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Annual report 2006

TMK

annual report

stable growth

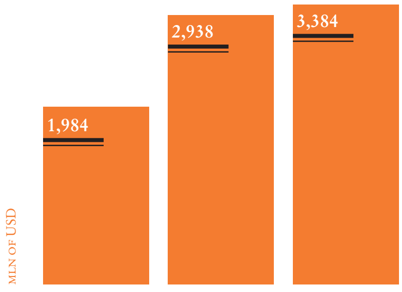
2006

annual report
2006

OAO
TMK

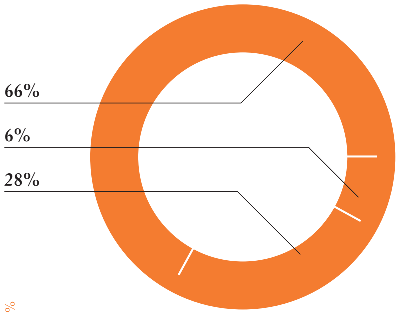
NET SALES
increased by 15% compared to 2005

(+15%)



2004	1,984
2005	2,938
2006	3,384

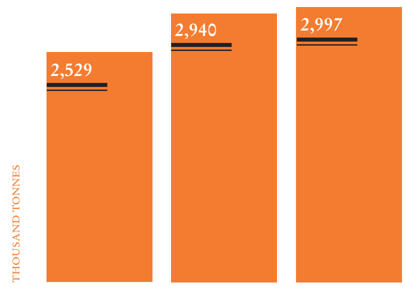
SEAMLESS PIPES SALES
accounted for 66% of net sales in 2006



Seamless	66%
Welded	28%
Other	6%

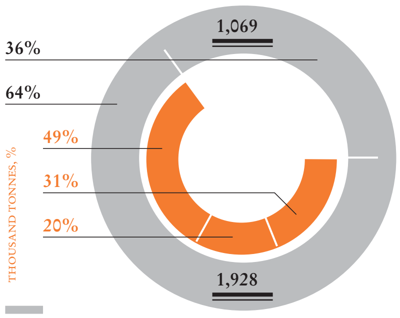
SALES VOLUMES
increased by 2% compared to 2005

(+2%)



2004	2,529
2005	2,940
2006	2,997

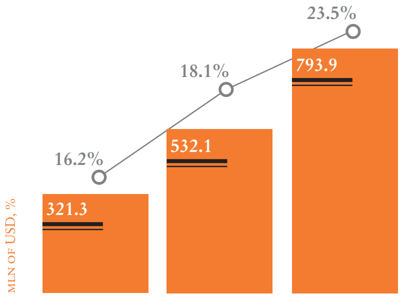
SALES VOLUMES
of seamless pipes were 1,928 thousand tonnes of which the highest-margin products (OCTG) were 49%



Welded	36%
Seamless	64%
OCTG	49%
industrial	31%
line pipes	20%

EBITDA*
increased by 49% compared to 2005

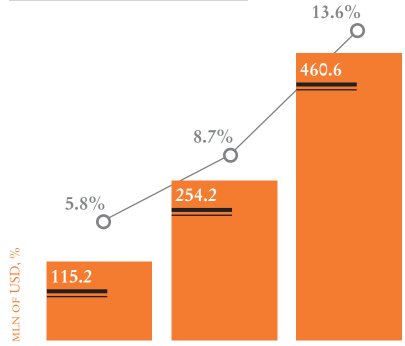
(+49%)



	EBITDA (MLN OF USD)	EBITDA MARGIN (%)
2004	321.3	16.2
2005	532.1	18.1
2006	793.9	23.5

NET PROFIT
increased by 81% compared to 2005

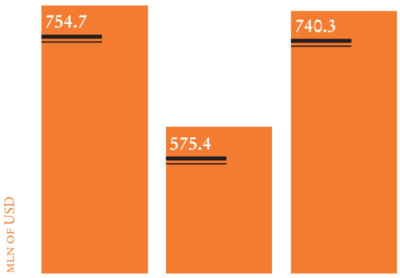
(+81%)



	NET PPROFIT (MLN OF USD)	NET PROFIT MARGIN (%)
2004	115.2	5.8
2005	254.2	8.7
2006	460.6	13.6

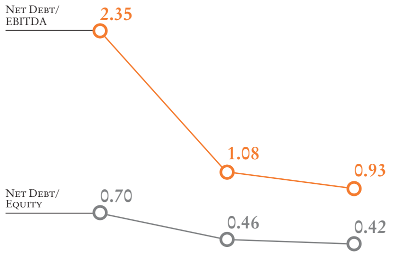
* *Please refer to EBITDA notes on page 192.*

NET DEBT *
at the end of the year



2004	754.7
2005	575.4
2006	740.3

NET DEBT
ratios show positive trend



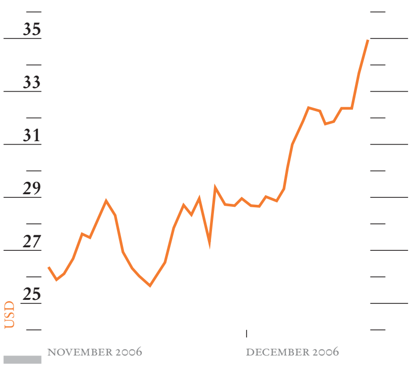
	Net Debt/EBITDA	Net Debt/Equity
2004	2.35	0.70
2005	1.08	0.46
2006	0.93	0.42

EFFICIENCY
ratios show positive trend

	2004	2005/2004	2005	2006/2005	2006
Return on Equity (ROE)*	11%	▲ 100%	22%	▲ 36%	30%
Return on Capital Employed (ROCE)*	17%	▲ 59%	27%	▲ 15%	31%
Working capital turnover (days)*	70	▼	66	▲	73

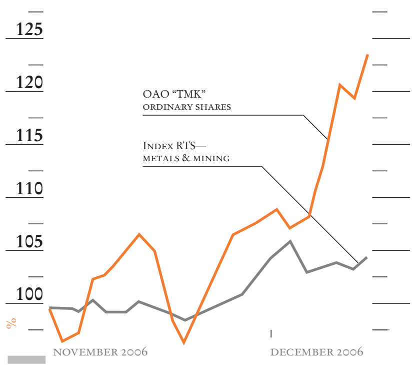
THE GDR PRICE**
As of 31 December 2006, the GDR price on LSE was 32% up on the price on the first trading day

(+32%)



THE ORDINARY SHARE PRICE ON RTS
As of 31 December 2006, the ordinary share price on RTS was 23% up on the price on the first trading day

(+23%)



** Please refer to Net Debt, ROE, ROCE, and working capital calculations on page 192.*

*** 1 GDR=4 ordinary shares.*

contents

stable
growth

SCALE

TMK ANNUAL REPORT 2006

TOP 3 IN THE WORLD

The company is among the top three pipe producers

1
Corporate History

TMK is Russia's largest manufacturer and supplier of steel pipes, and ranks among the top three pipe producers globally. OAO "TMK"'s GDRs are traded on the London Stock Exchange (LSE). Its ordinary shares are traded on the Russian Trading System (RTS) and the Moscow Interbank Currency Exchange (MICEX).

TMK was incorporated as a closed joint-stock company (ZAO) on 17 April, 2001 and was originally formed around the trading and sales operations of its underlying plants.

During the period from 2002 to 2004, ZAO "TMK" acquired majority interests in and took over the management functions of four Russian pipe plants: Volzhsky, Seversky, TAGMET and Sinarsky. By the end of February 2004, ZAO "TMK" held majority interests in and managed each of these leading manufacturers of the domestic pipe industry.

In May 2005, ZAO "TMK" acquired a 100% interest in Sinara Trading (subsequently renamed TMK Global) which is now responsible for sales and marketing operations outside Europe, Russia and the CIS countries.

On 16 June, 2005, ZAO "TMK" was re-registered as an open joint-stock company (OAO). During this period, TMK's Strategic Investment Programme was developed and independent members were elected to the Board of Directors of OAO "TMK" for the first time.

In March 2006, TMK acquired "Sinara Handel GmbH" (now TMK Sinara Handel GmbH) which is the majority shareholder of the Romanian pipe plant SC Artrom SA (now SC TMK – Artrom SA) and the Romanian Iron & Steel Works SC C.S.R. SA (now SC TMK – Resita SA).

In August 2006, TMK entered into an agreement to purchase a 75% interest in OAO Orsky Machine Building Plant (OMZ) which specializes in the production of tool joints, a critical component for drill pipes, as well as pump barrels and other equipment for the oil and gas and other industries.

In November 2006, OAO "TMK"'s GDRs were listed on the London Stock Exchange and its ordinary shares were listed on the Russian Trading System.

TMK's sales were centralised under its subsidiary, ZAO "TMK Trading House" which coordinates the sales of pipe products and the supply of raw materials to the plants. To increase TMK's foreign sales a representative office of ZAO "TMK Trading House" was opened in Baku (Azerbaijan) in 2002 and TOO "TMK – Kazakhstan" (Kazakhstan) was established in 2003. TMK's subsidiary, TMK North America Inc. (USA), as well as the representative office of ZAO "TMK Trading House" in the Republic of China started operating in 2003. The company TMK Middle East was established in Dubai (United Arab Emirates) in March 2006.

Through consolidation of its production assets, TMK has created a stable technology-based group of companies that manufactures high quality competitive products.

2 Chairman's Letter

Dmitriy Pumpyanskiy,
Chairman of the Board of Directors

As a dynamically growing company, TMK aspires to leadership not only in pipe manufacturing and sales but in all related areas: corporate governance, personnel management, industrial safety and environmental policy.

Dear shareholders

The 2006 results presented for your consideration are clear evidence of the dynamic growth of TMK as an integrated global producer of steel pipes. Following the Development Strategy mapped out up to 2015, TMK has taken a number of initiatives and has achieved a qualitatively new level of production, sales and investment activity, whilst following globally recognised standards of corporate governance and social awareness. In each of these areas, TMK's achievements would not have been possible without the outstanding professionalism, initiative and personal dedication of the TMK management team. To meet TMK's ambitious targets, production teams and sales staff worked skilfully and efficiently, making optimal use of the available materials and equipment. The global investment community gave a strong vote of confidence in TMK's understanding of the business, its future prospects and financial performance, as OAO "TMK" successfully completed its IPO and offered its securities on both the London Stock Exchange and the RTS exchange.

The Board of Directors worked in complement to the management team, allowing TMK to adhere to the established priorities for its operations and to use its strategic vision when making the necessary corrections to operating plans. TMK's independent directors play a vital role in the management structure, chairing all the committees of the Board of Directors. TMK's system of corporate governance was reassessed positively by Standard & Poor's: on the international scale, the rating is 6+, while the rating on the Russian national scale is 6.7. This increased rating is a reflection of the Board of Directors' commitment to following international principles of corporate governance and ensuring an appropriate level of informational openness and financial transparency in TMK's operations, which are essential to winning the trust of the investment community and other participants of the financial markets.

Guided also by the principles of sustainable development, TMK has made safety one of its top priorities in all areas of operations. Recognition of responsibility for the effect TMK's production operations have on the environment has led TMK companies to the creation of a corporate environmental policy and to the establishment of unified corporate principles for reducing environmental and human impact due to the operations. Focused investments are steadily introducing environmentally friendly technologies that meet the highest possible standards. TMK also works in conjunction with government agencies and NGOs on issues involving environmental safety.

On behalf of the Board of Directors, I should like to thank TMK's clients and partners for their contribution to TMK's success. I would also be remiss not to mention the dedication and responsibility of the production personnel who ensured that client orders were filled on time and that the ambitious investment programme was implemented on schedule. I am confident that the continuing efforts to implement TMK's strategic plans in 2007 will help TMK's capitalisation to grow further in the interests of employees and society as a whole.

3 CEO's Letter

KONSTANTIN SEMERIKOV,
Chief Executive Officer

Having set its strategic goal to be the world leader in pipe manufacture while simultaneously increasing the share of products with high added value, TMK has made significant progress in this direction in 2006.

The year 2006 is over and another page has been turned in the history of TMK. TMK set itself major challenges, and now, looking back over the year, it can be confidently said that TMK has successfully implemented the measures planned for 2006 as TMK continues to develop at a rapid pace.

TMK has shown good results against the background of increasing competition and nearly full utilisation of its seamless pipe production capacity, thus confirming the solidity of its market position and the commitment and determination of the management team in achieving its targets.

A strategic investment programme envisaging USD 1.4 billion in investments by 2010 was started in 2004 and is designed to increase the volume, improve the quality, and expand and optimise the structure of the products TMK manufactures.

The strategic programme has begun to show its first results last year. TMK's companies implemented several major projects reconstructing production facilities and installing new equipment. Two continuous casting machines have been put into operation, heading presses have been brought on line, methods of non-destructive inspection of pipes have been implemented and new hydraulic presses and other equipment have been installed. It should be noted that TMK is carrying out a large-scale modernisation of its production facilities and the development of new technologies without interrupting its existing production. The funds spent on implementing the strategic programme amounted to USD 323.2 million for the period 2004 – 2006.

TMK sold almost 3 million tonnes of pipes in 2006 generating turnover of USD 3,384 million and surpassing 2005 sales by 15%. The largest growth in sales occurred in the high-technology seamless pipes sector. Shipments of Oil Country Tubular Goods (OCTG) increased by 16% and their share in overall shipments grew by 3.6% (to 31.6%). The share of premium-class pipe products in the total volume of shipments in 2006 was 23%. TMK increased its share of Russian pipe exports from 49% to 56%. Sales outside Russia accounted for 32% of overall sales in 2006.

As a result of measures optimising the structure of the product portfolio, revenue per tonne of products sold increased by 13% compared to 2005 and amounted to USD 1,130 per tonne. EBITDA increased by 49% and amounted to USD 793.9 million. TMK has the potential for further growth in earning power which is essential for strengthening its position in the world pipe industry.

The structure of the credit portfolio has been improved such that as at 31 December 2006 it consists primarily of long-term loans. The share of rouble liabilities has decreased to 42% of the total. TMK issued Eurobonds in the principal amount of USD 300 million. TMK also successfully issued rouble-denominated bonds with a total par value of 5 billion roubles.

In implementing its strategic investment programme, TMK pays particular attention to developing new types of products and introducing state-of-the-art technologies. In 2006 TMK continued its work on integration with RosNITI, the only institute dedicated to the pipe industry in Russia. The TMK research and development centre is also being actively developed.

TMK is pursuing an active policy of developing its global marketing network. A subsidiary was established in Dubai (United Arab Emirates) in 2006 as the latest step in strengthening TMK's positions in that key market.

In 2006, the Romanian pipe plant SC Artrom SA (now SC TMK – Artrom SA) and the Romanian Iron & Steel Works SC C.S.R. SA (now SC TMK – Resita SA) joined TMK, thus creating a production base within the European Union and expanding TMK's presence on the European market for industrial seamless pipes.

As part of the measures to strengthen the operations of TMK, work to implement long-term partnership agreements with key suppliers of raw and other materials as well as with major clients was continued last year. Partnership agreements with Gazprom and TNK-BP are being implemented. A strategic agreement was concluded with OAO NK Rosneft in early 2007 and there are plans to conclude similar agreements on the supply of products with a number of other major Russian and international oil companies.

Without a doubt, TMK's achievements are to the credit of all of its employees. I should like to thank each and every employee for their contribution to advancing the course charted by TMK.

The scope of the strategic investment programme will increase in 2007 and will lay the groundwork for a significant increase in TMK's production capacity in 2008–2010. TMK will also continue the implementation of plans to increase its influence on world markets.

We are convinced that we shall continue to justify the trust of our shareholders, investors, partners and all who are interested in the successful development of TMK.

4 Key Events

2006

January

)) TMK made its first shipment of oil and gas pipes to Saudi Aramco (Saudi Arabia), one of the largest oil producers in the world.

February

)) TMK placed its third issue of bonds, with a total par value of 5 billion roubles.

March

)) TMK completed the acquisition of 100% of the shares of Sinara Handel GmbH (now TMK Sinara Handel GmbH) which owns controlling shares in the Romanian pipe plant SC Artrom SA (now SC TMK-Artrom SA) and the Romanian Iron & Steel works SC C.S.R. SA (now SC TMK-Resita SA).

)) TMK and China Petroleum Technology & Development Corporation concluded a long-term partnership agreement.

)) The company TMK Middle East was founded in Dubai (United Arab Emirates); this is the latest step in the development of TMK's international distribution network.

April

)) A new upsetting mill was commissioned at Sinarsky Pipe Plant.

May

)) The Volzhsky Pipe Plant qualified as an official supplier of pipe products for two of the largest oil production companies of Kuwait: Kuwait National Petroleum Company and Kuwait Oil Company.

June

)) The Board of Directors of OAO "TMK" approved the Ethics Code the purpose of which is to define the standards of behaviour of employees and to uphold the impeccable reputation of TMK.

)) TMK signed a strategic partnership agreement with Salym Petroleum Development N.V.

July

)) Construction of a continuous casting machine produced by SMS Demag (Germany) was completed at the Taganrog Metallurgical Works*.

August

)) The Volzhsky Pipe Plant was qualified by Royal Dutch Shell and included in the latter's list of official suppliers of oil and gas pipes.

)) TMK and OOO NGK ITERA concluded a long-term partnership agreement to cover the needs of ITERA group companies for pipe products.

September

)) The Standard & Poor's rating agency assigned OAO "TMK" a long-term credit rating of B+.

)) The Moody's rating agency assigned OAO "TMK" a B1 corporate family rating.

)) TMK placed an issue of Eurobonds in the principal amount of USD 300 million.

* *Named as Taganrog Metallurgical Plant in the "Consolidated Financial statements" section of the current report.*

October

)) OAO "TMK" announced its intention to float its shares in an initial public offering of securities on the Russian Trading System (RTS) stock exchange and the London Stock Exchange.

)) TMK Steel Limited increased (directly and indirectly) its ownership of OAO "TMK" to 100%.

)) A new gas cleaning system of the electrical metallurgical assembly was launched at the Volzhsky Pipe Plant.

November

)) TMK Steel Limited sold 22.98% of OAO "TMK" shares through a public offering.

)) Trading of OAO "TMK" GDRs began on the London Stock Exchange and trading of ordinary shares began on the RTS.

December

)) Comprehensive testing of a continuous casting machine produced by SMS Demag (Germany) began at the Seversky Tube Works*.

)) Standard & Poor's rating agency upgraded the corporate governance rating of OAO "TMK" to 6+ on the international scale and to 6.7 on the Russian scale.

)) Live testing of a cogging mill was performed at the Sinarsky Pipe Plant. The new equipment will make it possible for the plants to use billets produced by TMK plants when manufacturing pipes.

)) The construction of a new piercing mill was completed at the Seversky Tube Works. This project is an integral part of the creation of a modern high-technology seamless pipe production assembly at the plants.

** Named as Seversky Pipe Plant in the "Consolidated Financial statements" section of the current report*

4 Key Events

AFTER 2006

January

)) TMK and Corinth Pipeworks S.A., the largest pipe manufacturer in Greece, established a joint venture for the production of longitudinally welded pipes with a diameter of 168 to 530 mm to be used in the oil and gas, machine building and construction industries.

February

)) TMK acquired OAO Orsky Machine Building Plant which specialises in the production of tool joints, tubing couplings and pump barrels for portable drilling units and in services to companies in the oil and gas sector.

)) TMK and SMS Group (Germany), one of the world's leading producers of metallurgical and pipe mill equipment, signed a Strategic Partnership Agreement for the period up to 2015.

)) TMK and OAO Magnitogorsk Iron & Steel Works, the largest iron and steel works in Russia, signed a Strategic Partnership Memorandum.

)) A session of the Presidium of the Council of State of the Russian Federation devoted to Industrial Policy took place in Volgograd. Within the framework of the session Russian Federation President V.V. Putin visited the Volzhsky Pipe Plant.

)) A new continuous casting machine was put into operation at the TMK-Resita Iron & Steel Plant.

)) A new cross piercing elongator pipe rolling mill was brought on line at the TMK-Artrom pipe plant.

March

›› OAO Russian Pipe Industry Research Institute (RosNITI), the largest pipe sector research and development centre of Russia, joined TMK.

›› OAO "TMK" shareholders approved TMK's Share Option Programme*.

›› TMK and HAEUSLER (Switzerland) signed a contract for the supply of equipment for manufacturing large diameter longitudinally welded pipes.

›› TMK and OAO NK Rosneft concluded a contract on Long-Term Strategic Partnership.

April

›› OAO "TMK" shares admitted to trading on the Moscow Interbank Currency Exchange.

** *The details of the Share Option Programme are disclosed in the "Remuneration" section of the current report.*

stable
growth

LEADERSHIP

67 and 11%

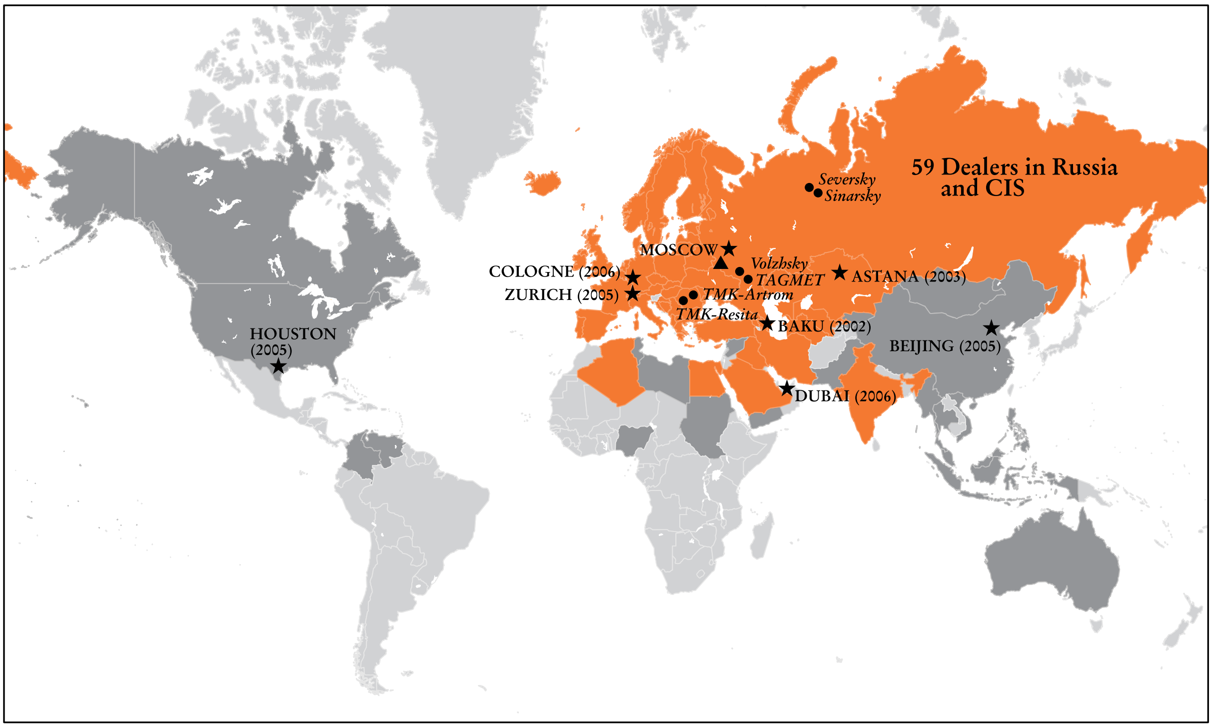
MARKET SHARES

67% Russian and 11% world market shares for OCTG pipes

5 (1)
About the Company

MARKET POSITION AND KEY ADVANTAGES

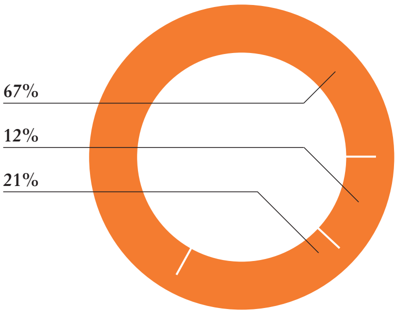
TMK: Global footprint



● PRODUCTION; ★ SALES AND MARKETING; ▲ TRANSPORT AND LOGISTICS; ■ PRINCIPAL MARKETS TODAY; ■ NEW MARKETS.

