointed by the board of directors, and charged with the task of identifying and reviewing potential investments or divestments. After review, a committee majority is needed to issue a recommendation for sale or purchase, upon which investment decisions are formally made by the Board of Directors of Vostok Komi (Cyprus) Ltd., and an execution order is issued. As for the investment process, as for all other company activities they are governed by internal guidelines and instructions. The organizational structure of Vostok Nafta is characterised by a close and flat organisation. The Company's limited number of staff members and close cooperation amongst them contribute to high transparency within the organisation, which complements fixed formal control routines.

Vostok Nafta's Financial Controller is responsible for the control and reporting of the Company's consolidated economic situation to management and board of directors.

Board of Directors' report on internal control

Risk assessment

The board of directors of Vostok Nafta is responsible for the identification and management of significant risks for errors in the financial reporting. The risk assessment specifically focuses on risks for irregularities, unlawful benefit of external part at Vostok Nafta's expense and risks of loss or embezzlement of assets. It is the ambition of Vostok Nafta to minimize the risk of errors in the financial reporting by continuously identifying the safest and most effective reporting routines. The Company's flat organizational structure and open internal communication facilitates the work to identify potential lacks in the financial reporting, as well as makes it easier to implement new, safer routines. The board of directors puts most effort into ensuring the reliability of those processes, which are deemed to hold the greatest risk for error, alternatively whose potential errors would have the most significant negative effect. Among other things this includes establishing clearly stated requirements for the classification and description of income statement and balance sheet items according to generally accepted accounting principles, pertinent legislation. Another example is the routine of a sequential procedure for investment recommendations and approvals of the same.

Control activities

This risk assessment leads to a number of control activities in place to verify compliance with set requirements and established routines. The purpose of the control activities is hence to prevent, detect and rectify any weaknesses and deviations in the financial reporting. For Vostok Nafta's part such control activities include the establishment of verifiable written decisions at every instance in the investment procedure. Thereto, after every completed transaction, purchase or sale, the whole process is examined to verify the validity of the transaction, from recommendation to approval and execution. Bank and custody reconciliations are also performed and compared to reported financial statement items. Control activities also include permanent routines for the presentation and reporting of company accounts, for example monthly reconciliations of Vostok Nafta's assets and liabilities, as well as portfolio changes. Special focus is also put on making sure that the requirements and routines for the accounting procedure, including consolidation of accounts and creation of interim and full year reports comply with pertinent legislation as well as generally accepted accounting principles and other requirements for publicly listed companies. Controls have also been carried out to ensure that the IT-/computer systems involved in the reporting process have a sufficiently high dependability for its task.

Information and communication

Vostok Nafta has tried to ensure an efficient and accurate provision of information internally and externally. For this purpose the Company has established fixed routines and invested in reliable technical applications to guarantee a fast and reliable way of sharing information throughout the organisation. Internal policies and general guidelines for financial reporting are communicated between the board of directors, management and other personnel through regular meeting and e-mails. Vostok Nafta's flat organizational structure and limited number of staff members further contributes to the efficient sharing of accurate information internally. To ensure the quality of the external reporting, which is the extension of the internal, there is a written communication policy which governs what and how information shall be communicated.

Monitoring

The board of directors receives monthly NAV reports and detailed quarter reports on Vostok Nafta's financial position and changes in its holdings. The Company's financial situation and strategy are discussed at every board meeting, as well as any problems in the activities and financial reporting since the last board meeting. The Audit Committee has a particular responsibility to review and bring any problems with the internal control of financial reporting to the board of directors' attention. Potential reported shortcomings are followed up via management and the Audit Committee. The Company prepares interim reports four times annually which are reviewed by the board and Audit Committee. Meetings with the Company's auditors are also held in connection with every quarterly reporting. A review of the Company's accounts is also performed at least once a year in addition to the comprehensive audit in connection with the Annual Report.

1P Proven reserves
2P Proven and Probable reserves
3P Proven, Probable and Possible reserves
ADR American Depository Receipt
bbl Barrel
bcm Billon cubic metres
bcmpa Billion cubic metres per annum
bln Billion
boe Barrels of oil equivalents
boepd Barrels of oil equivalent per day
bopd Barrels of oil per day, i.e. the number of barrels of oil produced (or transported) per day
Capex Capital Expenditures: expenditures by a company to acquire or upgrade physical assets such as equipment, property and industrial buildings
CIS Commonwealth of Independent States (former Soviet Union)
cm Cubic meters
CSFB ROS Credit Suisse First Boston ROS Index
Downstream Refining of crude oil and the marketing and distribution of oil products that occur after refining, as opposed to upstream.
E Estimate
EBITDA Earnings Before Interest, Taxes, Depreciation and Amortization
EV Enterprise Value, i.e. stock exchange value + net liability
Extractable reserves An estimate of the volume of extractable oil reserves held by the relevant oil company
F Forecast
FSU Former Soviet Union
Holding company The parent company in the vertically integrated Russian oil groups
kbpd Thousand barrels per day
kWh Kilowatt-hour, equal to 1,000 watts of electricity used for one hour. A measure of electric power consumption.
lb English pound – unit of weight (454 grammes)
lpapc Litres per annum per capita
LNG Liquified Natural Gas
mcm Thousand cubic metres
mln or mm Million
mmboepd Million barrels of oil equivalent per day
mmbopd Million barrels of oil per day
mmtnpa Million tonnes per annum
MSCI EM MSCI Emerging Markets Index
MW Megawatt
MWh Megawatt-hour, equal to 1,000,000 watts of electricity used for one hour. A measure of electric power consumption.
n/a Not available
Neft or Neftegas Russian for oil company
Netback A measure of oil and gas sales net of royalties, production and transportation expenses.
nm Not material
pa Per annum.
P/BV Relationship between stock exchange value and entered equity capital
P/barrel reserves The stock exchange value divided by the number of barrel reserves (oil) in the ground
P/Cash flow Stock exchange value divided by cash-flow, which in many cases relates to net profit after tax with the setting back of the depreciation
P/E Price/Earnings, i.e. the relationship between the stock exchange value and net profit
P/EBIT The relationship between the stock exchange value and the operating profit
P/prod Stock exchange value divided by number of barrels (oil) produced a year
P/S Price/Sales, i.e. the relationship between the stock exchange value and sales
q-o-q Quarter-on-quarter
RTS Russian Trading System, the leading trading place for Russian shares
RUB Rouble
SDR Swedish Depository Receipt
SEK Swedish kronor
Tcm Trillion cubic metres
Throughput The amount of crude oil processed by a refinery in a given period
T Thousand
tn Tonne
Upstream Upstream covers the exploration, production and transport prior to refining
USD American dollar
Vertically Integrated When applied to oil and gas companies, it indicates that the firm operates in both the upstream and downstream sectors.
y-o-y Year-on-year

Conversion factors
1 tonne oil = 7.33 barrels of oil
1 tonne condensate = 8.5 barrels of condensate

Glossary of terms and acronyms used in the annual report

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