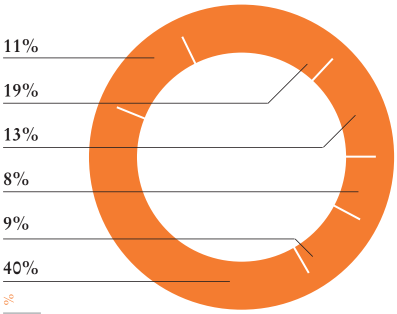
TMK delivers its products to customers in more than 60 countries. TMK's principal customers include major Russian oil and gas companies including Gazprom, Rosneft, Surgutneftegaz, TNK-BP and LUKOIL, major multinational oil and gas companies like Shell and national oil companies, e.g. ONGC, Saudi Aramco, Sonatrach and KOC.

Russian Market for OCTG, 2006



TMK	67%
ChTPZ	12%
Import	21%

World Market for OCTG, 2006



TMK	11%
Tenaris	19%
V&M	13%
US Steel	8%
TPCO	9%
Other	40%

As a pipe supplier, TMK has participated in many major national and international projects, such as the Caspian Pipeline Consortium, the Baltic Pipeline System, the Yamal-Europe gas pipeline and the Sakhalin-1 project. TMK is currently a supplier in the expansion of the Central Asia-Centre gas pipeline project.

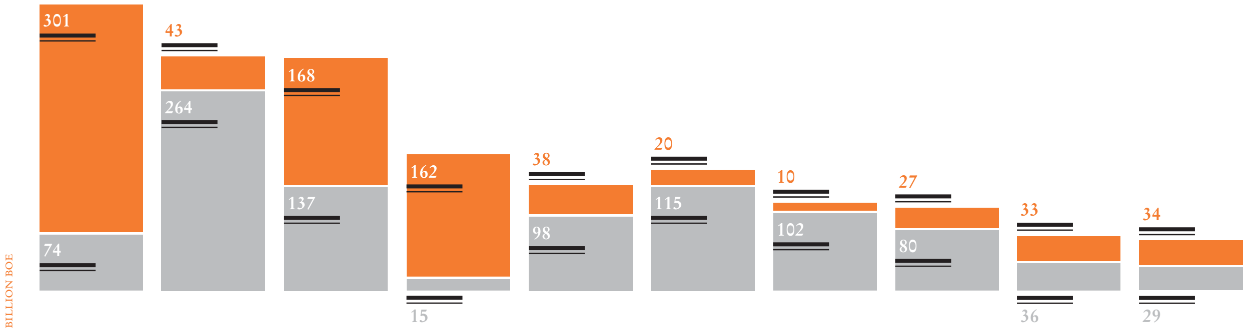
TMK is the leader in all market segments in which it operates in Russia, except the large-diameter welded and the industrial seamless segments which have a lower margin as compared to seamless pipes for the oil and gas industry. TMK is the third ranked global pipe producer, with a strong 11% world market share in the lucrative seamless Oil Country Tubular Goods (OCTG) segment. In 2006, TMK had approximately a 27% Russian market share for steel pipes and a 43% Russian market share for the technologically sophisticated seamless pipe segment, including a 67% Russian market share for OCTG pipes. TMK is also Russia's largest pipe exporter, non-domestic sales accounting for approximately 30% of the total sales volume for the year.

TMK — a strong company, operating in an attractive market

TMK's key competitive advantages:

- One of the leaders in the seamless OCTG pipes segment, a consolidated world business with high entry barriers.
- Focusing on the seamless pipes segment with continuously increasing demand in the mid-term.
- Technological integration in the value chain of customers in Russia and CIS, strengthening long-term partnerships with key customers.
- Leadership in the pipe industry with a dominant position in the seamless OCTG segment and a favourable base for the development of large-diameter welded pipes.
- Advantageous geographic distribution and specialised plants; implementation efficiency.
- Balanced stock of orders by nomenclature and regions.
- Competitive costs, differentiated production of seamless pipes and a rate of production ahead of customers requirements.
- Self-sufficiency in billets and an advantageous position in scrap; solid relations with suppliers of rolled steel and integrated supply management.
- Relatively low energy costs.

World ranking of countries by oil and gas reserves, 2005



	Gas	Oil
Russia	301	74
Saudi	43	264
Iran	168	137
Quatar	162	15
UAE	38	98
Iraq	20	115
Kuwait	10	102
Venezuela	27	80
Nigeria	33	36
USA	34	29

Source: BP, Wood Mackenzie, Credit Suisse research.

The market leader by far in the Russian/CIS market, one of the largest pipe markets with sustained growth opportunities

Russian oil and gas production has been increasing after a decade of decline following the collapse of the Soviet Union. Russia currently produces around one-eighth of global oil and gas and holds about 6 % of global oil and 27 % of natural gas reserves – though the reserve potential could be greater.

In 2006, TMK sold almost 3 million tonnes of steel pipes, including 1.93 million tonnes of seamless pipes of which 49 % are OCTG. Pipes for the oil and gas industry and "Premium" products accounted respectively for about 59% and 23% of total sales volume in 2006. TMK had a 69% domestic production share for OCTG and a 67% Russian market share of this technologically sophisticated segment.

As the leading Russian manufacturer of steel pipes, TMK also benefits from the strong Russian economy and current high levels of drilling and well completion activity inside the country. TMK further believes that in light of the relative under-investment in the oil and gas and power infrastructure in Russia since the collapse of the Soviet Union and the strong state support for the oil and gas industry, investment in oil and gas exploration, production and transportation in Russia and, consequently, demand for pipes for the oil and gas industry will continue to be strong.

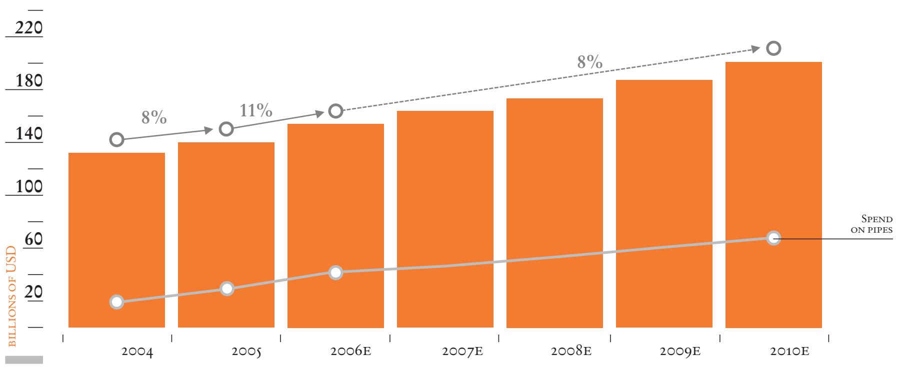
TMK's strong presence in the Russian market extends to almost all the main upstream oil and gas companies and TMK has a large share of the Russian majors' pipe demand. TMK's position is even stronger among its main domestic customers in seamless products, where it supplies more than two-thirds of the needs of the oil and gas industry companies.

Strong outlook for OCTG

The operating environment for oil and gas companies is becoming more complex, leading to increasingly capital-intensive drilling activity, such as offshore exploration and production drilling in challenging environments requiring technologically sophisticated pipes.

Strong demand for hydrocarbons in recent years and the decline in production at existing oil and gas fields have been primary drivers behind increasing exploration and production expenditures by oil and gas companies. According to the International Energy Agency, approximately 11% of exploration and production budgets of oil and gas companies are spent

Global Exploration & Production Expenses, (2004-2010E)



Source: International Energy Agency ("IEA"), Company estimates

on OCTG and approximately 40% of oil and gas pipeline construction costs are for seamless and welded line pipes and also for large diameter pipes.

TMK's product portfolio is strongly oriented towards higher value-added technologically sophisticated products necessary to the global oil and gas industry. OCTG is the most attractive market sub-segment with high margins and high expected demand growth.

OCTG is the segment where TMK has the highest relative exposure, with 32% of its current volume compared to 8% of total pipe market volume (*see diagram on page 27*). Line pipes and large diameter mains are second in attractiveness with:

- high market growth rates and relatively lower margins in large-diameter mains;
- relatively higher margins in line pipes.

Industrial seamless pipes are of lesser economic interest, while TMK considers industrial welded pipes as the relatively least attractive market sub-segment at this stage.

LEADER IN A CONSOLIDATED INDUSTRY WITH HIGH ENTRY BARRIERS

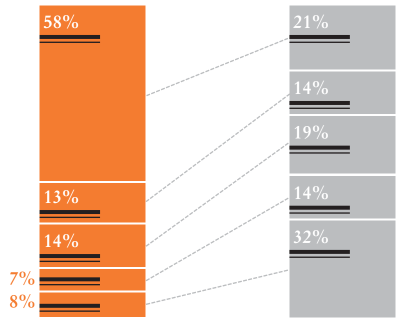
The global seamless pipe industry is characterised by:

- High entry barriers.
- A high degree of concentration with a small number of large international producers.
- High margins relative to other pipe products.

High entry barriers include:

- The capital-intensive nature of production.
- The technological sophistication of the production process and products.
- High technical requirements as to reliability, consistency and integrity of threading and couplings, especially in the OCTG segment.
- Availability of highly skilled specialists and the general level of development of the home country's economy.
- The need to be certified by state industrial bodies and qualified by oil and gas majors.

Comparison of global and TMK pipe output structure



	Share of global pipe output	Share of TMK pipe output
Welded industrial	58%	21%
Large diameter	13%	14%
Seamless industrial	14%	19%
Line pipe	7%	14%
OCTG	8%	32%

In Russia, TMK is the leader in the seamless pipe market and benefits from strong relationships with many of the principal oil and gas production and distribution companies, including Rosneft, Gazprom, Surgutneftegaz, TNK-BP and LUKOIL. TMK is qualified as an official supplier by a number of large international oil and gas companies including Shell, Saudi Aramco, KOC, KNPC and Agip KCO.

STRONG DEMAND FOR LARGE-DIAMETER WELDED PIPES

One of TMK's strategic products is large-diameter pipes used predominantly in oil and gas transportation.

The key driver here is global pipeline capacity either planned or requiring replacement. Currently there are some 90,000 km of pipelines planned or in actual construction across the globe of which 90% are intended for oil and gas transportation. Nearly 21% of these new projects (about 19,000 km) are in the former Soviet Union (fSU) and the Central and Eastern European (CEE) regions, TMK's main markets.

The pipe requirement for these projects is 45 million tonnes globally and 10 million tonnes for the projects in the fSU/CEE region. The replacement of aging global oil and gas pipelines, many over 30 years old will provide additional demand pull.

TMK is one of the most highly geared players toward this market segment, as it is the largest producer in Russia/CIS (with a 20.7% market share) and is one of the top 10 global producers, holding a 3.1% global market share. In March 2007, TMK and HAEUSLER (Switzerland) signed a contract for the supply of equipment for manufacturing large-diameter longitudinally welded pipes with a production capacity of 650,000 tonnes, thus doubling TMK's existing production capacity of such pipes.

HIGH EARNINGS GROWTH PROSPECTS – FIRSTLY THROUGH PRICING 'CATCH-UP'

The first element in the development of earnings is pricing growth. Average prices of seamless pipes are below its main competitors and TMK is expecting to significantly reduce this gap in the mid-term.

This gap will reduce as a result of the enhancement of product mix to more value-added products and the development of the marketing distribution network.

BEST-IN-CLASS VOLUME GROWTH POTENTIAL IN THE MEDIUM TERM

In addition to market price improvement (which should benefit every company in the sector), TMK expects to benefit disproportionately from its own volume growth prospects. TMK intends to increase seamless pipe capacity by 60% and large-diameter welded pipe capacity by 150%. Heat-treatment capacities will also be doubled.

TMK has the largest volume growth programme in the Russian pipe industry and more than half of TMK's growth in seamless capacity is expected to come from the OCTG market segment.

STRUCTURAL COST ADVANTAGE

Russia is a low-cost region for pipe production which provides TMK with cost advantages over its principal international competitors in the global seamless pipe market:

- The biggest structural advantage is in scrap prices, the single-biggest cost item in pipe manufacture. Russia is one of the largest sources of scrap in the world and domestic prices are somewhat lower than international prices, primarily due to lower supply chain costs. TMK is one of the largest domestic scrap consumers and in-house scrap yards provide a further cost advantage.
- TMK is also expanding its steel-making capacity and self-sufficiency in billets will reach 90% in 2007. TMK is able to achieve cost savings by reducing costs of seamless pipes production.
- TMK's unit labour costs, gas and electricity costs and seamless pipe raw material costs are all lower than those of its principal international competitors.
- Seversky and Sinarsky are located in the Urals region near transport routes linking Russian industrial centres with the oil and gas regions of Western and Eastern Siberia, thus assisting in reducing transportation costs.

VERTICALLY-INTEGRATED PRODUCER

Having internal steel-making capabilities also gives TMK a greater degree of quality and production cost control over the steel used in its pipe-making operations and reduces the cost of purchased billets. The steel-making plant, TMK-Resita (Romania), is also part of the TMK group of companies.

TMK continuously increases the amount of billets supplied from its other plants to Sinarsky, which does not have internal steel-making capabilities, thus reducing Sinarsky's dependence on billets purchased from third-party suppliers.

STRONG EXPORT PLATFORM

TMK was the leading pipe exporter in 2006, with an estimated 56% share of all steel pipe exports from Russia, an estimated 70% share of total seamless pipe exports, an estimated 75% share of OCTG exports and an estimated 84% share of total line pipe exports.

Two of TMK's plants, Volzhsky and TAGMET, are strategically located in the southwestern part of Russia near the Black Sea shipping routes, the Volga River and transit routes to the Caspian region, giving them a strong export orientation.

TMK's two Romanian plants, TMK-Artrom and TMK-Resita provide a strong base for the export of TMK's pipes to European markets, especially after Romania's entry into the EU.

5(2) About the Company

KEY RISKS

High dependence on a small group of customers

Approximately 39% of TMK's total sales volumes came from its top 10 customers in 2006. The largest customers for TMK's seamless pipes in the Russian market are Surgutneftegaz, TNK-BP, LUKOIL, Gazprom and Tatneft. These companies accounted for 32% of TMK's total seamless pipes shipment volumes in 2006. The main customer for TMK's welded pipes is Gazprom which accounted for 25% of total welded pipe shipments in 2006.

This level of dependence on a few customers could have mixed impacts. On the one hand, this can be seen as a risk, since dependence and low customer base diversification could lead to a higher degree of volatility in TMK's pipe business. On the other hand, it evidences strong relationships between TMK and its key customers. TMK considers that these strong relationships outweigh the risk.

Protectionism and trade barriers

The European Union has imposed anti-dumping duties on imports of seamless pipes. The US may also set anti-dumping duties. US and EU manufacturers are seeking positive outcomes on "sunset reviews" and may lobby for the introduction of more measures in the future, if economic harm to the industry becomes apparent.

The EU protectionist activity had a material impact on the seamless pipe sector in the second half of 2006. Going forward, TMK believes it is unlikely that protectionism in the EU will increase with respect to the seamless pipe market. TMK considers that a review of measures, leading to a subsequent reduction in duty levels, is more likely.

Increase in the cost of raw materials and energy resources

One of the main factors affecting the competitiveness of TMK's pipe products is the price for scrap metal, strips, sheet metal and tube billets. The increase in domestic steel and scrap metal prices could have a negative impact on TMK's business results. TMK believes, however, that its costs of primary raw materials will remain lower than those of its international competitors due to the more extensive use of scrap metal in the production of seamless pipes and the lower prices for scrap metal.

Energy resources make up nearly 4.5% of TMK's production cost and consist primarily of purchased electricity and gas. The growth in prices for energy resources could have a negative impact on TMK's business results. Despite, however, the possible increase in prices for energy, TMK will still have an advantage in comparison with its main international competitors due to the low level of Russian domestic tariffs.

Currency risk

TMK's products are typically priced in roubles for Russian sales and in US dollars for CIS and international sales. Direct costs, including raw materials, labour and transportation costs are largely incurred in roubles, while other costs, such as interest expenses, are incurred in roubles, US dollars and euros; capital expenditures are incurred principally in euros. The mix of revenues and costs is such that appreciation in real terms of the Russian rouble versus the US dollar tends to result in an increase in TMK's costs versus its revenues, while depreciation in real terms of the Russian rouble versus the US dollar tends to result in a decrease in costs versus revenues. At the same time, appreciation in real terms of the Russian rouble versus the US dollar results in an increase in TMK's capitalisation in dollars.

TMK is seeking to bring its financial liabilities in foreign currency in line with export net sales, thus mitigating currency risk. In recent years the effect of the Russian rouble appreciation versus the US dollar has been more than offset by increased prices for TMK's tubular goods, both domestically and internationally. As there can be no assurance that such a trend will continue in the future, TMK is considering the use of derivative instruments, including forward contracts to manage its foreign exchange risks with respect to currency fluctuations of the US dollar versus the Russian rouble.

Interest-rate risk

TMK's credit portfolio includes loans taken out at a floating interest rate. At the end of 2006, these loans, broken down by currencies, amounted to EUR 91 million and USD 169 million. Euro LIBOR and dollar LIBOR served as the basis for the calculation of interest rates on these loans.

As these loans accounted for only 30% of the total loan portfolio, TMK considers such risks immaterial and is not using instruments to hedge such interest-rate risks at present. Nevertheless, TMK monitors interest rates and will use instruments to hedge such risk as necessary.

Credit risk

TMK pays considerable attention to credit risk attributable to indirect loans provided by TMK to a number of customers. These loans usually take the form of deferrals on payments for products.

Credit is only offered to customers who are major Russian and foreign companies that have been working with TMK for a protracted period of time and have strong credit histories.

To manage the risk of payment arrears, TMK monitors the status of payables and receivables on a daily basis and has set up an Accounts Receivable and Accounts Payable Committee. In addition, TMK has developed procedures aimed at preventing payment arrears and ensuring effective collection. Comprehensive implementation of these measures enables TMK to substantially reduce credit risk.

5(3)
About the Company

ORGANISATIONAL STRUCTURE

TMK structure

PRODUCTION – RUSSIA	PRODUCTION – ABROAD[1]	SALES AND MARKETING	R&D AND SERVICES
100% VOLZHSKY PIPE PLANT	80,6%[4] TMK–ARTROM SA	100% TRADE HOUSE "TMK"	100% TMK TRANS
93%[2][3] SEVERSKY TUBE WORKS	99,5% TMK–RESITA SA	100% TMK GLOBAL AG	76,3%[5] ROSNITI
92,4%[3] SINARSKY PIPE PLANT		100% TMK NORTH AMERICA	
95,7%[3] TAGANROG METALLURGICAL WORKS		100% TMK MIDDLE EAST	
75%[5] ORSKY MACHINE BUILDING PLANT		100% TMK SINARA HANDEL GMBH	
51%[5] TMK–CPW		100% EUROSINARA	
		100% TMK–KAZAKHSTAN	

Note: Ownership precentages are rounded up to first decimal.
(1) *Owned through TMK Sinara Handel GmbH.*
(2) *3.22% of shares are traded in the form of ADR.*
(3) *Remaining ownership is listed and traded on RTS.*
(4) *Shares are listed on Bucharest Stock Exchange.*
(5) *Acquisitions or establishment of new entities after 31 December 2006.*

TMK conducts all of its production, sales and marketing operations through subsidiaries. TMK organisational structure represents the main production, trade, and logistics companies within TMK, showing TMK total direct and indirect ownership in these companies as at 31 December 2006.

Production

In 2006, TMK conducted all its manufacturing operations at six plants:

- Volzhsky, producing steel billets, seamless and welded large-diameter pipes, is located in Volzhsky, Volgograd region, Russia.
- Seversky, producing steel billets, seamless and industrial welded pipes, is located in Polevsky, Sverdlovsk region, Russia.
- TAGMET, producing steel billets, seamless and industrial welded pipes, is located in Taganrog, Rostov region, Russia.
- Sinarsky, producing seamless pipes, is located in Kamensk-Uralsky, Sverdlovsk region, Russia.
- SC TMK-Artrom, producing seamless pipes, is located in Slatina, Olt region, Romania.
- SC TMK-Resita, producing steel billets, is located in Resita, Caras-Severin region, Romania.

Sales and Marketing

- Trade House TMK, incorporated in the Russian Federation, is primarily responsible for sales of TMK's products in Russia and other CIS markets. Trade House TMK has branches or representative offices in several countries.
- TMK Global AG, incorporated in Switzerland, is primarily responsible for the distribution of TMK's tubular goods to customers outside Europe, Russia and the CIS countries. TMK Global operates a network of trade representatives, agents and distributors and has subsidiaries in the UAE and the USA.
- TMK Sinara Handel GmbH, incorporated in Germany, currently distributes TMK's products in Europe.

Research and Development

The following significant event after 31 December 2006 is worth mentioning:

- Acquisition of OAO Rossiisky Nauchno-Issledovatelsky Institut Trubnoi Promyshlennosti (RosNITI). In March 2007, OAO "TMK" acquired a majority stake in OAO Rossiisky Nauchno-Issledovatelsky Institut Trubnoi Promyshlennosti, the biggest industry research and pipe technology centre in Russia.

Production facilities

TMK produces pipes at five of its operating plants: Volzhsky, Seversky, Sinarsky, TAGMET and TMK-Artrom. TMK also produces steel at four of its plants: Volzhsky, Seversky, TAGMET and TMK-Resita.

TMK is currently carrying out its strategic capital expenditure programme for 2004–2010 which focuses on upgrading production facilities, as well as on increasing the efficiency of production processes.

The following significant events occurred after 31 December 2006:

- Acquisition of OAO Orsky Machine Building Plant. In January 2007, TMK acquired 100% of the voting shares in Orsky Machine Building Plant, a Russian manufacturer of tool joints (important parts of drill pipes and drilling accessories) to enhance TMK's premium drill pipe business. Orsky Machine Building Plant's principal customers include Surgutneftegaz, TNK-BP and Gazpromneft.

- Joint Venture with Corinth Pipeworks. In January 2007, Seversky and Corinth Pipeworks S.A., a leading producer of welded pipes in Greece, established a joint venture for the production of electric resistance longitudinally welded ("ERW") 168–530-mm pipes, mainly used in oil and gas, construction and machine-building applications. Annual production capacity of this JV will be 300 thousand tonnes.

VOLZHSKY PIPE PLANT. Volzhsky is TMK's largest plant, featuring modern steel-making, pipe-rolling and pipe welding equipment. The plant is located close to rail, road and river transport routes and is linked by the Volga River to ports on the Caspian, Black, Baltic and Azov Seas.

Volzhsky manufactures pipes of more than 800 sizes for various applications, including seamless casing and line pipes, spiral welded large-diameter pipes for oil pipelines, seamless pipes for steam boilers, seamless mechanical pipes and round and square steel billets. Volzhsky products are certified in accordance with Russian (CIS) and international standards, and technical documents (TU). Volzhsky also holds an API Monogram License allowing the plant to put the API Monogram on its products in accordance with API Q1, API Spec 5L (5L-0251), and Spec 5CT (5CT-0324). The plant applies the following certification systems:

- Quality Management System (ISO 9001:2000);
- Environmental Management System (ISO 14001:2004).

Volzhsky received certification as an official supplier from Saudi Aramco – one of the world's largest oil producers.

Volzhsky is currently the largest pipe manufacturer in Russia and one of two Russian plants producing 1420-mm pipes for high-pressure transportation gas pipelines in commercial volumes. Volzhsky supplies its entire output of spiral welded 1420-mm pipes to Gazprom.

SEVERSKY TUBE WORKS. Seversky is located in the Sverdlovsk region, in close proximity to the major Russian oil and gas fields of Western Siberia.

Seversky produces a variety of seamless and welded pipes principally for domestic oil and gas customers, including seamless casing, line and electric welded line pipes, as well as industrial seamless general purpose pipes and industrial welded pipes for the automotive and power industries. Seversky products are certified in accordance with Russian (CIS) and international standards, and technical documents (TU). Seversky also holds an API Monogram License allowing the plant to put the API Monogram on its products in accordance with API Q1, API Spec 5L (5L-0271), and Spec 5CT (5CT-0351). The plant applies the following certification systems:

- Quality Management System (ISO 9001:2000);
- Environmental Management System (ISO 14001:2004);
- Occupational Health and Safety Management System (OHSAS 18001:1999).

Taganrog Metallurgical Works. Taganrog Metallurgical Works (TAGMET) is located in the Rostov region, near the Azov Sea, and benefits from its close proximity to raw materials and sea export routes.

TAGMET produces principally drill pipes, casing and line pipes, industrial seamless pipes and electric welded pipes. TAGMET products are certified in accordance with Russian (CIS) and international standards, and technical documents (TU). TAGMET also holds an API Monogram License allowing the plant to put the API Monogram on its products in accordance with API Q1, API Spec 5L (5L-0327), Spec 5CT (5CT-0423), and Spec 5D (5D-0054). The plant applies the following certification systems:

- Quality Management System (ISO 9001:2000);
- Environmental Management System (ISO 14001:2004);
- Occupational Health and Safety Management System (OHSAS 18001:1999).

TAGMET also operates its own research and development unit specialising in pressure`-tight Premium connections for drill pipes, casing and tubing string.

Sinarsky pipe plant. As with Seversky, Sinarsky is located in the Sverdlovsk region. Sinarsky is the only plant in Russia built to supply primarily the oil and gas industry.

Sinarsky specializes in producing drill pipes, casing, tubing and line pipes as well as special grade seamless steel pipes principally for the power, chemical and machine-building industries. In 2006, OCTG accounted for approximately 62% of Sinarsky's total output. Sinarsky products are certified in accordance with Russian (CIS) and international standards, and technical documents (TU). Sinarsky also holds an API Monogram License allowing the plant to put the API Monogram on its products in accordance with API Q1, API Spec 5L (5L-0330), Spec 5CT (5CT-0427), and Spec 5D (5D-0056). The plant applies the following certification systems:

- Quality Management System (ISO 9001:2000);
- Environmental Management System (ISO 14001:2004);
- Occupational Health and Safety Management System (OHSAS 18001:1999).

Sinarsky does not have any in-house steel-making capacity and obtains steel billets from Volzhsky, Seversky, TAGMET and third-party suppliers.

Romanian plants

TMK-Artrom. TMK-Artrom, a leading Romanian pipe manufacturer, is located in Slatina in southern Romania.

The plant produces seamless pipes for industrial applications, including for the mechanical engineering and automotive industry. Clients also include oil and gas and energy companies, construction companies and utility companies. In 2006, TMK-Artrom had a 22% share of the European market for industrial seamless pipes. More than 80% of the plant's output is intended for export, mainly to the EU, the USA and Canada.

TMK-Artrom does not have any in-house steel-making capacity and is supplied by TMK-Resita as well as Volzhsky.

Its products are certified in accordance with national and international standards as well as European directives. TMK-Artrom holds an API Monogram License allowing the plant to put the API Monogram on its products in accordance with API Q1, API Spec 5L (5L-0352), and Spec 5CT (5CT-0440). The plant applies the following certification systems:

- Quality Management System (ISO 9001:2000);
- Environmental Management System (ISO 14001:2004).

TMK-Artrom is one of Europe's largest producers of seamless hot-rolled and cold-drawn pipes. In February 2007, a new pipe-manufacturing line was put into operation – a Cross Piercing Elongator. As a result, the production capacity of TMK-Artrom now reaches 200,000 tonnes per year.

TMK-Resita. TMK-Resita is located in Resita, in southwestern Romania, approximately 400 km from TMK-Artrom. The plant has more than 260 years of history and experience in producing steel and rolled products.

TMK-Resita produces tubular billets for TMK-Artrom and other consumers, as well as heavy round profiles, blooms and square billets. In February 2007, TMK-Resita launched a new continuous-casting line for blanks, with a capacity of 450,000 tonnes per year. From 2007, the majority of TMK-Resita's steel production will be delivered to TMK-Artrom.

The plant's products are certified in accordance with national and international standards as well as European directives. The plant applies the Quality Management System (ISO 9001:2000).

5(4) About the Company

PRODUCTS

TMK produces and distributes a wide range of pipe products for use in the oil and gas, machine-building, chemical and petrochemical, power, automotive, construction, aviation and aerospace industries.

TMK's products include seamless and welded pipes of various diameters, coatings and wall thicknesses. TMK's pipes are made of carbon, stainless and heat-resistant grades of steel, titanium and nickel alloys and composite metals. TMK's companies have the technological capability and equipment to manufacture anti-corrosion and insulating coatings.

The main advantages of seamless pipes are the high degree of structural uniformity of the metal, greater strength and corrosion resistance which allows them to be used in critical structures and as parts of machines and mechanisms.

Large-diameter welded pipes tend to be used principally for oil and natural gas pipeline transportation systems as well as drainage systems, fuel pipelines and other product pipelines.

The ability to meet customer product specification and quality requirements is a key differentiating factor in the modern tubular market. This is particularly true of products for the oil and gas industry which are often used in aggressive environments such as the northern regions of Russia and the ocean shelf. These pipes must meet both international quality standards and the requirements of each individual customer.

Pipes for the oil and gas industry are subject to strict requirements with respect to functional reliability and structural strength and need to be adjusted to the particular chemical composition of the petroleum and to temperature conditions.

TMK will continue to enhance its product range of pipes and connections that can better withstand aggressive environments: high pressure, high temperature, sub-surface and offshore oil and gas wells and horizontal drilling.

Seamless pipes

TMK is the leading producer of seamless pipes in Russia and one of the three largest seamless pipe producers in the world. TMK accounted for an estimated 6.74% world market share of seamless pipe production in 2006 in terms of volume.

TMK produces 1–426 mm seamless pipes with wall thickness of 0.1–65 mm and sells its seamless products principally to the oil and gas industry.

TMK's seamless product range:

- OCTG include drill pipes, casing for work-overs and tubing string. Drill pipes are used for lowering and raising the drill bit, transmitting rotational force, creating axial load on the tool and sending drilling mud or compressed air into the well. Casing is used to reinforce the walls of oil and gas wells during drilling and exploitation. Pipes for work-overs are used in maintenance of the production casing string of oil and gas wells. Tubing string is used during the exploitation of oil and gas wells to transport liquids and gases inside the casing for repairs and round-trip lowering and raising operations.

» Seamless line pipes are used to construct the main short-distance oil and gas pipelines and to transport crude oil, oil products and natural gas from wells to storage tanks, loading and distribution centres.

» Industrial seamless pipes are used for various industrial applications, including machinery, chemical and petrochemical applications as well as in the power and automotive industries. Industrial seamless pipes are also used to build pipelines that require high-performance pipes for the transportation of high-pressure steam, water, gas and air.

Welded pipes

TMK produces both longitudinally (industrial) and spiral welded pipes with a diameter of 8–2,520 mm and wall thickness of 1–25 mm.

Longitudinally welded pipes are made from steel plate with only one weld seam joining the two edges of the rolled plate. Spiral welded pipes are manufactured through the welding of rolled steel coils. In contrast to longitudinally welded pipe production, where each pipe diameter requires an exact plate width, various diameters of spiral welded pipe can be manufactured from a single steel coil width which is technologically and economically more effective.

Large-diameter welded pipes are used to construct the main oil and gas pipelines for long-distance transportation of crude oil and natural gas. TMK is one of the main producers of 1,420 mm pipes for Gazprom. In March 2007, TMK and HAEUSLER (Switzerland) signed a contract for the supply of equipment for manufacturing large-diameter longitudinally welded pipes with a production capacity of 650,000 tonnes, thus doubling TMK's existing production capacity of such pipes.

Steel billets

Steel billets are square or round semi-finished steel products used in the production of seamless pipes as well as other finished steel products. Billets can be supplied in various diameters and lengths, depending on the need for further processing. TMK made a significant technological advance in the production of billets in 2006, ending the production of billets from ingots and moving to continuous casting of billets. It will allow TMK to raise significantly its production volumes and to enhance the quality of products and reduce costs. TMK has installed continuous casting machines at its Volzhsky, Seversky, TAGMET and TMK-Resita plants.

Product quality standards

All of TMK's products are manufactured in accordance with a variety of internationally recognised and accepted standards set by the following standardisation bodies:

- American Petroleum Institute (API standards);
- ASTM International (ASTM standards);
- American Society of Non-destructive Testing (ASNT standards);
- German Standardisation Institute (Deutsches Institut fur Normung, DIN standards);
- Technical Inspection Association (Technischer Uberwachungs-Verein, TUV standards);
- International Standardisation Organisation (ISO certifications);
- The Russian Federal Agency on Technical Regulation and Metrology (national GOST R standards);
- Interstate Council for Standardisation (GOST standards);
- European Committee for Standardisation CEN (EN);
- French standards association (AFNOR), etc.

The compliance of the quality management systems and products with foreign, national, regional and industry standards is also confirmed by such well-known certification bodies as:

- Romanian State Inspection for Construction for authorisation of test laboratories;
- Germanischer Lloyd;
- LANDESMATERIAL PRUFAMT Sachsen-Anhalt Magdeburg for the U-sign;
- Technological and Test Institute for Construction Prague-Czech Republic for the constructions tubes;
- IQNet QMI quality certification bureau (Canada);
- Bureau Veritas Quality International (BVQI);
- RW TUV (Germany);
- TUV CERT NORD (Germany);
- DVGW (Germany);
- Product testing laboratory (University of Brescia, Italy).

To ensure compliance with industry standards and performance specifications, as well as the international competitiveness of TMK's products, each of TMK's plants has implemented an extensive quality management system. Currently, TMK holds Quality System Certification ISO 9001:2000 for all its manufacturing operations. The certification was granted by Germanischer Lloyd Certification (with respect to TMK-Resita and TMK-Artrom), TUV NORD Cert

Germany (with respect to Volzhsky), Bureau Veritas Quality International (with respect to Seversky) and the Quality Management Institute (with respect to Sinarsky and TAGMET). The American Petroleum Institute Spec Q1 license was granted by the American Petroleum Institute (with respect to Seversky, Sinarsky, Volzhsky, TAGMET and TMK-Artrom).

The ISO 9001:2000 Quality Management System is intended to ensure that the end product complies with applicable standards and customer quality requirements, from the acquisition of raw materials to the delivery of the final product.

The API Spec Q1 license takes into account all ISO 9001:2000 requirements as well as additional requirements on the quality management system for product suppliers to the oil-and-gas sector.

TMK products must also satisfy customer requirements. Many international oil and gas companies only buy pipes from qualified suppliers whose specific kinds of tubular goods have been certified. These companies often keep official lists of qualified suppliers. Since the beginning of 2005 TMK's Russian plants have received qualifications for various kinds of pipes from a number of large international oil and gas companies including Shell, Saudi Aramco, KOC, KNPC, Agip KCO. TMK continues to actively seek qualification from major global oil and gas companies as a way of increasing market recognition of its products globally.

stable
growth

EFFICIENCY

TMK ANNUAL REPORT 2006

+81%

PROFIT

Net profit increased by 81% in 2006 compared to 2005

6
Management Discussion and Analysis

Our financial review is based on and should be read in conjunction with the audited consolidated income statements of TMK and the related notes included elsewhere in this annual report. The financial review compares TMK's results on a consolidated basis for the fiscal year ended 31 December, 2006 with its results for the fiscal year ended 31 December, 2005. TMK prepares its consolidated income statements in accordance with International Financial Reporting Standards (IFRS).

Overview

In 2006, according to TMK estimates, TMK has retained the leading position on the Russian steel pipe market with an approximate 27% market share by sales volumes and a 67% market share by sales volume of the higher-margin OCTG products. TMK is also among the world's three largest steel pipe producers with a relatively high market share of approximately 11% in the OCTG segment. In 2006, TMK sold almost 3 million tonnes of steel pipes including 1.93 million tonnes of seamless pipes of which 946 thousand tonnes were OCTG. Pipes for the oil and gas industry accounted for approximately 59% of the total sales volume in 2006. TMK is also Russia's largest exporter of pipes, with sales outside of Russia accounting for approximately 56% of all Russian steel pipe producers' exports. In 2006, sales outside of Russia accounted for approximately 30% of the total sales volume.

In 2006, TMK continued the development of its seamless pipe business which has the higher margins and better growth opportunities, together with a mixed growth/protection strategy in the welded segment. TMK divides its pipes business into two main business segments and five principal product lines. The two main business segments are seamless pipes, consisting of seamless OCTG, seamless line pipes and seamless industrial pipes, and welded pipes, consisting of large-diameter welded pipes and industrial welded pipes. In 2006, annual production capacity was approximately 3.9 million tonnes of pipes, including 2.1 million tonnes of seamless pipes. TMK also operates its own steel-making facilities. In 2006, TMK produced approximately 2.1 million tonnes of steel.

Within the framework of the strategic investment programme for 2004 – 2010, focused on increasing the efficiency of its production processes and increasing seamless pipe production, TMK has spent USD 251.2 million in capital expenditures on its seamless pipe production in 2006. Pipe production capacity increased by approximately 100 thousand tonnes to 3.9 million tonnes in 2006 as compared to 2005 and, in particular, seamless pipe production capacity increased by 80 thousand tonnes to 2.1 million tonnes.

In 2006 as compared to 2005, consolidated revenue increased by 15% to USD 3,384.4 million and profit before tax increased by 77% to USD 618.5 million.

Acquisitions

On June 10, 2005, TMK signed an agreement for the purchase of a 100% ownership interest in Sinara Handel GmbH, an entity registered in Germany. Sinara Handel GmbH is TMK's distributor of pipe products in Europe and the supplier of certain types of raw materials and equipment. Sinara Handel GmbH owns controlling interests in a pipe plant (SC Artrom SA) and a metallurgical plant (SC C.S.R. SA) in Romania. Title transferred to TMK and control over Sinara Handel GmbH was obtained by the Group on March 1, 2006. TMK has applied the pooling of interests method with respect to this acquisition and presented its consolidated financial statements as if the transfer of the controlling interest in Sinara Handel GmbH had occurred from the beginning of the earliest period presented.

In December 2000, TMK acquired an initial 50% interest in Eurosinara S.r.L., an Italian company which acts as TMK's distributor of pipe products in Italy and other European countries. On May 16, 2006, TMK acquired the remaining 50% interest in Eurosinara for EUR 1.0 million (USD 1.3 million at the exchange rate as of May 16, 2006). As of the date of acquisition, Eurosinara had net liabilities of USD 9.8 million, and a reduction in accumulated profits was recorded in the amount of USD 4.9 million in TMK's financial statements for the year ended December 31, 2006 with respect to the 50% interest in Eurosinara held prior to obtaining control over Eurosinara. Goodwill of USD 6.2 million was recorded in connection with the acquisition of control of Eurosinara. Eurosinara recorded a net profit of USD 1,051 thousand for the period from May 16, 2006 to December 31, 2006.

From time to time TMK acquires shares in its subsidiaries: in the year ended December 31, 2006, TMK purchased 1.31% of OAO "Sinarsky Pipe Plant" shares, 1.37% of OAO "Seversky Tube Works" shares and 0.42% of OAO "Taganrog Metallurgical Works" shares for a total of USD 21.7 million.

Recent developments

On August 25, 2006, TMK signed an agreement for the purchase of a 75% ownership interest in open joint-stock company "Orsky Machine Building Plant" (OMZ) for USD 45.5 million from an entity under common control with TMK. Title transferred to TMK and control over "Orsky Machine Building Plant" was obtained by TMK on January 31, 2007. On February 1, 2007, a management agreement was signed under which TMK became the sole managing authority of OMZ. Prepayment for the 75% ownership interest in the amount of USD 45.5 million was made on November 9, 2006. The integration of OMZ, the sole Russian manufacturer of tool joints, the most critical components for drill pipes, into TMK will enhance TMK's competitive position on the Russian market of drill pipes. Moreover, the purchase of OMZ will enable TMK to consolidate its production platform for further downstream expansion by in-house manufacture of drilling tools and oilfield accessories thus strengthening the "single source of supply" approach.

On March 5, 2007, TMK purchased a 76.33% ownership interest in joint-stock company "Russian Research Institute of the Tube and Pipe Industries" (RosNITI) for USD 3.1 million. RosNITI is the sole scientific research institution engaged in the scientific and technological development of the Russian pipe industry and will contribute significantly to TMK's production technology development.

The Global and Russian industry growth drivers

The majority of TMK's steel pipe sales are carried out on the Russian market. The demand for seamless and welded steel pipes from the Russian oil and gas producers driven by the increased drilling activity has a significant influence on the general level of volumes and prices for TMK's products. High pipeline replacement demand from the Russian oil and gas sector is becoming evident after years of under-investment. Russia currently has more than 225 thousand km of long-distance oil transmission pipelines (owned by Transneft, Gazprom and Transnefteprodukt), and a major part of the infrastructure requires significant modernisation or replacement investment. These factors have strengthened the strong demand for large-diameter welded pipes. At the same time, spending growth in oil and gas exploration and production (E&P), strongly encouraged by the government in recent years, has become a key driver for OCTG production.

Sales to oil and gas companies worldwide represent a high percentage of TMK's total sales and demand for seamless and welded steel pipes from the global oil and gas industry is a significant factor affecting TMK's results.

Global demand for seamless and welded pipes is increasingly strongly driven by such factors as rising drilling activity and rig count and higher well complexity. E&P spending by oil and gas companies worldwide has recently increased sharply predominantly due to higher oil prices pushed by resilient global energy demand, depleting existing capacities, the political and socio-economic conditions of oil-producing countries, the persistent political uncertainty in the Middle East region and continuing economic growth in China and Asia. Moreover, new drilling activity is increasingly occurring at greater depths and in more corrosive environments, leading to an increase in demand for high value seamless pipes. According to International Energy Agency (IEA) expectations, global E&P spending will grow by 8% per annum in 2006–2010. IEA estimates that approximately 11% of E&P budgets are spent on OCTG pipes and approximately 40% of pipeline construction costs are spent on line pipes.

Management believes that, if global demand for oil and gas remains at the current level, the factors which have resulted in the high oil prices and the increased drilling activity and demand for pipes from the oil and gas industry shown in 2006 will persist in the near to medium term due to the long lead times and significant capital expenditures required for the development of major new oil and gas reserves.

Russian macroeconomic trends

Most of TMK's operations are based in Russia, and TMK generates a significant proportion of its sales in Russia, with 68% and 69%, respectively, of total net sales being made in Russia in 2006 and 2005, respectively. As a result, Russian macroeconomic trends, including the overall growth in the economy and in the markets in which TMK operates, significantly influence the results of operations, particularly the sales of industrial seamless and welded pipes. The table below summarises certain key macroeconomic indicators relating to the Russian economy in 2006 and 2005:

	2006	2005
GDP growth	6.7%	6.4%
Consumer price index	9.7%	10.9%
Unemployment rate	6.9%	7.6%

Source: Central Bank of Russia

Russian economic growth, driven by high prices for oil, gas and commodity products in international markets, has also resulted in the growth in Russia's federal budget surplus which has been a significant factor behind federal government spending and increasing support for the development of Russia's infrastructure. These factors have resulted in both increased Russian consumption of pipes in 2006 by 24.5% as compared to 2005, including an increase in consumption of large diameter pipes by 28% and OCTG pipes by 31%, and in increases in the cost of raw materials and other costs of production, such as labour and energy.

Currency exchange fluctuations

TMK's products are typically priced in roubles for Russian sales and in US dollars for CIS and international sales except for the European Union (in euros) and Romania (in Romanian lei). Direct costs, including raw materials, labour and transportation, are largely incurred in roubles, capital expenditures are incurred principally in euros and other costs, such as interest expense, are incurred in roubles, US dollars and euros. As a consequence, TMK is exposed to currency rate fluctuations between the rouble and both the US dollar and the euro.

The table below shows the nominal exchange rate and real rouble appreciation against the US dollar and the euro for the years ended December 31:

	2006	2005
Nominal exchange rate (roubles per US dollar) (1)	27.19	28.29
Real rouble appreciation against US dollar (2)	10.7%	10.8%
Nominal exchange rate (roubles per euro) (1)	34.11	35.26
Real rouble appreciation against euro (2)	11.5%	12.1%

(1) *The weighted average of the exchange rates on each day during the relevant period.*
(2) *Real rouble appreciation against the US dollar or the euro, as the case may be, is consumer price index adjusted for nominal exchange rate changes over the same period.*
Source: Central Bank of Russia

Segments

TMK prepares its consolidated financial statements in two segment reporting formats: business and geographical. (*See Note 1 to the Consolidated Financial Statements for the year ended December 31, 2006.*) There are no sales or other transactions between the business segments.

Business segment

The primary segment reporting format is business segments which presents net sales, gross profit, assets, liabilities and depreciation costs based on the main groups of products segregated into seamless pipes, welded pipes and other operations comprising principally the sale of steel billets to third parties.

Geographical segment

The secondary segment reporting format is geographical segments. In the financial statements, net sales are disclosed based on the location of the customer, not by the location of the end-user. Segment assets and long-term investments are based on the location of the assets.

Results of operations

The following table sets forth the consolidated operating results as a percentage of revenue for the years ended December 31:

	2006	2005
Revenue	100.0%	100.0%
Cost of sales	(69.4)%	(74.6)%
Gross profit	**30.6%**	**25.4%**
Selling expenses	(5.3)%	(5.0)%
Advertising and promotion expenses	(0.2)%	(0.1)%
General and administrative expenses	(4.7)%	(4.2)%
Research and development expenses	(0.2)%	(0.2)%
Other operating expenses	(0.8)%	(0.9)%
Other operating income	0.3%	0.0%
Foreign exchange (loss)/gain, net	0.4%	(0.5)%
Finance costs	(2.3)%	(2.7)%
Finance income	0.5%	0.1%
Profit before tax	**18.3%**	**11.9%**
Income tax	(4.7)%	(3.2)%
Net profit	**13.6%**	**8.7%**
Attributable to:		
Equity holders of the parent entity	13.0%	8.4%
Minority interests	0.6%	0.3%

Revenue

In 2006 as compared to 2005, TMK revenue increased by 15% and amounted to USD 3,384.4 million. Revenue represents total sales to customers net of value-added tax. Consolidated revenue increased due to a combination of higher average selling prices and higher sales volumes for pipe products.

Sales volumes

The following table shows pipe sales volumes for the years ended December 31:

THOUSANDS OF TONNES, %

	2006	2005	% CHANGE
Russia	1,266	1,154	9.7%
Outside Russia	662	740	(10.5)%
Seamless pipes	**1,928**	**1,894**	**1.8%**
Russia	839	949	(11.6)%
Outside Russia	230	97	137.1%
Welded pipes	**1,069**	**1,046**	**2.2%**
Total pipes	**2,997**	**2,940**	**1.9%**
of which Russia	2,105	2,103	0.1%
Outside Russia	892	837	6.6%

Seamless pipe sales growth has been primarily driven by continuing strong demand from oil and gas companies as a result of increased drilling activity in the oil and gas sector. In particular, sales volumes of the highest margin products, seamless OCTG for the oil and gas industry increased by approximately 16% in 2006 as compared to 2005. In 2006, production of seamless pipes was at full capacity which explains the relatively small increase in seamless pipes sales as compared to 2005. In 2006, there were lower sales of industrial seamless pipes compared to 2005 as seamless production capacity was redeployed to focus on the production of OCTG.

There was a relative redistribution of seamless pipes sales volumes between the non-Russian and the Russian markets. A decrease in exports of seamless pipes from Russia attributable to anti-dumping procedures established in the European Union was compensated by increased sales in the Russian market.

The increase in welded pipes sales in 2006 as compared to 2005 was predominantly attributable to the increased sales of industrial welded pipes of which the growth was driven by increasing demand from the building sector. Sales volumes of large-diameter welded pipes in the Russian market decreased in 2006 as compared to 2005 due to lower demand from Gazprom. The decrease was attributable to the completion of two significant construction projects: the Yamal-Europe gas pipe line (section Northern Tyumen Oblast–Torzhok) and Blue Stream (section Pochinki–Izobilnoye) in the first half of 2006. The decrease of large-diameter welded pipes sales in the Russian market was compensated by the growth of sales volumes in Central Asia and the Caspian region driven by the Kazakhstan government's gas pipe lines modernisation programme (Central Asia–Centre pipeline).

Revenue by business segment

The following table shows revenue by business segment for the years ended December 31:

MLN OF USD, %

	2006	2005	% CHANGE
Seamless pipes	2,216.1	1,788	23.9%
Welded pipes	949.0	912.9	4.0%
Other operations	219.3	237.3	(7.5)%
TOTAL REVENUE	**3,384.4**	**2,938.2**	**15.2%**

The following table shows revenue by business segment as a percentage of total revenue for the years ended December 31:

	2006	2005
Seamless pipes	65.5%	60.8%
Welded pipes	28.0%	31.1%
Other operations	6.5%	8.1%
TOTAL NET SALES	**100%**	**100%**

SEAMLESS PIPES. In 2006, TMK recorded both higher average selling prices and higher sales volumes for seamless pipes largely attributable to increased demand from the oil and gas industry in the light of the high levels of hydrocarbons prices globally.

In 2006 as compared to 2005, the increase in seamless pipe revenue was primarily attributable to increases in the prices for seamless pipes as well as increased sales volumes of the highest priced product, seamless OCTG. Average selling prices for seamless pipes increased by 22% to USD 1,151 per tonne in 2006 from USD 944 per tonne in 2005 principally reflecting the passing on of increased manufacturing costs attributable to higher raw material costs. The volume of seamless pipes sold increased by 2% in 2006 as compared to 2005, with sales volumes of OCTG increasing approximately by 16% as a result of the growing drilling activity of Russian oil companies driven in turn by increasing oil prices.

WELDED PIPES. TMK's welded pipes business is largely dependent on sales to Gazprom, TMK's principal customer, and particularly for sales of large-diameter welded pipes.

In 2006 as compared to 2005, the increase in welded pipe revenue was primarily attributable to an increase in the sales volumes of medium- and small-diameter pipes driven by higher construction activity. A reduction in the volumes of large-diameter pipes sold to Gazprom was partly compensated by the growth of sales volumes in Central Asia and the Caspian region driven by the Kazakhstan government's gas pipe lines modernisation programme (Central Asia – Centre pipeline). As a result of a change in product mix, caused by the increase in sales volumes of medium- and small-diameter pipes with lower margins and the decrease in sales volumes of higher-margin large-diameter pipes, total welded pipes sales volumes and the average selling price increased slightly. The average selling prices in US dollars for welded pipes increased by 2% to USD 889 per tonne in 2006 from USD 873 per tonne in 2005 due predominantly to US dollar depreciation against the Russian rouble in 2006, whereas average selling prices and total welded pipes revenue in roubles slightly fell. The relative reduction in welded pipes revenue in 2006 as compared to 2005 was primarily attributable to a decrease in revenue in the first six months of 2006 which resulted from lower volumes of large-diameter welded pipes sold to Gazprom. The increase in sales volumes of medium- and small-diameter pipes in the first six months of 2006 as compared to the same period of 2005 was not significant due to the unfavourable market environment (fall in prices for medium- and small-diameter welded pipes). The positive market trend for industrial welded pipes in the second half of 2006, particularly the growth in selling prices together with the relative increase in sales volumes of large-diameter welded pipes to Central Asia and the Caspian region, resulted in significantly higher welded pipes revenue in the second half of the year as compared to the first six months of 2006.

The following table provides an analysis of sales growth attributable to changes in prices and volumes of pipes:

MLN OF USD, %

2006 AS COMPARED TO 2005	Welded pipes		Seamless pipes		Total	
Changes in price	15.5	43%	390.0	91%	405.5	87%
Changes in volumes	20.6	57%	38.1	9%	58.7	13%
Total change	**36.1**	**100%**	**428.1**	**100%**	**464.2**	**100%**

OTHER OPERATIONS principally include sales of steel billets and various supplementary services to third parties, such as energy distribution. Net sales from other operations decreased by 7.5% in 2006 as compared to 2005 principally reflecting TMK's strategy of focusing on the production of seamless pipes and, hence, a decrease in the sales of steel billets.

Revenue by geographical segment

The following table shows revenue by geographical area based on the customer's location for the years ended December 31:

MLN OF USD, %	2006	2005	% CHANGE
Russia	2,308.5	2,041.5	13.1%
Europe	586.2	514.3	14.0%
Central Asia & Caspian region	177.6	77.2	130.1%
Middle East & Gulf region	183.0	127.4	43.6%
Africa	12.9	3.5	268.5%
Americas	102.4	126.7	-19.2%
Asia & Far East	13.8	47.6	-71.0%
Total revenue	**3,384.4**	**2,938.2**	**15.2%**

The following table sets forth consolidated revenue by geographical area based on the customer's location as a percentage of total revenue for the years ended December 31:

	2006	2005
Russia	68.2%	69.5%
Europe	17.3%	17.5%
Central Asia & Caspian region	5.3%	2.6%
Middle East & Gulf region	5.4%	4.4%
Africa	0.4%	0.1%
Americas	3.0%	4.3%
Asia & Far East	0.4%	1.6%
Total revenue	**100.0%**	**100.0%**

Revenue from sales of pipes in Russia increased in 2006 as compared to 2005 primarily due to an increase in average selling prices in the Russian markets evidencing strong growth in the Russian oil and gas industry. However, the rate of increase in revenue from sales of pipes in Russia slowed in 2006 as compared to prior years principally due to production reaching the capacity limits for seamless pipes.

The significant increase in sales to Central Asia and the Caspian region over 2005 is credited to growing sales to Uzbekistan and Kazakhstan by TMK's subsidiary TMK-Kazakhstan, driven by an increased demand from the oil and gas sector. The Kazakhstan government's gas pipe lines modernisation programme (Central Asia – Centre pipeline) particularly stimulated the strong demand for large diameter welded pipes. The increase in sales to the Middle East and the Gulf region over 2005 is primarily attributable to the beginning of sales to Saudi Aramco and increased sales prices. A slight decline in sales to the Americas was predominantly attributable to the reallocation of seamless pipe sales to the Middle East. TMK reduced sales to its North American distributor, Lone Star, in order to meet an increase in demand from TMK's customers in the Middle East and the Gulf region. TMK's Asian and Far East sales, suffering from heightened Chinese competition, decreased sharply in 2006. The launch of sales to Repsol in Libya significantly increased TMK's sales in Africa.

Gross profit

TMK's gross profit, which represents revenues less cost of sales, improved by 38.5% in 2006 as compared to 2005 due to various factors: increases in overall selling prices in excess of the increases in raw material costs, volume growth, improved product mix and higher operating efficiency.

The table below illustrates TMK's gross margin by business segment for the years ended December 31:

	2006	2005
Seamless pipes	39.6%	33.3%
Welded pipes	15.1%	14.1%
Other operations	6.1%	9.6%
Overall gross margin	**30.6%**	**25.4%**

SEAMLESS PIPES. Gross margins for seamless pipes increased in 2006 as compared to 2005 as a result of an increased proportion of higher-priced OCTG products, thus generating higher margins in product mix and improved efficiency at the pipe rolling mills due to the ongoing modernisation programmes.

WELDED PIPES. The increase in gross margins for welded pipes in 2006 as compared to 2005 was primarily attributable to a significant increase in margins for medium- and small-diameter pipes driven by the favourable market environment, particularly the growth of selling prices and the decrease in prices for purchased coil and plate.

OTHER OPERATIONS. Gross margins generated by other operations in 2006 as compared to 2005 decreased principally due to the relatively lower growth of prices for steel billets, the major component of sales of other operations, together with a significant increase in prices for metal scrap, the major raw material of other operations. Furthermore, the share of sales of higher-margin billets produced by TMK's Russian plants decreased, whereas the share of lower-margin TMK-

Resita billets sales increased in 2006 as compared to 2005.

Cost of sales

The table below sets out TMK's cost of sales for the years ended December 31:

MLN OF USD, % OF TOTAL COST OF PRODUCTION

	2006		2005	
Direct costs				
Raw materials	1,575.6	66.1%	1,481.5	68.0%
Energy	107.5	4.5%	82.7	3.8%
Add-on materials of production	82.3	3.5%	80.7	3.7%
Labour cost	93.2	3.9%	76.3	3.5%
Contracted services	11.7	0.5%	4.6	0.2%
Total direct costs	1,870.3	78.5%	1,725.8	79.2%
Production overheads				
Salaries and wages	178.3	7.5%	150.6	6.9%
Other compensation	8.6	0.4%	7.7	0.4%
Travel	1.3	0.1%	0.7	0.0%
Freight	5.8	0.2%	3.1	0.1%
Communications	0.7	0.0%	0.4	0.0%
Professional services	7.5	0.3%	6.6	0.3%
Rent/occupancy	0.3	0.0%	0.3	0.0%
Utilities	68.0	2.9%	59.8	2.8%
Depreciation	105.9	4.4%	98.9	4.5%
Insurance	0.3	0.0%	0.1	0.0%
Taxes	14.6	0.6%	12.7	0.6%
Repairs and maintenance	24.7	1.0%	18.4	0.8%
Supplies	96.4	4.0%	86.7	4.0%
Specialised tools	15.5	0.7%	12.5	0.6%
Other	0.6	0.0%	2.1	0.1%
Less: capitalised costs	(14.7)	(0.6)%	(6.6)	(0.3)%
Total production overheads	513.8	21.5%	454.0	20.8%
Total cost of production	**2,384.1**	**100.0%**	**2,179.8**	**100.0%**
Changes in inventory	(54.3)		(7.1)	
Cost of merchandise	20.2		16.7	
Inventory adjustment	0.5		2.4	
Total cost of sales	**2,350.5**		**2,191.8**	

Raw materials, labour costs and energy costs are the major components of the cost of production.

Raw materials and add-on materials of production

Raw materials costs and costs of add-on materials of production include principally purchases of steel plates and coil, steel billets, metal scrap, pig iron, ferroalloys and certain other materials used in the production processes. Raw materials costs and costs of add-on materials of production remained constant or increased slightly in 2006 as compared to 2005, reflecting the reducing trend in prices for certain materials in the first six months of 2006. In the second half of 2006, raw material prices increased as compared to the first half of 2006 although the general trend in average prices in 2006 as compared to 2005 remained favourable. The prices paid in Russia for several types of steel billets in 2006 as compared to 2005 decreased by approximately 10% and prices for purchases of steel coil decreased by 2–7% (depending on the type of material). On the other hand, scrap prices increased by 19–27% (depending on the region in Russia) in 2006 as compared to 2005.

Labour cost and salaries and wages

Labour costs and salaries and wages together constitute the second largest component of cost of sales. Labour costs include costs of personnel directly engaged in pipe and steel production. Salaries and wages expense included in production overheads represents labour costs attributable to personnel engaged in auxiliary workshop activities. Labour costs and salary and wages include salaries and wages of production personnel and the social and pension contributions attributable to these salaries. These contributions are made to the Russian Federation government funds at the statutory rates in force (ranging in 2006 and 2005 from 26 to 2% of gross payroll cost per employee applied on a regressive scale basis). Similar contributions to Romanian government funds are made at rates ranging in 2006 up to 36.9% and in 2005 to 38.9%). Labour costs also include net post-employment benefit expenses.

The increase in labour costs and salaries and wages in 2006 as compared to 2005 was driven principally by salary and wage increases in line with inflation as well as by increased production volumes, as the salaries of TMK's employees are linked to performance indicators.

Energy and utilities

Energy costs include principally purchases of electricity from RAO UES and purchases of natural gas from Gazprom.

Energy costs increased in 2006 as compared to 2005 principally due to increased production and higher energy prices. The weighted average prices for natural gas and electrical energy increased by approximately 10–12% in 2006 as compared to 2005.

Utilities mainly comprise costs for heat, electricity, gas and water that are not directly used in production processes. Costs increased in 2006 as compared to 2005 principally due to higher energy and utilities prices.

Repairs and maintenance

Repair and maintenance costs mainly comprise repair and maintenance services rendered by service organisations to TMK.

Repair and maintenance costs increased in 2006 as compared to 2005 due to the growth of repair and maintenance activities at TMK's plants in accordance with the planned repair programme. In 2006, repairs to the tube-rolling workshop and electric tube-welding workshop production equipment were undertaken at Volzhsky. The increase in maintenance costs in 2006 as compared to 2005 was primarily driven by the implementation of new technology (continuous casting machines put into operation) at TAGMET and STZ and related reconditioning works carried out at the plants.

Supplies

Supplies costs mainly comprise purchases for repair and maintenance of machinery and equipment, fire- proof materials, fuels and lubricants, and certain other materials used in production processes.

The increase in supplies costs in 2006 as compared to 2005 was predominantly attributable to the growth of repair and maintenance activities at the plants in the second half of 2006 and to general price increases.

Depreciation

Depreciation costs increased in 2006 as compared to 2005 principally as a result of the decision to replace open hearth furnaces and related equipment at the TAGMET and Seversky plants starting in the second half of 2005 as part of the strategic investment programme and management's reassessment of the remaining estimated useful lives of such furnaces and equipment. Management's decision to shorten the estimated useful lives of such furnaces and related equipment resulted in increased deprecation costs in 2006 as compared to 2005. Moreover, a continuous casting machine was put into operation at TAGMET in July 2006 in line with the production technology modernisation strategy. This also contributed to the higher depreciation change in 2006.

Changes in inventory and cost of merchandise

Changes in inventory represent decreases (increases) in the balances of semi-manufactured goods, finished goods, goods in transit and work-in-progress. The increase in changes in inventory in 2006 as compared to 2005 was caused by the increase in goods-in-transit relating to sales outside Russia, driven by increased selling activity in the Middle East region and the incorporation of TMK North America with its own inventories which are held to meet customers' needs in the Americas region. The balance of work-in-progress increased in 2006 as compared to 2005 predominantly as a result of an increase in semi-finished goods volumes (billets produced by Volzhsky and Resita) at TMK Artrom in order to satisfy production demand growth in connection with the new rolling mill planned to be put into operation in the first quarter of 2007. The general increase in the level of production and sales in 2006 as compared to 2005 also contributed to the growth of work-in-progress.

Cost of merchandise represents the cost of inventories purchased from suppliers and sold to customers without further processing. Cost of merchandise of USD 20.2 million in 2006 and USD 16.7 million in 2005 relates primarily to sales by TMK's Russian subsidiaries of the surpluses of raw materials initially purchased for own consumption. The increase in the cost of merchandise in 2006 as compared to 2005 was principally due to TMK Trade House sales of third-party produced pipes not specifically manufactured by TMK.

Selling expenses

The following table shows a breakdown of TMK's selling expenses for the years ended December 31:

MLN OF USD, % OF REVENUE	2006		2005	
Salaries and wages	32.6	1.0%	23.7	0.8%
Freight	104.4	3.1%	88.9	3.0%
Professional services	13.5	0.4%	10.4	0.4%
Other	29.4	0.9%	24.8	0.8%
TOTAL SELLING EXPENSES	**179.9**	**5.3%**	**147.8**	**5.0%**

Selling expenses mainly consist of freight costs and salaries and wages attributable to sales activities. The increase in all types of selling expenses in 2006 as compared to 2005 was driven by the increased selling activity of TMK Sinara NA and the consolidation of Eurosinara in 2006.

FREIGHT COSTS. Railway transportation is TMK's principal means of transporting raw materials and steel products to its facilities and pipe products to its Russian and CIS customers, as well as to ports for onward transportation overseas. Rail tariffs in Russia are currently regulated by the Russian government. The increase in freight costs in 2006 as compared to 2005 was attributable to increased sales volumes, particularly in the non-Russian markets, and by increased tariffs. Transportation costs with respect to raw materials are reflected in raw materials costs.

SALARIES AND WAGES. The increase in salaries and wages in 2006 as compared to 2005 was due to the increased salaries in the selling units and higher bonus payments linked to increases in sales volumes.

PROFESSIONAL SERVICES. Professional services relate principally to commissions relating to customs and freight forwarding services. The increase in professional services costs in 2006 as compared to 2005 was primarily attributable to increased sales volumes.

Advertising and promotion expenses

Advertising costs mainly consist of product displays and exhibits at industry trade fairs, TMK product brochures and web and print advertising. TMK incurred advertising and promotion expenses of USD 5.1 million and USD 3.1 million in 2006 and 2005, respectively. TMK's advertising costs have increased in 2006 as compared to 2005 as a consequence of increased marketing efforts.

General and administrative expenses

The following table shows a breakdown of TMK's general and administrative expenses for the years ended December 31:

MLN USD, % OF REVENUE	2006		2005	
Salaries and wages	88.6	2.6%	66.3	2.3%
Professional services	26.3	0.8%	22.3	0.8%
Travel	8.7	0.3%	4.5	0.1%
Other	34.1	1.0%	30.1	1.0%
Total general and administrative expenses	**157.7**	**4.7%**	**123.2**	**4.2%**

General and administrative expenses consist principally of wages and salaries of administrative personnel and professional services costs including costs of legal and accounting advisers, audit services, management consultants and investment banking. The increase in salaries and wages in 2006 as compared to 2005 is attributable to salary increases in line with inflation, an increase in bonuses as a result of the successful IPO of TMK and the share purchase option offered to the personnel in 2006. At the same time, the administrative staff headcount increased due to needs to reinforce controls over the newly acquired foreign operations of Sinara Handel GmbH, Eurosinara and the Romanian entities (SC Artrom SA and SC C.S.R. SA) in 2006. This factor also influenced the significant growth of travel expenses in 2006 as compared to 2005. The increase in professional services in 2006 as compared to 2005 is attributable to advisers, including investment banking, accounting and legal advisers, retained in connection with the IPO.

Research and development expenses

Research and development expenses consist primarily of the salaries and wages of TMK's research personnel. Research and development costs were USD 6.7 million and USD 5.5 million in 2006 and 2005, respectively.

The increase in research and development expenses in 2006 as compared to 2005 was primarily attributable to increased salaries and wages as a result of annual indexation and to additional professional services related to studies in respect of new production technologies at the plants.

Other operating income and expenses

The following table shows a breakdown of other operating expenses for the years ended December 31:

mln USD, % of revenue

	2006		2005	
Other operating expenses				
Social and social infrastructure maintenance	10.6	0.3%	11.1	0.4%
Loss on disposal of property, plant and equipment	5.1	0.2%	4.5	0.2%
Charitable donations	11.7	0.3%	7.5	0.3%
Other	0.0	0.0%	3.0	0.0%
Total other operating expenses	**27.4**	**0.8%**	**26.1**	**0.9%**
Other operating income				
Government grants	3.7	0.1%	–	–
Profit share of associate	1.2	0.0%	–	–
Gain on sale of current assets	0.2	0.0%	0.2	0.0%
Other	3.9	0.1%	0.1	0.0%
Total other operating income	**9.0**	**0.2%**	**0.3**	**0.0%**

Social and social infrastructure maintenance expenses represent costs related to the maintenance of sport, medicine, culture and other social infrastructure facilities used by TMK employees and expenses related to social events. Social and social infrastructure maintenance expenses decreased in 2006 as compared to 2005 due to the implementation of new policies whereby employees are required to bear a larger portion of such costs themselves.

Charitable donations, which comprise donations and membership fees to non-commercial organisations, increased in 2006 as compared to 2005 as a result of increased sponsorship of sports activities and local sports teams.

The losses in disposal of property, plant and equipment for both 2006 and 2005 were mainly due to the replacement of part of the production equipment at TAGMET.

In 2006, income from government grants was USD 3.7 million which represents partial reimbursement by the government of interest expense incurred in relation to loans received by TMK's Russian plants from banks of the Russian Federation in 2005 – 2006. This government programme to partially reimburse interest expense was established for Russian exporters of manufacturing goods.

TMK's share in the profit of an associate in the amount of USD 1.2 million represents a 20% interest in profit of the associate (OOO "Northern-European Pipe Project") in 2006. In 2005 the associate did not conduct any selling or production activities.

Foreign exchange gain/(loss)

The functional currency of TMK and its subsidiaries located in the Russian Federation and Switzerland is the Russian rouble. The functional currency of the Romanian subsidiaries is the Romanian lei and for Sinara Handel GmbH and Eurosinara it is the euro. Monetary assets and liabilities denominated in foreign currencies are translated into the respective functional currencies of TMK and its subsidiaries at the exchange rate as of the relevant balance sheet date. Changes in the values of such assets and liabilities are recorded as a result of exchange rate changes in the results of operations under the line item foreign exchange gain/(loss).

Foreign exchange gains were USD 13.0 million in 2006 as compared to a loss of USD 14.6 million in 2005. Foreign exchange rate differences relate primarily to the revaluation into roubles of the US dollar denominated loans and Eurobonds as at the end of the reporting periods. During the years 2006 and 2005 TMK had monetary liabilities denominated in US dollars as a result of US dollar borrowings and Eurobonds issued in 2006 thus a decrease in the nominal value of the dollar relative to the Russian rouble has historically resulted in foreign exchange gains and an increase in the nominal value of the US dollar relative to the Russian rouble has historically resulted in foreign exchange losses. In 2006, foreign exchange gains were primarily due to appreciation of the Russian rouble against the US dollar as at December 31, 2006 as compared to December 31, 2005. The gain was partly offset by losses incurred on the conversion of US dollar loan proceeds into roubles.

Finance costs

Finance costs were USD 76.5 million in 2006 as compared to USD 78.2 million in 2005. Finance costs principally reflect interest expense. Interest expense decreased in 2006 as compared to 2005, primarily due to early repayment of several long-term loans received before January 1, 2006 and the replacement of more expensive short-term loans by Eurobonds and long-term loans with lower interest rates. In addition, the average interest rate of rouble-denominated coupon debt securities decreased in 2006 as a result of the replacement of higher-interest (10–14%) bonds with lower-interest (7.95%) bonds. On the other hand, arrangement fees paid in connection with borrowings increased in 2006 as compared to 2005 due principally to costs incurred in connection with the Eurobonds issue in 2006 and due to higher arrangement fees recognised in 2006 as a result of early repayment of long-term loans received in 2005 and 2006 (Moscow Narodny Bank, Dresdner Bank, Natexis).

Income tax expense

Income tax expense was USD 157.9 million in 2006 as compared to USD 95.9 million in 2005. Income tax expense increased in 2006 as a result of the increase in profit before tax. The effective tax rate, defined as income tax expense as a percentage of profit before tax, decreased from 27.4% in 2005 to 25.5% in 2006 as a result of a relative reduction in non-deductible expenses, such as certain consulting fees and social maintenance expenses, as compared to profit before tax: non-deductible expenses increased slightly in 2006 over 2005 while profit before tax grew significantly in the light of overall revenue growth. TMK also recognised certain tax benefits as a result of changes in tax legislation.

Net profit

For the reasons set forth above, net profit increased by 81% to USD 460.6 million in 2006 as compared to 2005.

Liquidity and capital resources

Capital requirements

Historically, TMK has mainly relied on cash provided by operations and short-term debt to finance working capital and other capital requirement and management expects that these will continue to be important sources of cash in the future. At the same time, TMK intends increasingly to replace short-term debt with long-term debt in order to better match capital resources to planned expenditure. The outstanding balance of short-term borrowings as of December 31, 2006 decreased to USD 364.5 million from USD 425.5 million as of December 31, 2005. TMK does not make use of off-balance sheet financing arrangements.

Cash flows

The table below sets forth the summarised cash flows for the years ended December 31:

MLN USD	2006	2005
Profit before income tax	**618.5**	**350.0**
Non-cash and other adjustments	167.1	206.8
Changes in operating assets and liabilities	(185.7)	(35.2)
Income taxes paid	(170.2)	(107.3)
Net cash from operating activities	**429.7**	**414.3**
Net cash used in investing activities	**(519.6)**	**(138.1)**
Net cash from/(used in) financing activities	**182.6**	**(241.9)**
Effect of exchange rate changes on cash and cash equivalents	**3.2**	**0.1**
Net increase in cash and cash equivalents	**95.9**	**34.4**

Operating activities. Cash provided by operating activities primarily consists of net income adjusted for certain non-cash items including depreciation, amortisation and other items and the effect of changes in working capital.

Net cash from operating activities was USD 429.7 million and USD 414.3 million in the years ended December 31, 2006 and 2005, respectively. The lower increase in net cash from operating activities as compared to the increase in profit before tax in 2006 was predominantly due to an increase in accounts receivable, prepayments and inventory balances driven by increased production and selling activity as well as a decrease in accrued liabilities.

The significant increase in the accounts receivable balance as at December 31, 2006 as compared to December 31, 2005 was mainly attributable to the growth of trade receivables due from Gazprom, one of TMK's key customers. The major part of the Gazprom debt, outstanding as at December 31, 2006, was paid in the beginning of 2007.

Inventory growth was caused by the increase in goods-in-transit related to sales outside Russia, driven by increased selling activity in the Middle East region and the incorporation of TMK North America with its requirement to warehouse stock. In addition, the work-in-progress balance increased in 2006 as compared to 2005 predominantly as a result of increased semi-finished goods volumes at the Romanian plants satisfying production demand growth in connection with the start-up of the new rolling mill planned for the first quarter of 2007.

Prepayments increased in 2006 primarily due to a rise in prepayments for inventories driven by the growing production activity. In addition, the input VAT balance, subject to refund by the Federal budget in respect of export sales outside Russia, increased as at December 31, 2006 as compared to December 31, 2005 as a result of higher sales outside Russia by TMK's Russian subsidiaries. The purchase of a new office building in 2006 also contributed to the growth in the input VAT balance.

The reduction of accrued liabilities was primarily due to the payment of deferred VAT accrued as of December 31, 2005. In 2006, Russian tax legislation changed the calculation of VAT payment from a cash to an accruals basis.

The increases in accounts payable and advances from customers partially compensated the adverse effect of the aforesaid factors on the operating cash flow.

Investing activities. Net cash used in investing activities was USD 519.6 million and USD 138.1 million in the years ended December 31, 2006 and 2005, respectively. Substantially all the cash used in investing activities related to purchases of property, plant and equipment, purchases of shares in subsidiaries, purchase of an interest in Eurosinara and bank deposits. The significant increase in net cash used in investing activities in 2006 as compared to 2005 was predominantly attributable to funds spent on production equipment in line with the strategic investment programme, amounting to USD 335.9 million in 2006 as compared to USD 139.1 million in 2005.

In addition, at the end of 2006, surplus monetary funds were partly placed on bank deposit and partly invested short-term in the total amount of USD 170 million at interest rates of 6.25–8.75%.

TMK also paid USD 21.7 million for an increase in ownership interest in its subsidiaries in 2006 as compared to USD 6.8 million in 2005.

In October 2006, through TMK and TMK Trade House, loans were made to the principal shareholder, TMK Steel, in the total amount of USD 780 million. The loans were unsecured and bore interest at 8.51% per annum. The debt was repaid by TMK Steel in November 2006.

Financing activities. Net cash from financing activities during the year ended 31 December, 2006 of USD 182.6 million was due principally to net proceeds from borrowings of USD 340.7 million, offset mainly by interest paid in the amount of USD 71.8 million, prepayment to an entity under common control for the transfer of ownership interest in OMZ in the amount of USD 45.5 million and final payment to an entity under common control for the transfer of ownership interest in Sinara Handel GmbH in the amount of USD 20 million.

Dividend. In June 2006, TMK paid dividends in respect of 2005 in a total amount of USD 17.1 million. In May 2005, TMK paid interim dividends in a total amount of USD 2.6 million.

Indebtedness

The following table summarises outstanding interest-bearing debt, including loans and other borrowings, by currency and interest rate as of December 31, 2006:

MLN USD

	DOLLAR-DENOMINATED	ROUBLE-DENOMINATED	EURO-DENOMINATED	TOTAL
Total debt, of which	**471.9**	**434.9**	**118.8**	**1,025.6**
Fixed-rate debt	302.8	415.9	0.8	719.5
Variable-rate debt	169.1	19.0	118.0	306.1

As of December 31, 2006, USD 268.1 million of total debt was secured by collateral of property, plant and equipment, inventories, deposits, accounts receivable (*see Notes 13, 15, 18 and 19 to the Financial Statements*).

The following table summarises the short-term and long-term interest-bearing debt, including loans and other borrowings, outstanding as of December 31, 2006:

MLN USD

	UP TO 1 YEAR	1 TO 2 YEARS	2 TO 3 YEARS	3 TO 4 YEARS	OVER 4 YEARS	UNAMOR-- TISED DEBT ISSUE COSTS	TOTAL
Interest-bearing loans & borrowings	268.7	112.4	38.4	11.7	16.8	(4.2)	443.8
Bearer coupon debt securities	97.3	189.9	300.0	–	–	(5.4)	581.8
Total Debt	**366.0**	**302.3**	**338.4**	**11.7**	**16.8**	**(9.6)**	**1,025.6**

As of December 31, 2006, the most significant borrowings included the following:

In connection with the funding of the TMK Steel Loan, TMK incurred the following debt:

Loan participation notes. On September 29, 2006, TMK issued 3,000 8.5% loan participation notes with a nominal value of USD 100,000 each, due in September 2009. The notes were issued by TMK Capital S.A., a Luxemburg special purpose vehicle, for the sole purpose of funding a loan to TMK. The notes have been admitted to trading on the London Stock Exchange. The terms of the notes provide for certain restrictions on TMK's ability to incur liens, to engage in assets sales, to engage in transactions with affiliates and to engage in mergers and similar transactions.

BANK LOANS. On September 25, 2006, TMK entered into a syndicated facility agreement with Bank Natexis, as arranger, in an aggregate principal amount of up to USD 155.0 million. The facility has a term of 30 months from the date of the first drawdown, which occurred on September 26, 2006. The maturity date of the facility may be extended in certain circumstances at the election of TMK. As of December 31, 2006, TMK has drawn the equivalent of USD 155.0 million under this facility.

On September 29, 2006, TMK entered into an agreement with Dresdner Bank that provided for a bridge loan facility in the principal amount of USD 160.0 million, with a term of 364 days from the date of signing. The facility was repaid on November 8, 2006.

On October 2, 2006, TMK entered into a medium term facility with Moscow Narodny Bank and Commerzbank in the principal amount of USD 140.0 million. The term of the facility was 24 months. The facility was fully drawn and was repaid on November 10, 2006.

BEARER COUPON DEBT SECURITIES. On February 21, 2006, TMK issued 5,000,000 bonds with a nominal value of 1,000 roubles (USD 35.53 at the exchange rate of the date of issuance) each. The maturity date is February 15, 2011. The interest rate for the first four coupon periods is 7.95% per annum. Early redemption of the bonds is possible in February 2008.

Capital expenditures

TMK has a strategic capital expenditure programme, which began in 2004 and extends through 2010, aimed at increasing seamless pipe production, increasing the efficiency of production facilities, improving the quality and range of TMK's products and increasing the production of high value-added products.

The following table provides the breakdown of capital expenditures by types of activities for the years ended December 31:

MLN USD, %	2006	2005	%CHANGE
Seamless pipes	251.2	119.6	110%
Welded pipes	5.9	1.7	247%
Other operations	1.9	4.2	(55)%
Unallocated	112.9	13.8	718%
Total capital expenditures	371.9	139.3	167%

The principal portion of the capital expenditures in 2006 and 2005 related to the installation of new continuous casting machines at TAGMET and Seversky, a new reducing mill at Sinarsky, a new rolling mill at Artrom, upgrades of the electric furnace and the continuous casting machine at Volzhsky and improvements on the heat treatment and finishing capacity of the pipe plants. The significant increase in capital expenditures summarised under line item "Unallocated" was primarily attributable to the purchase of a new office building in Moscow.

TMK expects to continue to finance most of its capital expenditure needs through operating cash flows, existing cash balances, as well as debt financing and other sources as appropriate.

Contractual commitments and guarantees. As of December 31, 2006, TMK had contractual commitments for the acquisition of property, plant and equipment from third parties for 1.8 billion roubles (USD 70.1 million), 193 million euros (USD 254 million), USD 10.1 million and 8.8 million Romanian lei (USD 3.4 million) for the total amount USD 337.8 million (all amounts of contractual commitments are expressed net of VAT). TMK has paid advances of USD 32.3 million with respect to such commitments.

Under the contractual commitments disclosed above, TMK has opened unsecured letters of credit in the amount of USD 47.3 million.

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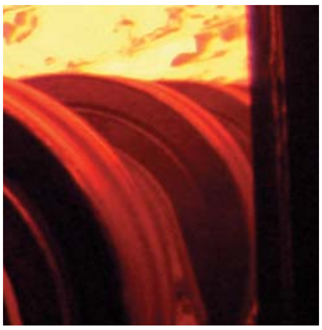
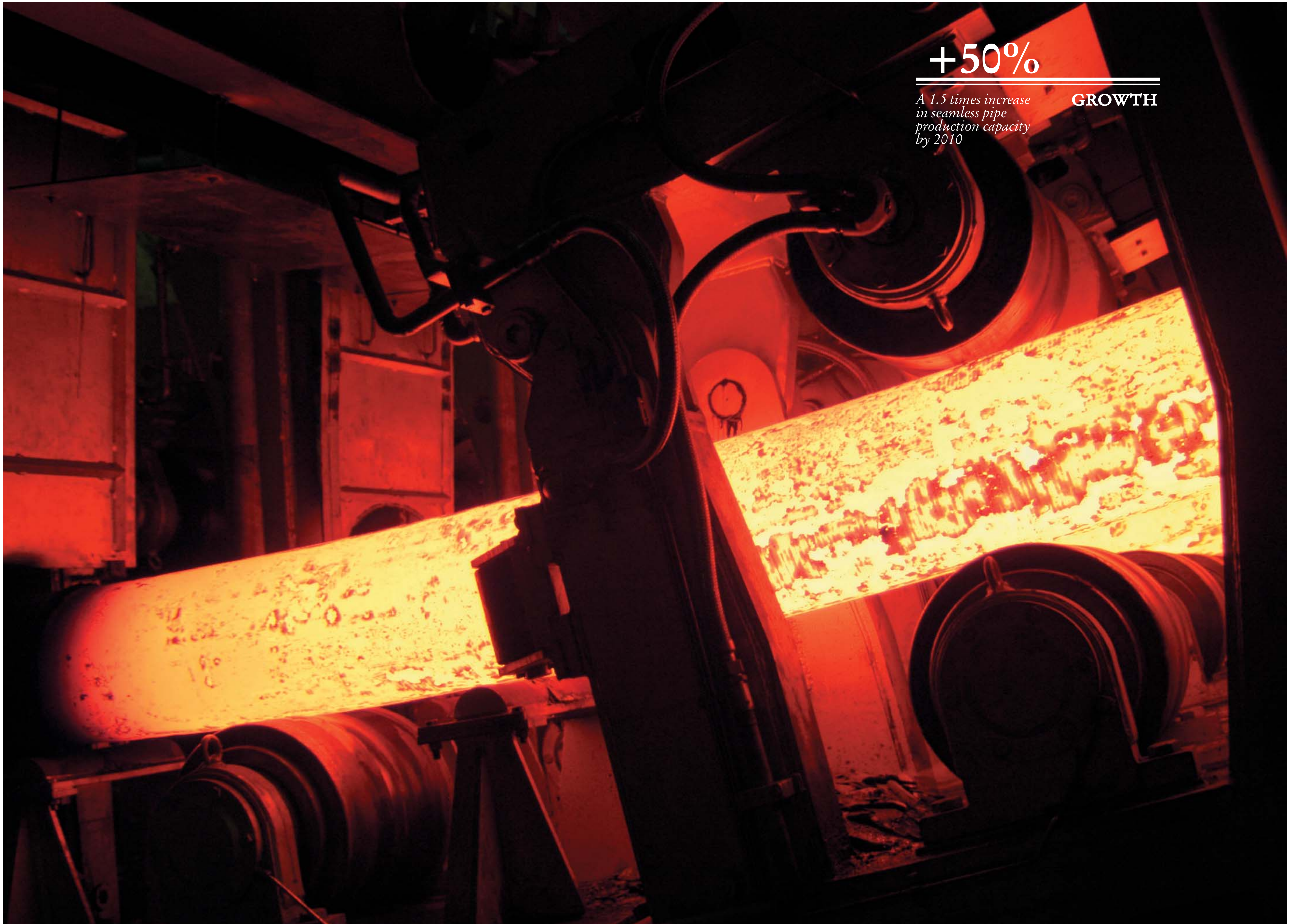
UNIQUE



TMK ANNUAL REPORT 2006



7(1) Key Development Trends

STRATEGY

((7)) BECOME | A GLOBAL LEADER IN THE OIL AND GAS PIPE SECTOR

((6)) COMPLEMENT | QUALITY PRODUCT LINES WITH VALUE ADDED SERVICES

((5)) EXPAND | GLOBALLY THROUGH ACQUISITIONS AND ALLIANCES

((4)) DEVELOP | GLOBAL MARKETS THROUGH EXPORTS AND COMMERCIAL PRESENCE

((3)) ENHANCE | DOMINANT SUPPLIER POSITIONS IN RUSSIAN OIL AND GAS SECTOR

((2)) ESTABLISH | A SOLID MANUFACTURING BASE IN RUSSIA AND INTEGRATION OF FOREIGN ASSETS

((1)) CONSOLIDATE | PIPE INDUSTRY ASSETS IN LARGEST RUSSIAN PIPE COMPANY

RUSSIA IS A NATURAL HOME MARKET TO START THE JOURNEY

In 2005, TMK adopted a growth strategy and formulated a strategic vision for its development for 2005–2015.

Targeting the enhancement of its position as the leading pipe producer in Russia and the consolidation of its position as a leading global producer of seamless pipes TMK has defined the following key strategic objectives:

- Significant enhancement of production capacities of technologically sophisticated OCTG pipes (TMK's highest-margin business segment).
- Increase of TMK's business profitability through its global market presence and extra customer value.

Strategic vision of TMK's development for the next 5 years
Seamless oil and gas pipes (OCTG and line pipes) are and will continue to be TMK's "flagship business".

((UPSTREAM))	(1) RAW MATERIALS	(2) COIL&PLATE
((MIDSTREAM))	(3) TUBE ROUND/TUBE BILLETS (3) INDUSTRIAL SEAMLESS (3) LINE PIPE (3) OCTG	(4) SMALL DIAMETER WELDED FOR INFRASTRUCTURE (3) LARGE DIAMETER TRANSMISSION
((DOWNSTREAM))	(1) PREMIUM THREADS (1) SERVICES	
	RUSSIA/CIS AND GLOBAL MARKETS	RUSSIA/CIS MARKETS

(1) *Develop*, (2) *Alliance*, (3) *Grow*, (4) *Protect*.

Based on TMK's market position, key competitive advantages and to comply with the strategic vision of TMK's development, guidelines have been formulated. TMK's development involves building on its natural strengths as a supplier to the energy sector in the Russian market.

Main strategic initiatives:

- Increase of large-diameter welded and OCTG seamless pipe production capacities, including steel-making operations by fundamental re-equipment and modernisation of existing plants through large-scale investment.
- Programme to expand TMK's global commercial presence and enhance long-term relations with key Russian and foreign customers.
- Development of innovative solutions and downstream services to meet the growing requirements of the energy and industrial sectors.
- Selective acquisitions, alliances and joint ventures to consolidate TMK's competitive position in the global pipe market.
- Solid pursuance of advanced principles of corporate governance.

TMK intends to accomplish its strategic vision for development by:

- Focusing principally on higher-growth and higher-margin products (seamless pipes, especially OCTG).
- Enhancing TMK's product mix in seamless and welded segments to improve its margin profile and increase revenues per tonne of pipe sold.
- Expanding and modernising TMK's seamless pipe business through significant capital investment.
- Increasing large-diameter welded pipe production for the oil and gas industry.

» Consolidating TMK's existing market share in industrial welded segment with limited capital investment.
» Entering into a number of joint ventures with TMK's partners to increase production of technologically sophisticated premium products, including premium connections for the oil and gas industry, thus enhancing the offering of high-margin products.
» Strengthening partnerships with customers on joint development of innovative higher value-added products and services.
» Expanding TMK's global presence organically as well as through acquisitions and strategic alliances.

Seamless Segment

Strategic vision and key objectives in the seamless segment:

» To maintain the position as the leading supplier of seamless OCTG and line pipes to the oil and gas industry in Russia, the CIS and the Caspian region.
» To become a leading supplier of OCTG and line pipes to the global oil and gas industry, targeting the Middle Eastern and North African markets, by enhancing TMK's product mix and combining high-quality low-cost production in Russia with global development of a strategically located distribution network and increased productivity of threading and finishing facilities.
» To offer a complete range of seamless pipes, enhanced by innovative solutions and supply-chain management for oil and gas customers.
» To become a leading low-cost supplier of quality industrial seamless pipe across Russia, the CIS and Europe.

TMK intends to accomplish these objectives by:

» Enhancing the seamless product mix by increasing TMK's share of premium production for the oil and gas industry compatible with a global leader's product range.
» Consolidating TMK's position as a leading supplier of OCTG and line pipe in Russia and other CIS countries and consolidating its position in the global market.
» Strengthening alliances with suppliers of raw materials.
» Focusing on select high-margin segments within the industrial seamless pipe sector.

Enhance TMK's seamless product mix of pipes for the oil and gas industry to a level compatible with the product range of global leaders

TMK plans to enhance the product mix of new high-performance pipes, including Premium threads, designated for use in high pressure drilling environments, such as deepwater offshore wells and arctic drilling, including alloyed steel OCTG and line pipes with stronger tolerances, high anticorrosion characteristics and greater resistance to temperature.

TMK intends to develop its threading capabilities and downstream services, such as threading repair, production, maintenance and the sale of pipe accessories, assistance in drilling string assembly and drill-string running.

TMK believes that, by enhancing product mix and enlarging the share of the value-added features of its oil and gas product portfolio, it will be able to offer a more attractive product mix to global oil and gas companies and to increase profit margins.

Consolidation of TMK's position as a leading supplier of OCTG and line pipe in Russia, in other CIS countries and on the global market

In Russia and other CIS markets, TMK intends to consolidate its leading position in the OCTG and line pipes segments by expanding relations with existing customers and developing downstream services and supplies of technological components.

TMK has signed strategic partnership agreements with Gazprom, TNK-BP and Rosneft. TMK has also signed an agreement on strategic cooperation through to 2015 with SMS Group (Germany), one of the world's leading manufacturers of metallurgical and pipe-rolling equipment. The strategic cooperation stipulates coordination of long-term joint activities to develop and implement SMS Group's best technologies and equipment for steel-making and seamless pipe production at TMK mills.

TMK aims to become actively involved with sponsors at all stages of pipeline projects, from the initial planning stage to development and implementation stages to enhance opportunities to supply pipes to these projects.

TMK plans to strengthen its position in important oil and gas producing regions worldwide by developing its global network of commercial and distribution centres that will offer supply management, threading and downstream services. TMK will also seek to obtain the necessary qualifications from leading global oil and gas companies to increase global market recognition.

By means of these initiatives TMK will develop an international brand. In addition, TMK will consider the acquisition of additional OCTG and seamless line pipe manufacturing facilities in strategic locations outside Russia and seek to establish commercial alliances and partnerships as an efficient way of consolidating its global presence.

Consolidation of alliances with raw materials suppliers

TMK's policy is to make long-term alliances with a small number of large suppliers of raw materials to improve management of the availability and quality of scrap and other raw materials needs and to reduce raw materials costs. In February 2007, TMK and OAO Magnitogorsk Iron & Steel Works, the largest iron and steel works in Russia, signed a Strategic Partnership Memorandum.

TMK is considering the acquisition of a major steel scrap processor in Russia to ensure the availability of high quality steel scrap.

TMK plans to establish long-term supply arrangements with coil and plate suppliers in connection with the production of 1,420 mm diameter line pipe.

To improve control over the quality of production, TMK will continue performing material and production inspections at the plants of its raw materials and coil/plate suppliers. TMK also plans to implement a supplier qualification (approval) procedure.

Welded Segment

Strategic vision and key objectives in the welded segment:

- To expand the large-diameter welded pipe business.
- To organise the production of longitudinally welded large-diameter pipes which Gazprom and Transneft prefer for high-pressure oil and gas transportation.

- To work in terms of long-term supply and co-operation arrangements with key customers, such as Gazprom and Transneft.
- To become actively involved in all stages of pipeline projects, from the initial planning stage to the development and implementation stages to enhance opportunities to supply such projects with pipes.
- To enhance management of rolled products availability and quality for large-diameter welded pipe production.
- To expand product mix and increase output of the industrial welded business in a controlled manner based on the existing capacities without significant investment.

TMK intends to accomplish these objectives by:

- Focusing on sales of large-diameter welded pipes to oil and gas companies and pipeline projects in Russia, the CIS and the Caspian region.
- Installation of an additional longitudinally large diameter production line at Volzhsky plant to increase the output of large-diameter welded pipes for high-pressure oil and gas transportation.
- Participating in ongoing and proposed large-scale oil and gas transportation projects.
- Establishing a joint venture with Corinth Pipeworks, for the production of 168 – 530 mm welded pipes, principally for use in the oil and gas industry.
- Considering a potential partnership with feedstock suppliers.

7(2) Key Development Trends

STRATEGIC INVESTMENT PROGRAMME

A key component of TMK's strategy is to implement the main operational development goals by increasing the capacity and efficiency of seamless pipe and large-diameter welded pipe production through the strategic investment programme.

The key goals are the following:

- To increase seamless pipe production capacity (especially OCTG and line pipes).
- To increase the efficiency of production processes through modernisation and expansion of steel-making operations and pipe-rolling facilities.
- To increase production of large-diameter welded pipes at the Volzhsky plant.
- To improve the quality and product mix of TMK's products.
- To increase the production of high value-added products.
- To reduce the environmental impact of TMK's operations.

The strategic investment programme commenced in 2004 and foresees expenditure of approximately USD 1.4 billion between 2004 and 2010. Expenditure under the programme totaled USD 323.2 million between 2004 and 2006.

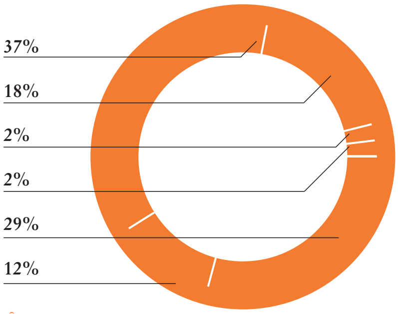
In TMK's steel-making operations, the installation of a continuous casting machine was completed at Volzhsky in the beginning of 2007. At TAGMET, Seversky and TMK-Resita ingot casting equipment was replaced and continuous casting machines producing billets for seamless pipes were installed. In 2006, to improve its steel-making operations, TMK upgraded electric arc furnaces and installed a gas cleaning system at TMK-Resita.

In 2006, installation of a piercing mill at Seversky and of two upsetting mills at TAGMET and Sinarsky was also completed.

Several other projects were carried out to improve quality, product mix, testing and finishing capacities.

TMK has financed the first phase of its strategic capital expenditure programme primarily from cash flows from operating activities, supplemented by borrowing and other sources as appropriate.

TMK STRATEGIC INVESTMENT PROGRAMME BY SEGMENTS



%

Increase production capacity for seamless pipes	37%
Increase production capacity fro heat-threatment and finishing of pipes	18%
Upgrade testing and control facilities	2%
Environmental protection systems	2%
Modernise our steel-making facilities	29%
Increase production capacity for large diameter welded pipes	12%

stable
growth

TRANSPARENCY

6+

RAITING

Corporate governance rating is 6+ on the international scale and 6.7 on the Russian national scale

8(1) Corporate Governance

CORPORATE GOVERNANCE PRINCIPLES

In its operations OAO "TMK" adheres to the requirements of Russian law, the requirements of the London and Russian Stock Exchanges and the recommendations of best Russian and international corporate governance practices. It also develops and implements these principles both at the level of OAO "TMK" and of the subsidiaries. TMK sees adherence to corporate governance principles as the key to success and to an increase in shareholder value. The implementation of corporate governance principles can be seen in the practical measures taken:

Exercise of shareholders' rights

Shareholders are given a real opportunity to exercise their rights to participate in TMK's management and the distribution of profits and to receive complete, reliable information on TMK on a regular and timely basis. These rights are guaranteed by the Charter of OAO "TMK".

Equality of shareholders

Shareholders owning an equal number of one type of share are guaranteed equal treatment. All shareholders have the right to effective protection in case of violation of their rights. These principles are enshrined in the Charter of OAO "TMK" which stipulates the procedure for holding the general meeting, the procedure for electing the members of the Board of Directors and senior management and the right to receive information on OAO "TMK"'s activities and copies of its articles of association and other documents.

Activity and accountability of the Board of Directors

The Board of Directors of OAO "TMK" undertakes the strategic management of TMK's operations and monitors the activity of the executive bodies. To improve the supervisory function, the Board of Directors includes independent directors, Committees of the Board of Directors have been created and the Board of Directors has the right to appoint and terminate the authorities of the executive bodies.

Activity and accountability of the executive bodies

The executive bodies of OAO "TMK" are accountable to the Board of Directors and the shareholders. The Chief Executive Officer and the Management Board are responsible for the management of OAO "TMK"'s day-to-day activities and their remuneration reflects their actual contribution to TMK's overall performance.

Disclosure of information about the Company

TMK has a policy of information openness and operational transparency for shareholders, employees and third parties and uses all available sources of information (Internet, print media, press conferences, television and radio) to ensure that all interested parties have free access to the information disclosed on TMK. OAO "TMK"'s Regulations on Use of Insider Information aim to prevent the illegal use of such information.

Relations with interested parties

Relations between TMK employees, their colleagues and third parties are built on principles of integrity, honesty, professionalism, mutual trust and respect; the inviolability of obligations; full disclosure of necessary information; and the precedence of negotiations over court proceedings.

Monitoring of financial and business activity

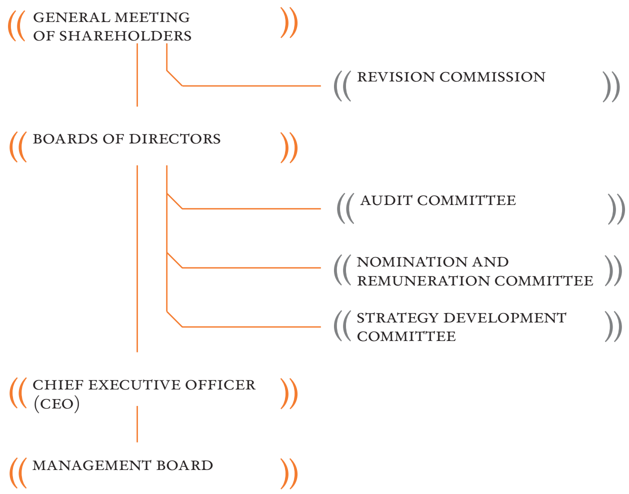
TMK takes measures to ensure the monitoring of financial and business activity in order to protect the rights and lawful interests of shareholders. The Revision Commission and the Internal Audit Service perform regular checks of TMK's financial and business activity. The Audit Committee under the Board of Directors coordinates relations between the external and internal auditors, with the aim of improving the effectiveness of control measures.

Ethical standards

TMK employees, irrespective of their position, and also members of the Board of Directors, members of the Management Board and the Revision Commission assume the obligation to work honestly and to adhere to ethical rules (standards) as specified in OAO "TMK"'s Ethics Code.

The effectiveness of OAO "TMK"'s implementation of corporate governance principles is supported by the conclusions of independent experts. In December 2006, Standard & Poor's Corporate Governance Rating Service raised the corporate governance rating (CGR) of OAO "TMK" from 5+ to 6+. At the same time, Standard & Poor's improved the CGR from CGR 5.9 to CGR 6.7 on the Russian scale.

The following corporate governance system has been created and implemented at OAO "TMK" to ensure that corporate governance principles are observed:



8(2) Corporate Governance

BOARD OF DIRECTORS

The Board of Directors of OAO "TMK" operates on the basis of the Charter, the Regulations of the Board of Directors and other internal statutes of OAO "TMK" and is responsible for the overall management of OAO "TMK"'s operations, except for issues that Russian law and the Charter of OAO "TMK" assign to the competence of the general meeting of shareholders.

The goals of the Board of Directors are to ensure the underlying conditions for TMK to achieve maximum profits and to increase the value of TMK's assets, to defend the rights and lawful interests of shareholders and to ensure that public information about OAO "TMK" is complete, reliable and objective. Through its oversight of TMK's executive management, the Board of Directors also plays a key role in ensuring that a balance is maintained between the rights and lawful interests of shareholders and those of other stakeholders.

Main duties

The Board of Directors of OAO "TMK" performs the following main functions:

- setting priorities for OAO "TMK"'s operations and for improvements to corporate governance;
- calling annual and extraordinary meetings of shareholders;
- making decisions on the placement of shares and other issuable securities in those cases stipulated by the OAO "TMK" Charter;
- approving annual budgets and strategic development plans, as well as overseeing the use of TMK's assets through the prior approval of major transactions and other transactions stipulated by the TMK Charter;
- appointing and removing the Chief Executive Officer of OAO "TMK" and members of the Management Board.

The Board of Directors monitors the performance of all of TMK's business units and is responsible for creating and maintaining an effective system of internal controls in OAO "TMK" and its business units.

Issues within the competence of the Board of Directors may not be delegated to the Chief Executive Officer, the Management Board or the general meeting of shareholders.

Members

The Board has ten members, four of whom are independent directors according to criteria defined in the Regulations of the Board of Directors.

No changes took place to the membership of the Board of Directors in 2006.

As of 31 December 2006, the members of the Board of Directors of OAO "TMK" were:

D. Pumpyanskiy	Chairman of the Board of Directors	
P. Galitzine	Member of the Board of Directors Member of the Strategy Development Committee	Independent director
A. Kaplunov	Member of the Board of Directors Member of the Nomination and Remuneration Committee	
A.N.W. Cobb	Member of the Board of Directors Member of the Audit Committee	
J. Marous	Member of the Board of Directors Chairman of the Strategy Development Committee Member of the Nomination and Remuneration Committee	Independent director
S. Papin	Member of the Board of Directors	
G. Townsend	Member of the Board of Directors Chairman of the Audit Committee	Independent director
I. Khmelevsky	Member of the Board of Directors	
A. Shiryaev	Member of the Board of Directors Member of the Strategy Development Committee	
M. Eskindarov	Member of the Board of Directors Chairman of the Nomination and Remuneration Committee Member of the Audit Committee	Independent director

Dmitriy Pumpyanskiy

Born: 1964.
Graduated from Urals State Technical University, Candidate of Science.
Positions in other organisations: President of ZAO "Sinara Group".
Previous positions held: Chief Executive Officer of OAO "TMK", First Deputy Chief Executive Officer, Chairman of the Board of Directors of OAO "Sinarsky Pipe Plant".
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares owned in OAO "TMK": 0%.

Piotr Galitzine

Born: 1955.
Graduated from Massachusetts Institute of Technology, received an MBA from New York University.
Positions in other organisations: Chief Executive Officer of ZAO "BASF" in Russia and CIS, Head of the representative office of BASF AG in Russia.
Previous positions held: Managing Director of ZAO "BASF", Director of "Jysk Staalindustrie ApS", representative office in Denmark.
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares owned in OAO "TMK": 0%.

Andrei Kaplunov

Born: 1960.
Graduated from Moscow Finance Institute, Candidate of Economy.
Positions in other organisations: Vice-President of ZAO "Sinara Group".
Previous positions held: Deputy Chief Executive Officer for Organisational Development of OAO "TMK".
Share in the charter capital of OAO "TMK": 0.0005%.
Share of ordinary shares owned in OAO "TMK": 0.0005%.

Adrian Cobb

Born: 1949.
Graduated from the University of Durham (United Kingdom), a Fellow of the Institute of Chartered Accountants of England and Wales.
Positions in other organisations: adviser to President of ZAO "Sinara Group".
Previous positions held: CFO of the Caspian Pipeline Consortium, Senior Financial Adviser of Shell Exploration and Production Services B.V.
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares owned in OAO "TMK": 0%.

Josef Marous

Born: 1949.
Graduated from Johann Wolfgang Goethe University, Frankfurt-am-Main.
Positions in other organisations: member of the Board of Directors of OOO ThyssenKrupp Materials, member of the Board of Directors of OOO ThyssenKrupp Elevator, Head of representative office of ThyssenKrupp AG in Russia.
Previous positions held: Chairman of the Committee of Automobile Parts Manufacturers of AEB.
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares owned in OAO "TMK": 0%.

Sergey Papin

Born: 1955.
Graduated from Donetsk Polytechnic Institute.
Positions in other organisations: Vice-President of ZAO "Sinara Group".
Previous positions held: Deputy Chief Executive Officer for External and Special Projects of OAO "TMK", Vice-President/Director of Department for Government Relations, Advertising and Public Relations of ZAO KB GUTA-Bank.
Share in the charter capital of OAO "TMK": 0.0004%.
Share of ordinary shares owned in OAO "TMK": 0.0004%.

Geoffrey Townsend

Born: 1949.
Graduated from St. Catherine's College (Oxford), a Fellow of the Institute of Chartered Accountants of England and Wales.
Positions in other organisations: member of the Board of Directors of OAO "Raspadskaya".
Previous positions held: Partner in KPMG, Partner in Deutsche Treuhand-Gesellschaft.
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares owned in OAO "TMK": 0%.

Igor Khmelevsky

Born: 1972.
Graduated from Sverdlovsk Legal Institute.
Positions in other organisations: Vice-President of ZAO "Sinara Group".
Previous positions held: Deputy Chief Executive Officer for Legal Work of OAO "TMK", Head of Department of Legal Issues of ZAO "Sinara Group" in Ekaterinburg.
Share in the charter capital of OAO "TMK": 0.003%.
Share of ordinary shares owned in OAO "TMK": 0.003%.

Alexander Shiryaev

Born: *1952.*
Graduated from Sverdlovsk National Institute of the Economy.
Positions in other organisations: Chief Executive Officer, Vice-President of ZAO "Sinara Group".
Previous positions held: Deputy Chief Executive Officer of Finance and Economics of OAO "TMK", Deputy Chief Executive Officer of Finance and Economics of ZAO "TMK Trading House".
Share in the charter capital of OAO "TMK": 0.006%.
Share of ordinary shares owned in OAO "TMK": 0.006%.

Mukhadin Eskindarov

Born: *1951.*
Graduated from Moscow Finance Institute, Doctor of Economics, Professor.
Positions in other organisations: Rector of the Finance Academy of the Government of the Russian Federation, member of the Board of Directors of OAO "Bank of Moscow", OAO "Rosbank".
Previous positions held: First Vice Rector of the Finance Academy of the Government of the Russian Federation.
Share in the charter capital of OAO "TMK": 0.0002%.
Share of ordinary shares owned in OAO "TMK": 0.0002%.

Results of operations in 2006

The Board of Directors of OAO "TMK" work actively on the strategic management of TMK's operations.

Meetings of the Board of Directors were held at least once per quarter. In 2006, the Board of Directors held 47 meetings, 11 of which were held through joint attendance.

The following table shows the number of meetings held through joint attendance which each director attended in 2006:

Name	Number of meetings
D. Pumpyanskiy	9
P. Galitzine	9
A. Kaplunov	11
A.N.W .Cobb	11
J. Marous	10

Name	Number of meetings
S. Papin	11
G. Townsend	10
I. Khmelevsky	10
A. Shiryaev	10
M. Eskindarov	9

The Board of Directors took decisions on the following important matters in 2006:

- investment plans for 2006 were approved;
- key performance indicators were approved for evaluating the performance of management;
- the development model for the Internal Audit Service was approved;
- the risk management programme was approved;
- the Ethics Code was approved;
- various transactions regarding asset management were approved.

An important element of corporate governance is the joint meetings of the Boards of Directors of OAO "TMK" and its subsidiaries. These joint meetings are held to discuss key aspects of the subsidiaries' operations and to facilitate the regular exchange of information between the corresponding management bodies allowing for a deeper and more objective assessment of the performance of the subsidiaries' boards.

Committees of the Board of Directors

The Board of Directors has three standing committees that assist the Board in performing its duties:

- The Audit Committee
- The Nomination and Remuneration Committee
- The Strategy Committee

The main task of these committees is to make the Board's work more efficient by giving preliminary consideration to certain issues under the Board's competence and preparing the appropriate recommendations.

Each committee provides the Board of Directors with an annual report on the implementation of its tasks for the year. The committees' annual reports (except for confidential information) are included in the materials provided to those entitled to participate in the general meeting of shareholders.

The following table shows the number of meetings which each committee member attended in 2006*:

	The Audit Committee	The Nomination and Remuneration Committee	The Strategy Committee
P. Galitzine			11
A. Kaplunov		16	
A. N.W.Cobb	13		
J. Marous		16	19
G. Townsend	12		
A. Shiryaev			19
M. Eskindarov	5	15	

* *The total number of committee meetings held in 2006 is presented below in sections describing the activity of each Committee.*

The committees hold joint sessions to make their work more effective. In 2006, the Audit Committee held four joint meetings with the Strategy Committee and one with the Nomination and Remuneration Committee. The Strategy Committee and the Nomination and Remuneration Committee also held one joint meeting. In addition, one joint meeting involved all three committees of the Board of Directors.

The Audit Committee

The Audit Committee ensures that there is effective oversight of the process of preparing the financial statements of TMK, of the internal audit function and of risk management measures. Issues within the Committee's purview include:

» Examination of the financial statements.

» Examination and development of recommendations to the Board of Directors regarding standards and procedures to be used in internal controls and risk management.

» Relations with the Revision Commission, the Internal Audit Service and the external auditor (including oversight of the independence of the external auditor).

» Examination of asset valuation issues.

Only independent directors may be members of the Audit Committee; if this is not possible for objective reasons, then only independent directors and directors who are not officers of OAO "TMK" may be members of the Committee.

Throughout 2006 and as of 30 April, 2007, the Audit Committee had the following members:

» G. Townsend *(Committee Chairman)*

» A.N.W. Cobb

» M. Eskindarov

In 2006, the Audit Committee held 13 meetings, of which six were joint meetings with other Committees.

» IFRS financial statements for 2005, the first 9 months of 2006 and 2006.

» Assessment of the independence of the external auditor.

» Selection of a candidate for external auditor.

» Annual work plan and evaluation of the work of the Internal Audit Function.

» Relations between the external auditor and the Internal Audit Function.

» Work of the Risk Management Committee.

Audit Committee Report

Composition and schedule

The members of the Audit Committee throughout the period were G. R. Townsend (Chairman), A. N. W. Cobb and M. Eskindarov. G. R. Townsend and M. Eskindarov are independent non-executive directors, whilst A. N. W. Cobb is a non-executive director who until October 2006 represented the interests of the minority shareholders of the TMK Group and since December 2006 has been employed by companies which, whilst not being part of the TMK group, are controlled by D. Pumpyanskiy.

The formal non-independence of A. N. W. Cobb means that the composition of the Committee is not in full formal compliance with provision C.3.1 of the Combined Code. However, Audit Committee Regulation 3.2 permits his membership; we consider that his employment by other companies controlled by D. Pumpyanskiy does not compromise his independence in substance; furthermore, in our opinion, his former experience as CEO in related industries operating in the CIS environment and subject to strict international reporting rules more than compensates the formal non-independence.

The three members bring varied and complementary experience to the Committee: a former Big 4 partner, a former oil industry CFO and a leading academic.

The Committee normally meets twice between regular Board meetings. The second of these meetings is usually held on the same day as meetings of the Strategy Development and Nomination and Remuneration Committees.

Members of the Committee normally attend the meetings of the other Board committees.

Furthermore, certain topics fall under the competence of more than one committee and joint committee meetings are held to deal with such matters.

Role and authority

The activity of the Audit Committee is governed by “Regulations on the Audit Committee of the Board of Directors of OAO ‘TMK’ ” (The Regulations) which were adopted by the Board on 30 June, 2005 and were last amended on 13 October, 2006; the Regulations are available on the TMK website. In addition, the activities of the Audit Committee are governed by Russian legislation, the statutes of TMK and the Regulations on the Board of Directors. Taken together, the rules are broadly in compliance with section C3 of the Combined Code on Corporate Governance and reflect The Smith Guidance and are actually broader in scope.

Section 6.2 of the Regulations gives the Committee the right, inter alia, to request any information it requires for the discharge of its duties from management and from internal and external auditors.

The Regulations do foresee the Committee’s right to commission independent advice when the Committee deems it necessary (2.15 of the Smith Guidance). The Committee has not felt the need to receive such advice during the year.

Process

Audit Committee meetings are normally open to other members of the Board and relevant representatives from management are invited to attend. The Committee does hold closed sessions with the external auditor from which management and non-Committee members of the Board are excluded. Furthermore, the Committee chairman has free access to the external audit partner.

The Committee sets an annual agenda designed to cover all areas falling under its responsibility. Additional items are added as and when the need arises. The chairman meets with the CFO and external audit partner on a frequent and informal basis to review emerging issues.

The Committee chairman reports a summary of the work undertaken and future work plan to each regular meeting of the Board. On an ad hoc basis the chairman also presents papers to the Board on critical issues.

Furthermore, the Committee prepares an annual report of its activities and submits this report to the Board.

2006 Financial Reports

The Committee reviewed the consolidated financial statements for the year 2005, the nine months to 30 September, 2006 and for the year 2006 as well as the financial reporting sections of prospectuses issued in respect of Eurobonds and the IPO, and recommended their adoption by the Board.

Possible changes in accounting policies or issues arising from the application of accounting policies were discussed with management and with the external auditor.

The external auditor presented his audit plan to the Audit Committee in advance and discussed matters relating to scope. Upon conclusion of the audit, the external auditor presented a summary of findings including summaries of audit adjustments made and potential audit adjustments which had not been made.

Internal control and risk management

The management has created a committee for risk management and has made adequate staff resources available to it. The full remit of the Risk Management Committee is broader than financial, accounting and reporting risk and it reports regularly to the Board and to the Audit and Strategy committees.

The work of the Risk Management Committee is ongoing.

External auditor

There are regular meetings with the external auditor. Parts of these meetings are held without the presence of management or Board members. Furthermore, there is regular informal contact between the Committee chairman and the external audit partner.

TMK's practice concerning awarding contracts for non-audit services to the external auditor is extremely restrictive. The overwhelming majority of fees for services not directly concerned with the performance of the annual audit are in respect of audit-related services connected with bond or share prospectuses.

The external auditor has adequate procedures for rotation of audit partners and senior audit staff.

The Audit Committee has established a procedure for the appointment/reappointment of the external auditor which commences eight months before the annual general meeting at which the auditor is appointed. The procedure is designed to identify and resolve potential problems with quality, service level and remuneration in a timely manner so that a search for a new auditor could, if necessary or desirable, be completed before the annual general meeting.

The Audit Committee has recommended to the Board that it should recommend the reappointment of Ernst & Young for the financial year 2007.

- A summary of audit adjustments proposed by the auditor and accepted by TMK.
- A summary of audit adjustments proposed by the auditor but not accepted by TMK; the external auditor considers the non-acceptance of these proposed adjustments as immaterial in the context of forming an opinion of the economic performance and status of TMK from the financial statements.
- A management letter concerning matters arising from the audit and making recommendations.

As a result of its work on the oversight of the external audit, the Audit Committee recommends acceptance of the external auditor's audit opinion.

Audit Committee evaluation of the external auditor's opinion on the 2006 financial statements

This section describes the Audit Committee oversight of the external audit of the consolidated financial statements of TMK for 2006 and also of the legal entity statutory financial statements of OAO "TMK" for 2006. Most of the oversight activity was carried out in 2007.

The external auditor discussed its plans for the audit of the 2006 financial statements with the Audit Committee before commencement of the audit. During the course of the audit the external auditor discussed potential problems and their resolution with the Audit Committee. At the conclusion of the audit the external auditor presented to the Audit Committee:

Internal audit

TMK has established an internal audit function at both OAO "TMK" and plant level. The internal audit function is governed by regulations on internal audit which have been approved by the Board.

Internal audit activities at plant level are planned, coordinated and controlled by TMK's internal audit function.

Internal audit plans, results and action plans are agreed with the appropriate level of management and reported to management. Action plans are followed up.

The internal audit function presents its plan and all audit reports to the Audit Committee and presents its plan and a summary of the audit results to the Board annually. The presentation of internal audit reports to the Audit Committee is a standing agenda item on the regular agenda of the Audit Committee and is undertaken once between each regular Board meeting.

Performance evaluation

TMK is a young company and its corporate governance procedures are necessarily new. Furthermore, the execution of IPOs in Moscow and London in addition to bond issues, the consolidation of diverse pipe-making activities into a logically consistent group and the expansion of international activities have all required the constant re-examination of corporate governance structures and procedures.

In this light, the Audit Committee sees evaluation of its performance as a continuous activity.

Furthermore, there is an annual performance evaluation as part of the Board's evaluation of the performance of itself and its committees.

TMK subjects itself to an annual corporate governance rating procedure executed by Standard and Poor's, the results of which are published and are available on Standard and Poor's website (http://www.standardandpoors.ru). A large part of this review is concerned with the activities of the Audit Committee. We find the external evaluation and detailed comments very useful – both in detail and as a general incentive "to do better".

The Nomination and Remuneration Committee

The main purpose of the Committee is to provide assistance to the Board of Directors in finding quality executives for the management of TMK and in creating appropriate incentives for them to work successfully.

Issues within the Committee's purview include:

- Setting criteria for candidates to the Board of Directors, the Chief Executive Officer, the Management Board and managers of the main divisions as well as the preliminary assessment of the candidates.
- Establishing the principles and criteria for determining the amount of remuneration, compensation and other payments to members of the Board of Directors, the Chief Executive Officer, the members of the Management Board, managers of the main divisions and members of the Revision Commission.
- Considering candidates for the Chief Executive Officer's position and developing proposals on the membership of the Management Board and on early termination of their authority.
- Regularly evaluating the performance of the Chief Executive Officer and members of the Management Board, and preparing proposals for the Board of Directors on whether to reappoint them as well as a regular performance evaluation of members of the Board of Directors.
- Keeping the Board of Directors informed of changes in corporate governance rules and standards and considering plans to bring TMK's corporate governance system into line with the best Russian and international principles of corporate governance.

Only independent directors may be members of the Nomination and Remuneration Committee; if this is not possible for objective reasons, then only independent directors and directors who are not officers of OAO "TMK" may be members of the Committee.

Throughout 2006 and as of 30 April, 2007, the Nomination and Remuneration Committee had the following members:

- M. Eskindarov *(Committee Chairman)*
- A. Kaplunov
- J. Marous

In 2006, the Committee held 16 meetings, of which three were joint meetings with other Committees. The Committee also worked with officials of TMK on issues overseen by the Committee.

During its meetings, the Nomination and Remuneration Committee considered the following key issues:

- Candidacies for the members of the Board of Directors, the Chief Executive Officer, members of the Management Board and managers of OAO "TMK"'s divisions.
- Determining the amount of remuneration and compensation to members of the Board of Directors, the Chief Executive Officer, members of the Management Board and managers of OAO "TMK"'s divisions.
- Evaluation of the performance of members of the Board of Directors and Committees, the Chief Executive Officer and members of the Management Board.
- Changes to Russian and foreign laws regarding corporate governance standards, principles and procedures.
- Recommendations on changes to OAO "TMK"'s internal regulations and procedures related to corporate governance.
- Performance of the management function by OAO "TMK" in respect of its subsidiaries.
- Implementation of the restructuring programme for the subsidiaries.

The Strategy Committee

The main purpose of the Strategy Committee is to assist the Board of Directors in forming the development strategy for TMK and overseeing its implementation

Issues within the Committee's purview include consideration of proposals:

- On priority areas of operations, including the budgets of various levels, future plans, strategies, and development programmes of OAO "TMK".
- On improving the budgeting system and the investment planning, monitoring and analysis system.
- On key performance indicators and the system for managing OAO "TMK" operations.
- On TMK's investment policy.
- On the strategy for working with shareholder's and borrowed capital.
- On asset and liquidity management policies.
- On dividend policy.

Committee members may be members of the Board of Directors and, where necessary, officers and employees of OAO "TMK" who are not members of the Board of Directors.

Throughout 2006 and as of 30 April, 2007, the Strategy Committee had the following members:

- J. Marous *(Committee Chairman)*
- P. Galitzine
- A. Shiryaev

In 2006, the Committee held 19 meetings of which six were joint meetings with other Committees. All members of the Board of Directors were invited to participate in the Committee meetings.

During its meetings, the Strategy Committee considered the following key issues:

- Investing activity and implementing TMK's strategic programme.
- Acceptance of financial obligations.
- Mergers and acquisitions.
- Dividend policy.
- Development of TMK's strategic partnerships and distribution networks.

8(3) Corporate Governance

EXECUTIVE MANAGEMENT

OAO "TMK" has an effective team of managers who are focused on common goals and have the knowledge, experience and dedication necessary to reach successfully the set goals. There is also a formal Management Board chaired by the Chief Executive Officer (CEO).

The actions of the CEO and the members of the Management Board are regulated by Russian law and regulatory acts, TMK's internal regulations and the contract concluded between each of them and OAO "TMK". OAO "TMK" strives to create the best possible working conditions for the CEO and the Management Board to ensure that they can work effectively in the interests of shareholders.

The CEO and the Management Board are responsible for managing OAO "TMK"'s day-to-day activities and carrying out the decisions of the general shareholders' meeting and the Board of Directors.

The CEO submits Management Board candidates to the Board of Directors for approval and represents the Management Board's point of view at the general shareholders' meetings and at the meetings of the Board of Directors.

As part of his everyday duties the CEO takes decisions on operating issues of OAO "TMK", represents it in relations with third parties, concludes transactions on OAO "TMK"'s behalf, hires and dismisses employees and organises the accounting and reporting functions at OAO "TMK".

The Management Board ensures that objective and considered decisions are taken on the most important and complicated issues of TMK's day-to-day activities.

The following issues are within the competence of the Management Board:

- development of strategic proposals, implementation of the corporate strategy and control over the strategic planning process;
- operating management of OAO "TMK"'s day-to-day activity, including the development and implementation of the current business policy for its main lines of business, approval and monitoring of the implementation of production and shipping programmes, development and monitoring of achievement of key performance indicators, approval and control over budget implementation;
- development and implementation of the overall development strategy and coordination of the activity of OAO "TMK"'s subsidiaries, including organisation of uniform production and technical, financial, pricing, marketing, social and human resource policies at subsidiaries;
- preparation of decisions on various issues of OAO "TMK"'s financial and business activity that have been assigned to the competence of the Board of Directors.

The CEO and the members of the Management Board are elected by the Board of Directors for a term of one year. The Board of Directors may terminate early the authorities of the CEO and members of the Management Board.

On the recommendation of the Nomination and Remuneration Committee, the Board of Directors approved Konstantin Semerikov as the Chief Executive Officer for 2006.

By decision of the Board of Directors, Adrian Popescu and Tigran Petrosian were elected to the Management Board of OAO "TMK" in 2006. Thus, as at 31 December, 2006 the Management Board of OAO "TMK" had the following 14 members:

Konstantin Semerikov

Born: *1959.*
Graduated from Moscow Steel and Alloys Institute.
Position: *the Chief Executive Officer of OAO "TMK".*
Previous positions held: *the Chief Executive Officer of ZAO "TMK Trading House", member of the Management Board of OAO "TAGMET".*
Share in the charter capital of OAO "TMK": 0.01%.
Share of ordinary shares in OAO "TMK": 0.01%.

Anatoly Brizhan

Born: *1942.*
Graduated from the Kirov Urals Polytechnical Institute.
Position: *Managing Director of OAO "SinTZ".*
Previous positions held: *the Chief Executive Officer of OAO "SinTZ".*
Share in the charter capital of OAO "TMK": 0.0001%.
Share of ordinary shares in OAO "TMK": 0.0001%.

Alexei Degai

Born: *1958.*
Graduated from the Kirov Urals Polytechnical Institute.
Position: *Managing Director of OAO "STZ".*
Previous positions held: *the Chief Executive Officer of OAO "STZ".*
Share in the charter capital of OAO "TMK": 0.0002%.
Share of ordinary shares in OAO "TMK": 0.0002%.

Alexander Lyalkov

Born: *1961.*
Graduated from Volgograd Polytechnical Institute.
Position: *Deputy Chief Executive Officer of Production of OAO "TMK".*
Previous positions held: *First Deputy CEO of Production Issues of ZAO "TMK Trading House", Managing Director of OAO "VTZ".*
Share in the charter capital of OAO "TMK": 0.0001%.
Share of ordinary shares in OAO "TMK": 0.0001%.

Nikolai Fartushny

Born: 1949.
Graduated from the M.I. Arsenichev Dneprodzerzhinsky Red Banner of Labour Industrial Institute.
Position: Managing Director of OAO "TAGMET".
Previous positions held: the Chief Executive Officer of OAO "TAGMET".
Share in the charter capital of OAO "TMK": 0.0003%.
Share of ordinary shares in OAO "TMK": 0.0003%.

Sergei Agafonov

Born: 1964.
Graduated from Vakhurshev Sverdlovsk Mining Institute.
Position: Deputy Chief Executive Officer of Supplies of OAO "TMK", Director of Supplies of ZAO "TMK Trading House".
Previous positions held: Deputy Director of Work with Companies of the Fuel and Energy Complex of ZAO "TMK Trading House", the Chief Executive Officer of ZAO "Kuznetsky Ferroalloy Trading House".
Share in the charter capital of OAO "TMK": 0.0005%.
Share of ordinary shares in OAO "TMK": 0.0005%.

Sergei Bilan

Born: 1962.
Graduated from Rostov Institute of Railway Transportation Engineers and the Budget and Treasury Academy of the Ministry of Finance.
Position: Deputy Chief Executive Officer of Marketing of OAO "TMK".
Previous positions held: First Deputy Chief Executive Officer of ZAO "TMK Trading House".
Share in the charter capital of OAO "TMK": 0.0002%.
Share of ordinary shares in OAO "TMK": 0.0002%.

Oleg Borisov

Born: 1953.
Graduated from Sverdlovsk Higher Military Political Tank and Artillery Academy.
Position: Deputy Chief Executive Officer of Security – Director of the Economic Security Service of OAO "TMK.".
Previous positions held: Director of the Security Department of ZAO "Sinara Group", member of the Management Board of AKB SKB-Bank.
Share in the charter capital of OAO "TMK": 0.00006%.
Share of ordinary shares in OAO "TMK": 0.00006%.

Leonid Marchenko

Born: 1951.
Graduated from the Kirov Urals Polytechnical Institute.
Position: Deputy Chief Executive Officer – Chief Engineer of OAO "TMK"
Previous positions held: First Deputy Chief Executive Officer – Chief Engineer of OAO "SinTZ".
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares in OAO "TMK": 0%.

Vladimir Oborsky

Born: 1961.
Graduated from the Frunze Military Academy and the Frunze Kiev Higher Combined Arms Command Academy.
Position: Chief Executive Officer of ZAO "TMK Trading House".
Previous positions held: Director of the Department for Work with OAO "Gazprom", Independent Gas Producers and AK Transneft of ZAO "TMK Trading House".
Share in the charter capital of OAO "TMK": 0.002%.
Share of ordinary shares in OAO "TMK": 0.002%.

Natalia Khonina

Born: 1952.
Graduated from the Gorky Urals State University.
Position: Chief Accountant of OAO TMK, Chief Accountant of ZAO "TMK Trading House".
Previous positions held: Chief Accountant ZAO "Sinara Group".
Share in the charter capital of OAO "TMK": 0.00007%.
Share of ordinary shares in OAO "TMK": 0.00007%.

Vladimir Shmatovich

Born: 1964.
Graduated from Moscow Finance Institute and University of Notre Dame (USA).
Position: Deputy Chief Executive Officer of Finance of OAO "TMK", Deputy Chief Executive Officer of Finance and Economics of ZAO "TMK Trading House".
Previous positions held: Director of Finance and Economics of OOO "RusPromAvto".
Share in the charter capital of OAO "TMK": 0%.
Share of ordinary shares in OAO "TMK": 0%.

Adrian Popescu

Born: 1961.
Graduated from Traian Vuia Politehnica University, Romania.
Position: Chief Executive Officer and Chairman of the Administrative Board of SC TMK-Artrom SA.
Share in the charter capital of OAO "TMK": 0.0011%.
Share of ordinary shares in OAO "TMK": 0.0011%.

Tigran Petrosian

Born: 1968.
Graduated from Yerevan State University.
Position: Deputy Chief Executive Officer of Economics of OAO "TMK".
Share in the charter capital of OAO "TMK": 0.0004%.
Share of ordinary shares in OAO "TMK": 0.0004%.

In 2006, the Management Board of OAO "TMK" held nine meetings five of which were held through joint attendance.

During 2006, the Management Board adopted the following important decisions:

- The human resources policy and human resources policy implementation plan of the plants of TMK were approved.
- The work plan on restructuring companies and the methods of analysis of the economic benefit of the restructuring were approved.
- The environmental protection measures of TMK's production enterprises were approved.
- The programme on creating a corporate-wide system of quality management was approved.
- The strategy for research and development work was approved.
- A number of decisions on the creation of joint ventures were made.

The CEO and the Management Board have two standing committees that assist them in performing their duties.

The Committee on Work with Stock Exchanges and Investors started working in January 2007. The Risk Management Committee has been operating since October 2006. The first results of the latter's work are presented in the report below:

Risk Management Committee Report

The Risk Management Committee reports to the Chief Executive Officer. The Committee is responsible for minimising the risks of TMK operations, developing and improving TMK risk management policy, drafting risk identification, assessment and management methodologies and ensuring that these methodologies are incorporated in TMK business processes.

In 2006, the Risk Management Committee was chaired by the Chief Financial Officer Vladimir Shmatovich and held its first meeting in November 2006. During the last two months of 2006 the Committee considered the following documents:

- Committee Charter;
- Risk Management Policy;
- Risk Management Programme;
- Risk Management Work Plan.

In 2006, the first quarter of 2007 the Committee focused on the following key areas: definition of the main strategic, financing and operating risks of TMK, development of risk monitoring systems, analysis of the insurance coverage level and assessment of the impact of strategic risks on financial results.

8(4) Corporate Governance

REMUNERATION

OAO "TMK" strives to make the principles of remuneration simple, transparent and understandable for shareholders.

The Nomination & Remuneration Committee is responsible for developing the principles and criteria for determining the amount of remuneration, compensation and other payments to members of the Board of Directors, the General Director and the members of the Management Board. The remuneration paid should be fair compensation to the members of the Board of Directors, the Chief Executive Officer and the members of the Management Board for the work they perform and should take into account the long-term interests of shareholders.

Board of Directors

The members of the Board of Directors of OAO "TMK" have the right to receive remuneration and be compensated for expenses related to their work. The remuneration to be paid to each director includes:

- Fixed remuneration for performing the duties of a member/Chairman of the Board of Directors.
- Additional remuneration for managing/participating in the work of committees.

Remuneration for participation in the work of the Board of Directors is paid on a monthly basis (1/12 of the annual fixed amount). Additional remuneration for managing/participating in the work of committees is paid every six months (1/2 of the approved annual additional remuneration).

The contract with the members of the Board of Directors stipulating the payment of remuneration and compensation of expenses to the members of the Board of Directors was approved by decision of the general shareholders meeting of 30 June, 2006. In 2006, the members of the Board of Directors of OAO "TMK" were paid the following amount of remuneration (excluding a gain from the excess of the shares' fair value over the offer price earned through a share sale by "TMK Steel Limited" to a member of the Board of Directors and Management Board)*:

THOUSANDS OF USD

Total remuneration for the performance of the duties of a member/Chairman of the Board of Directors	1,756.2
Total	1,756.2**

** Total gain amounted to USD 1,277.8 thousand.*
*** At the exchange rate 27.185 RUR/USD.*

Executive bodies

Remuneration of the Chief Executive Officer and the members of the Management Board for 2006 consisted of:

- **Salaries,** determined according to the employment contract and paid on a monthly basis.
- **Bonuses,** determined with account taken of goals and target figures, which are established individually for the CEO and each member of the Management Board according to the duties they perform.

The bonus is paid to the CEO and the members of the Management Board if they achieve their goals and meet targets. In general, the performance bonus for the reporting year is paid within 10 business days after the Board of Directors approves the audited RAP financial statements of OAO "TMK" for the reporting year. The bonuses to the CEO, to the Chief Financial Officer and to the Chief Accountant are paid within 10 business days after the Board of Directors approves the audited consolidated IFRS financial statements of OAO "TMK" for the reporting year.

For their work in 2006, the CEO and the members of the Management Board were paid the following amount of remuneration (excluding a gain from the excess of the shares' fair value over its offer price earned through share sale by "TMK Steel Limited" to a member of the Board of Directors and the Management Board)*:

THOUSANDS OF USD

Total salaries	5,264.8
Total bonuses	1,981.4
Total	7,246.2**

Share option programme

In 2007, OAO "TMK" will introduce a share option programme (the Programme) to give incentives to key employees of OAO "TMK" and its subsidiaries, increase their interest in TMK achieving its short- and long-term goals and to converge the economic interests of shareholders and the people on whom the success of TMK's operations depend.

The option programme was approved by an extraordinary shareholders meeting on 2 March, 2007 and split into stages with completion dates in 2007, 2008 and 2009.

Around 100–110 employees have the right to receive options under the Programme, including the members of the Board of Directors, the Management Board and senior management of OAO "TMK" and subsidiaries/associate companies.

The amount of the option package has been established for each group of participants, including the Board of Directors and the Management Board, depending on their impact on OAO "TMK"'s capitalisation and is fixed for the duration of participation in the Option Programme.

Through the Option Programme participants can purchase up to 1.1% of the total ordinary shares in OAO "TMK" as at 1 January, 2007 which equals 9,603,011 shares. Moreover, a reserve for options for new Programme participants in the amount of 0.03% of the total number of

** Total gain amounted to USD 1,277.8 thousand.*
*** At the exchange rate 27.185 RUB/USD.*

ordinary shares in OAO "TMK" as at 1 January, 2007, which equals 261,900 shares, will be formed from the shares allocated to the Option Programme.

Employees and management staff are a key resource for achieving TMK's set goals. That is why TMK constantly strives to improve the system of incentives for personnel and the principles of remuneration.

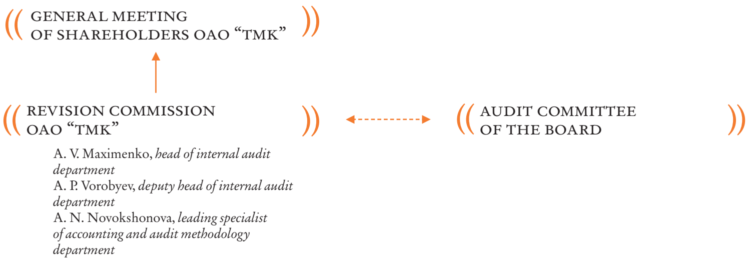
8 (5) Corporate Governance

INTERNAL CONTROL

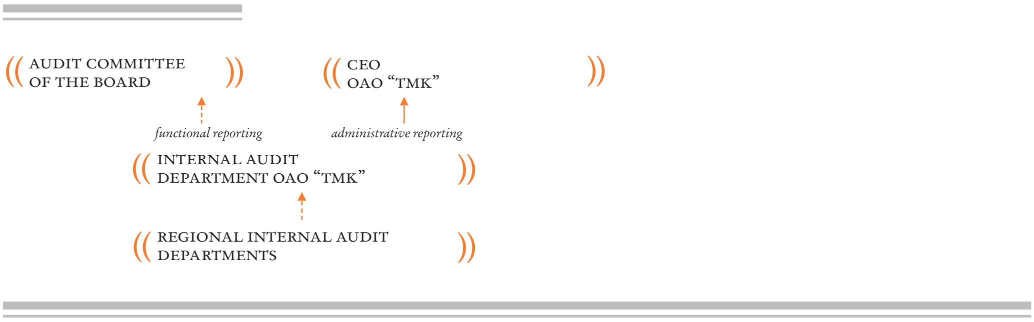
OAO "TMK" has established a multi-tier internal control system which it constantly enhances. Three key structural units of the system help maintain and improve the effectiveness of internal control and risk management processes. The Audit Committee elaborates and drafts recommendations on the functioning of TMK's internal control and risk management system.

THE REVISION COMMISSION. In accordance with Russian legislation, the Charter and the Regulations on the Revision Commission of OAO "TMK", the Revision Commission monitors the financial operations on behalf of shareholders.

The Revision Commission assesses the reliability of the accounting data, financial accounting and management accounting data of OAO "TMK", assesses the financial position of OAO



"TMK", assesses compliance of its operations with external and internal regulations and standards and verifies the competency of decisions adopted by the Board of Directors and executive bodies. Based on the results of comprehensive audits of financial and business activity, the Revision Commission prepares an opinion containing a confirmation of the reliability of the financial statements and other financial documents and also information on violations that have been disclosed.



THE INTERNAL AUDIT SERVICE covers the activity of OAO "TMK" and its subsidiaries. The Internal Audit Service is governed by the Regulations on Internal Audit of OAO "TMK".

The main objective of the Internal Audit (IA) is to provide an objective and independent assessment of the risk management, internal control and corporate governance processes to enhance their reliability and effectiveness. The IA implements this goal through audits of TMK and advisory services to management on internal control, internal audit and risk management issues.

To make sure that it has sufficient independence to implement these tasks, the IA of OAO "TMK" administratively reports to the CEO and functionally to the Audit Committee of OAO "TMK".

Regional internal audit departments are functionally subordinate to the Internal Audit Service of OAO "TMK", reflecting the specifics of the organisational structure of TMK and facilitating an increase in the effectiveness of the Internal Audit Service.

THE RISK MANAGEMENT COMMITTEE is a collegiate consultative body under the Chief Executive Officer. The operations of the Committee are governed by the Regulations on the Risk Management Committee of OAO "TMK".

The main goals of the Committee are to develop and implement the underlying principles of the risk management process in OAO "TMK" and ensure they comply with the development strategy of OAO "TMK" and its divisional units and to identify and assess risks inherent in the activities of TMK.

The Committee started up in 2006. OAO "TMK"'s management has outlined the actions to be taken to develop the Committee's activities in 2007.

OAO "TMK" has also set up departments at divisional level to establish and maintain effective control procedures within the framework of a division. The Accounting and Audit Methodology department, The Economic Security department, the department of Analysis of Investment Activities and other departments are the internal control tools of top and middle level management.

8(6) Corporate Governance

ENHANCEMENT OF CORPORATE GOVERNANCE

The Board of Directors and the executive management of OAO “TMK”are constantly looking for ways to improve corporate governance practices at TMK. In order to become more responsive to changes in corporate governance issues, OAO “TMK” is taking part in the corporate governance rating performed by Standard & Poor’s.

The corporate governance measures being implemented or planned for implementation in the near future include the following key initiatives:

» Expanding co-operation between the Board of Directors and the executive management through open and joint meetings of the committees of the Board of Directors, attended by the members of the executive bodies and OAO “TMK”’s officials.

» Developing management incentive and remuneration practices through a Stock Option Programme and KPI-based performance evaluation of management.

» Improving the procedure for the Board of Directors to assess its own activity.

» Improving the performance and added value of internal audit functions by optimising internal audit functions and assignments and expanding co-operation between the internal audit function and the Audit Committee and the external auditor.

» Further implementation of risk management procedures by drafting a Corporate Risk Management Policy and organising risk identification and assessment processes at the level of OAO “TMK”’s divisions and its subsidiaries.

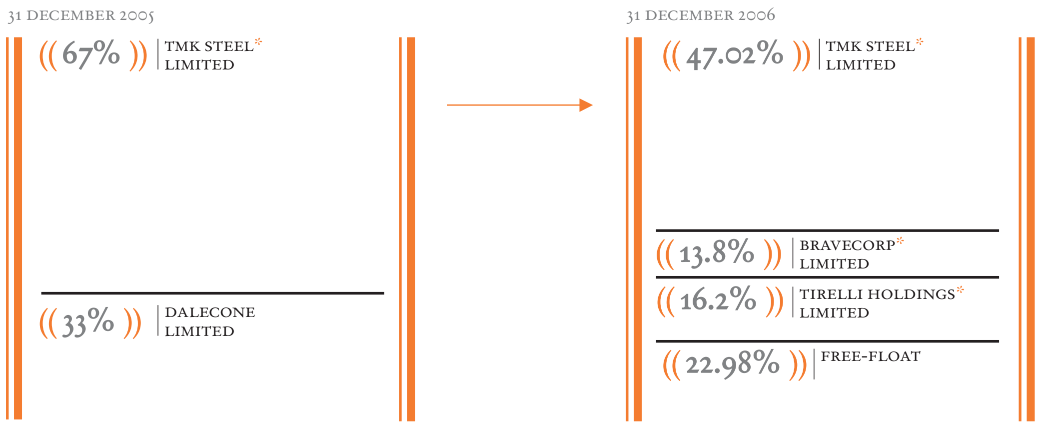
» Improving TMK’s internal regulations by formalising the business processes associated with strategic planning, operating and investment planning, budgeting, business administration, external and internal audit and risk management.

» Improving investor relations through an expansion of the operations of the Committee on Work with Stock Exchanges and Investors.

8(7) Corporate Governance

SHARE CAPITAL

873,001,000 ordinary shares



Free-float:	22.98%
GDRs of OAO "TMK"	19.1%
Shares of OAO "TMK"	3.88%

As of 31 December, 2006 the share capital of OAO "TMK" consisted of 873,001,000 registered ordinary shares, fully paid, issued and outstanding, with a par value of RUB 10 each. All OAO "TMK" shares are registered ordinary shares.

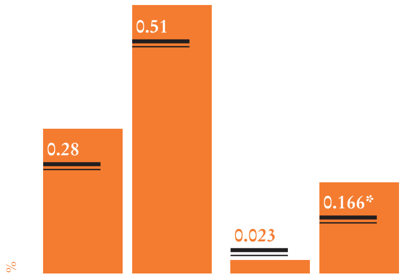
Holders of ordinary shares may vote at all shareholder meetings. In accordance with the Law on Joint-Stock Companies and OAO "TMK"'s charter, all ordinary shares of OAO "TMK" have the same par value and grant identical rights to shareholders. The shares were issued in accordance with the laws of the Russian Federation.

No preference shares of OAO "TMK" are authorised or outstanding.

** Dmitriy Pumpyanskiy is the major shareholder of TMK Steel Limited, Bravecorp Limited and Tirelli Holdings Limited.*

8(8) Corporate Governance

DIVIDENDS



	2005	2006
Earnings per share	0.280	0.510
Dividends per share	0.023	0.166

** Recommended dividends calculated by rate of 1USD=25.84 RUB.*

OAO "TMK" introduced a dividend policy in 2005 which was updated and approved in its current version by the Board of Directors on 21 January, 2007.

The main objective of the dividend policy is to establish a transparent and efficient mechanism for determining dividends and the procedure governing dividend payments. The dividend policy aims to increase OAO "TMK"'s capitalisation, heighten its appeal for investors and to increase the prosperity of shareholders.

In accordance with the renewed dividend policy OAO "TMK"'s target is to pay dividends amounting to at least 25% of annual IFRS consolidated net profits. The actual percentage is based on the net profits for the period, production development needs and investment plans, the availability of external funding and other relevant factors.

A decision on the three-month, six-month and nine-month dividend is adopted at a shareholder meeting within three months of the end of the respective quarter. A decision on annual dividends is taken at the annual general shareholders meeting. Dividends are distributed to shareholders as of the record date of the shareholders meeting which approved the dividend payment.

The dividend policy is published on TMK's website: http://www.tmk-group.com.

TMK did not declare or pay any dividends with respect to the years ended 31 December, 2003 and 2004 owing to the legal structure which was in force at that time and TMK's investment plans.

In 2005, TMK paid interim dividends of USD 2.59 million (RUB 73.33 million), or USD 0.003 per share with respect to the first quarter of 2005. In addition, in 2006 TMK paid annual dividends of USD 17.10 million (RUB 473.36 million), or USD 0.02 per share with respect to the year ended 31 December, 2005.

Owners of GDRs on the relevant record date will be entitled to dividends payable with respect to the ordinary shares subject to the terms and conditions of the Deposit Agreement. TMK will pay cash dividends on the Depositary in roubles which will be converted into US dollars by the Depositary and distributed to holders of GDRs, net of respective taxes and the Depositary's fees and expenses.

stable
growth

TRUST

TMK ANNUAL REPORT 2006

USD **24.7** million

INVESTMENT

An environmental safeguard investment of USD 24.7 million

9(1) Sustainable Development

OVERVIEW

Sustainable Development

THE ECONOMIC DIMENSION

*The economic dimension of sustainability concerns the organization's impacts on the economic conditions of its stakeholders and on economic systems at local, national and global levels.**

THE SOCIAL DIMENSION

*The social dimension of sustainability concerns the impats on organisation has on social systems within which it operates.**

THE ENVIRONMENTAL DIMENSION

*The environmental dimension of sustainability concerns an organisation's impact on living and non-living systems, including ecosystems, land, air, water.**

TMK's management is fully aware of its social responsibility and understands that long-term success is linked to adherence to the principles of sustainable development.

In the modern world it is not enough to be economically efficient. The stability of a company and its prospects for long-term sustainable development are also determined by the quality of its products, its social policy and a judicious approach to environment and natural resources. TMK's concept of sustainable development is founded on maintaining a stable balance between its interests and the interests of all other stakeholders, including investors, employees and the population in the regions where TMK is operating.

TMK's management is aware of the need for systematic sustainable development work and is actively pursuing it.

* *GRI Sustainability Reporting Guidelines, 2006.*

9(2) Sustainable Development

QUALITY MANAGEMENT

Throughout its history TMK has always paid special attention to the quality of its products and has earned a reputation as a reliable supplier of high-quality pipes.

In 2006, TMK set the following main product quality goals:

- to start production of new products with improved performance in line with market demands,
- to increase the output of target products in comparison with 2005 figures;
- to increase customer satisfaction, as measured by the number of legitimate claims and complaints about quality.

All of TMK's goals were successfully met. The introduction of new types of products, the improvement and optimisation of production process and the use of customer questionnaires and surveys resulted in a reduction in customer complaints, in product quality improvement and an increase in sales.

The quality assurance management system in place at TMK's plants complies with ISO 9001:2000 and API Spec Q1 and is based on the following eight principles of quality management:

- customer focus;
- involvement of employees;
- system approach to management;
- factual approach to decision making;
- leadership system;
- process approach;
- continual improvement;
- mutually beneficial supplier relationships.

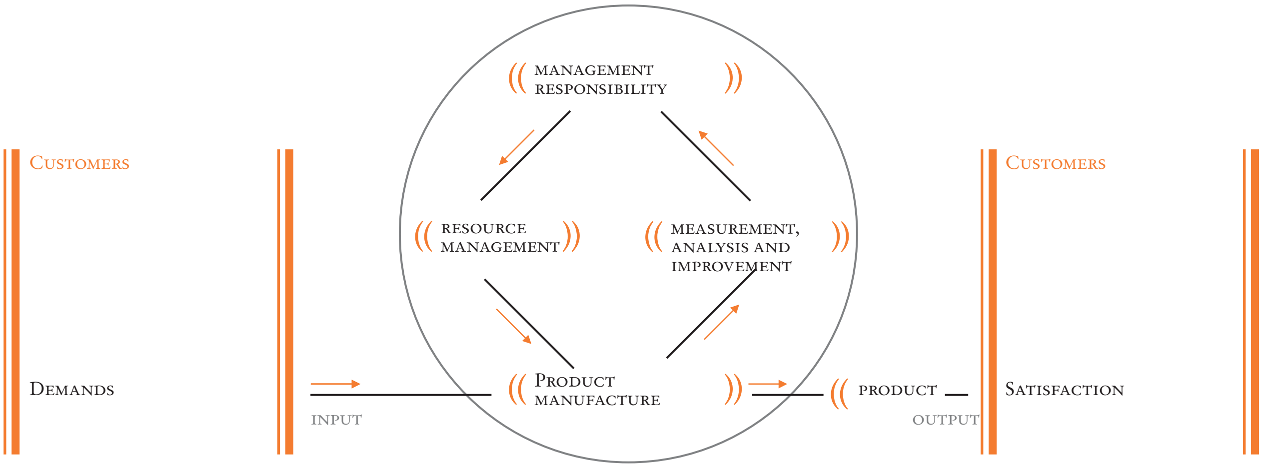
TMK's work in the area of quality assurance management has visible results. All TMK's products are certified according to international standards API, ASTM and European directives and possess all required permits.

A steadily-decreasing number of complaints and claims from TMK's customers attest to the results of the effort being put into quality improvement. The number of claims has been generally low over the last few years and has been consistently falling.

TMK does its best to prevent negative product feedback by working closely with its customers. With this in mind, customer questionnaires and surveys were introduced in 2006 by TMK's trade companies which have direct contact with customers allowing them to obtain customer comments on quality and receive recommendations. This customer feedback is sent to

QUALITY ASSURANCE MANAGEMENT SYSTEM OF TMK PLANTS

Continual Improvement of Quality Assurance Management System



TMK's plants where measures are taken to improve product quality based on the customer's comments. This system has already proven its worth and has made it possible not only to improve the quality of products but also to increase sales.

The quality of TMK's products has been confirmed by leading world oil companies which place extremely strict requirements on their suppliers. At present, TMK is qualified as an official supplier of such companies as KOC (Kuwait), Aramco (Saudi Arabia), Shell, Maersk Oil, NNPC (Nigeria), Bharat (India) and PDVSA (Venezuela).

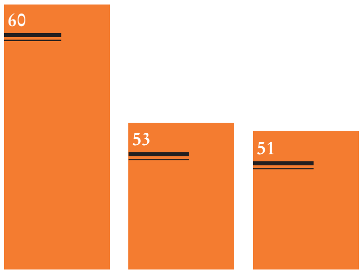
The largest customers of TMK have the opportunity to appraise the Quality Assurance Management System at TMK's plants not only during tenders but also over the effective term of contracts by carrying out audits confirming TMK's status as a qualified supplier. In 2006, no contract was terminated due to TMK's failure to pass such audits.

Specialised organisations hired by TMK's clients for product acceptance also have the chance to verify the quality of the products of TMK. In 2006, experts representing such companies as Moody International, Tuboscope, SGS, Bureau Veritas, Lloyd's Register, Spetsneftegaz, Transsert and others visited TMK's production sites. Acting on behalf of TMK's customers, they gave opinions declaring its products fit for use and issued shipment authorisations. No contract was disrupted in 2006 due to the product quality not meeting the standards of a third party.

TMK today is active in developing a system of "reasonable demands" as a member of the Manufacturers Advisory Group (MAG) of the American Petroleum Institute (API).

Recognising that product quality requirements are becoming stricter, TMK's plans to act accordingly. TMK believes that an effective system of adjustments and preventive measures,

Trend of customers' claims



2004	60
2005	53
2006	51

internal audits, monitoring of processes and products, goal-oriented planning and independent confirmation of compliance instil confidence in its customers of the guaranteed on-time receipt of the required products. Such a system also supports the continuous Quality Assurance Management System.

9(3) Sustainable Development

HUMAN RESOURCES POLICY

TMK is currently one of the largest employers in Russia. More than 49,600 people were employed at TMK's plants and enterprises in 2006.

Salaries and wages

TMK recognises its responsibility towards its employees and their families for stable employment and a decent standard of living.

Total payroll expenses at TMK in 2006 exceeded USD 339.7 million which is 21% higher than the same figure for 2005. This was due to an increase in the average salary and the development of employee incentive systems.

The average monthly salary of employees at TMK's Russian plants grew by 18.6% in 2006 compared to 2005 reaching USD 470. The raise was 6.6% greater than the rate of inflation.

Training programmes

The main areas in employee training in 2006 were:

- Training employees to work on new equipment ensuring that qualified staff is available for the technical upgrading programme.
- Regularly scheduled professional development programmes for factory workers.
- Mandatory training in quality management systems, environmental management and occupational safety.

Some employees of TMK plants underwent more than one training course per year. The targeted training programmes in quality management and environmental management applied to more than 24,000 employees at TMK plants in 2006.

Direct training costs at TMK plants in 2006 amounted to USD 1.7 million of which USD 0.8 million (47%) was for training workers and USD 0.7 million (41%) for training managers which substantially enhanced employees' level of proficiency.

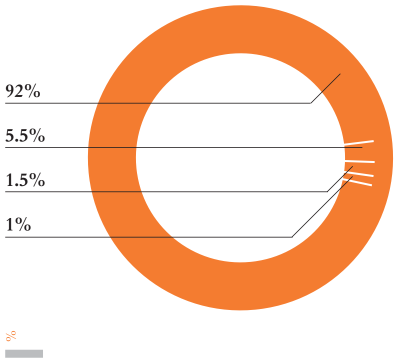
Heath and safety

TMK tries to provide its employees with safe and comfortable working conditions. Occupational and industrial safety for office workers are provided in accordance with State Health and Safety Standards by an occupational and industrial safety system based on the OHSAS 18001 standard.

The Department of Occupational and Industrial Safety monitors and analyses TMK practices in this area and develops programmes to improve the conditions and techniques for ensuring job safety.

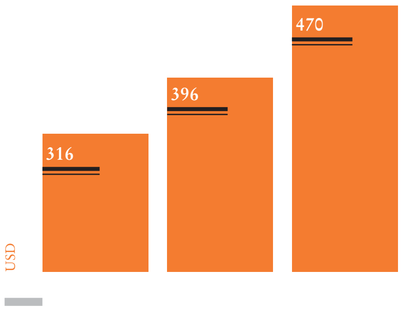
In 2006, TMK's companies spent USD 4.71 million to implement and improve occupational and

Personnel allocation by TMK main activities



Production in Russia	92%
Production in Romania	5.5%
Marketing and Sales	1.5%
OAO "TMK"	1%

Average monthly salary at TMK production companies in Russia



2004	316
2005	396
2006	470

industrial safety measures, to develop good production practices and to create better working and living conditions for its workers. This figure represents a year-on-year increase of 31%. As a result of the measures undertaken, the number of occupational illnesses has been reduced. The number of sick leave days has also decreased (in 2005 by 1.5% compared to 2004, and in 2006 by 2.8% compared to 2005).

Complementing investments in occupational safety improvement programmes, TMK has spent approximately USD 3.7 million on maintaining its own medical facilities and acquiring modern medical equipment. More than USD 4.7 million was spent on promoting physical fitness and sports among workers and maintaining sports facilities and clubs.

Social protection

TMK's social protection system aims to attract and secure qualified specialists. In 2006, costs related to implementing collective bargaining agreements of TMK plants regarding social benefits and guarantees, organising cultural and sporting events, subsidising health treatment and leisure, paying grants to youth and providing material aid to non-working pensioners amounted to USD 15.8 million.

9(4) Sustainable Development

SOCIAL ACTIVITY AND CHARITY

TMK's activities are based on principals of social responsibility. TMK actively supports the welfare of society, strives to improve the territories in which its enterprises are located and makes a solid contribution to their economic and social development. TMK performs this activity on a voluntary basis and spends USD 10–12 million a year on social and charity programmes.

TMK sees social activity as an investment in employees. Since TMK's plants are the major local employers, almost any external social and charitable activity involves TMK's employees to one degree or another. The desire to perform social work is shared by TMK's employees and there are programmes in place at all plants that make it possible for each employee to help the needy.

When selecting the recipients of social and charity work TMK conducts a dialogue with the regional authorities. Underlying TMK's socially oriented activity are multilateral agreements on socio-economic cooperation which are concluded with the municipal and regional governments. Social relations at TMK's companies are secured by collective bargaining agreements.

The priorities of TMK's corporate-wide Programme of social and charity activity include:

- Support for children.
- Support for youth.
- Support for veterans.

As part of its social and charity activity in 2006, TMK subsidised a number of programmes aimed at providing support to children. For example, the Volzhsky Pipe Plant participated in the financing of twelve programmes of the regional Children's Fund: "Warm home", "Behind bars, children's eyes", "Gifted children", "Children's diabetes", "Emergency social assistance", "Life preserver" and others.

TMK recognises its obligation to future generations and implements a number of programmes to support young people. Working youth is getting involved in sports and cultural events. TMK gives young employees the opportunity to receive interest-free housing loans and the chance to receive training and professional development. TMK makes a significant contribution to maintaining and improving the level of education in the regions. TMK's companies finance not only upgrading of the facilities of educational institutions but also award stipends as incentives for the most capable students.

TMK provides financial support for the maintenance and active development of municipal infrastructure. For example, material aid of USD 700,000 was allocated in 2003–2005 for the construction of the Maternity Centre in the city of Kamensk-Uralsky. TMK carries out charity and sponsorship projects to provide effective assistance to national culture, sport, and the physical and spiritual health of people. TMK also supports socially oriented organisations, movements and funds aimed at improving the level of trust and loyalty of the local community to TMK.

9(5) Sustainable Development

ENVIRONMENTAL PROTECTION

Implementation of a balanced environmental policy is an integral part of TMK's strategic development. TMK's main goal in implementing the environmental policy is to do business in accordance with international standards and Russian environmental protection legislation and so achieving a gradual reduction in TMK's environmental impact.

To reach this goal, an Environmental Management System conforming to ISO 14001-2004 has been introduced and is undergoing constant improvement at all TMK's plants. Planning of production activity at the plants is performed based on established environmental targets.

Investment programmes implemented at TMK's enterprises relate to the environmental aspects of TMK's operations and include the implementation of new modern equipment and the best of existing technologies, with strong economic and environmental specifications. In 2006, special investments in environmental measures for all of the TMK's plants totalled USD 24.7 million (RUB 670.1 million).

Air protection

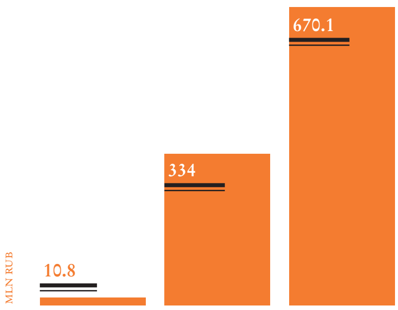
As at any industrial facility, the plants of TMK release pollutants into the atmosphere. These emissions are related to the combustion of organic fuels during production and auxiliary processes.

A total of 12.2 thousand tonnes of atmospheric pollutants were released in 2006 by TMK's Russian plants, 10% less than the previous year. At no point during the reporting year did atmospheric emissions exceed established limits. Per-unit atmospheric emissions at TMK plants in 2006 dropped by 9.5% compared to the previous year.

At SC TMK-Artrom SA and SC TMK-Resita SA plants, atmospheric emissions measurements are taken in accordance with the EU requirements. Emissions at these plants did not exceed established limits in 2006.

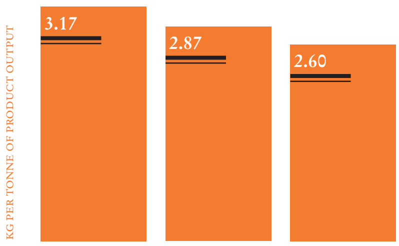
The most significant measures in protecting the atmosphere in 2006 include meeting requirements to reduce the technological impact of the operation of the arc-furnace shop of the Volzhsky Pipe Plant as a result of the stabilisation of the gas-cleaning system. More than USD 4.67 million was spent on rebuilding the gas-cleaning system.

Investment in environmental related activity



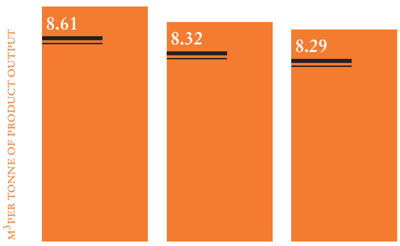
2004	10.8
2005	334
2006	670.1

Per-unit atmospheric emissions



2004	3.17
2005	2.87
2006	2.60

Amount of water taken from natural sources



2004	8.61
2005	8.32
2006	8.29

Emissions of greenhouse gases

In its operations TMK takes due account of the obligations Russia accepted when it ratified the UN Framework Convention on Climate Change (FCCC). TMK has in place a Programme for Implementing Market Mechanisms for Regulating Greenhouse Gas Emissions which stipulates a systematic approach to managing these emissions.

In 2006, the first stage of the Programme was carried out. An inventory of greenhouse gas emissions (from 1990 to 2005) was taken and an evaluation of prospective emissions, taking into account expected production growth to 2012, was performed.

Water protection

TMK's main goals in terms of water protection are to reduce water consumption and decrease the amount of effluents discharged into water bodies.

Despite increased production, a reduction in the consumption of water resources was achieved in 2006. As in previous years, in 2006 the amount of water taken from surface sources, totalling 39 million m^3, did not exceed the established limits. Recycling water systems operate at TMK's plants to ensure efficient usage of natural resources.

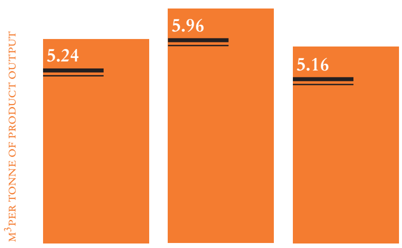
The high percentage of water used in these recycling systems allows TMK to reduce the amount of water taken in and accordingly to reduce the amount of effluent released into surface water bodies. Over the past few years TMK has managed to steadily reduce the amount of water taken from natural sources per tonne of product output.

The use of recycling water systems is mandatory in the reconstruction of facilities. In 2006, when continuous casting machines were installed at TAGMET and Seversky, "clean" and "dirty" water recycling systems were installed. More than USD 14.7 million was allocated for this purpose.

Like all production steelmaking involves the creation and release of waste water. For TMK, including the companies outside Russia, a total of 32 million m^3 of waste water was released into surface waters in 2006 of which Russian plants accounted for 24.3 million m^3.

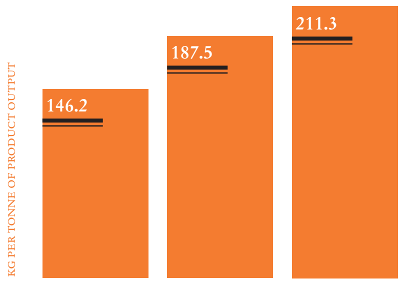
Unit volumes of emissions were reduced at all of TMK's Russian plants. For TMK as a whole, the unit volume of waste-water emissions was cut by 13.4% year-on-year, to 5.16 m^3/t of product.

Amount of waste-water emissions



2004	5.24
2005	5.96
2006	5.16

Volume of waste created



2004	146.2
2005	187.5
2006	211.3

Land protection

TMK performs a great deal of work in protecting land from contamination by industrial waste.

Up to 90% of industrial wastes consist of by-products generated by the main production processes: slag, cinders, furnace waste, ferrous scrap, spent lubricants and sewage sludge.

During 2006, manufacturing activity at TMK's Russian plants resulted in the formation of 992 thousand tonnes of waste.

A certain increase in wastes (107 thousand tonnes) can be seen for TMK as a whole. However, as in the previous year, at no point in 2006 were the established limits exceeded. Unit figures for the creation of wastes rose by 12%. Some of the increase in waste figures is due to the large-scale construction and reconstruction of plants, with the resultant increase in the amount of construction waste.

Of the total amount of waste created, 68% was recycled in production, 21% of waste was transferred to third-party organisations, 7% disposed of at TMK's own sites and 4% was processed and purified.

In order to reduce the quantity of waste disposed of at TMK's own disposal sites, sludge tanks and waste collection sites, a corporate Waste Management Action Plan was adopted in 2006.

Compliance with environmental legislation

TMK's plants emit and dispose the production waste according to the relevant permits issued by law.

In 2006, the Artrom plant received Authorisation of the International Plant Protection Convention – confirmation that the norms of the EU environmental protection directive had been met.

In accordance with Russian law, TMK's Russian plants pay an environmental impact fee. TMK's environmental fees totalled USD 1.1 million in 2006, 3% less than in 2005.

The Romanian plants do not pay environmental pollution fees under European law. Payments are only foreseen in the form of fines if established limits are exceeded and there were no cases of this in 2006.

In the future, TMK's environmental activities will continue to be aimed at strengthening its reputation as a leading company, distinguished by its modern, positive and responsible approach to environmental issues.

10 Consolidated Financial Statements

INDEPENDENT AUDITORS' REPORT

The Shareholders and Board of Directors
OAO TMK

We have audited the accompanying consolidated financial statements of OAO TMK and its subsidiaries ("the Group"), which comprise the consolidated balance sheet as at December 31, 2006, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Basis for Qualified Opinion

We did not observe the counting of the physical inventories at certain subsidiaries of the Group as of December 31, 2004 with carrying value of USD 42,985 thousand, since that date was prior to our appointment as auditors for those subsidiaries of the Group. We were unable to satisfy ourselves as to inventory quantities at that date by other audit procedures. Since opening inventories enter into the determination of the results of operations, we were unable to determine whether adjustments to the results of operations and opening retained earnings might be necessary for the year ended December 31, 2005. Our auditors' report on the consolidated financial statements for the year ended December 31, 2005 was modified accordingly.

Qualified Opinion

In our opinion, except for the effect on the corresponding figures of the adjustments, if any, to the results of operations for the year ended December 31, 2005, which we might have determined to be necessary had we been able to satisfy ourselves as to the matter described in the Basis for Qualified Opinion paragraph, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at December 31, 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC
April 23, 2007

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All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED INCOME STATEMENT

For the year ended December 31, 2006	Notes	2006	2005
Revenue	1	3,384,471	2,938,193
– Goods		3,360,309	2,905,131
– Services		24,162	33,062
Cost of sales	2	(2,350,470)	(2,191,768)
Gross profit		**1,034,001**	**746,425**
Selling and distribution expenses	3	(179,926)	(147,780)
Advertising and promotion expenses	4	(5,083)	(3,084)
General and administrative expenses	5	(157,718)	(123,188)
Research and development expenses	6	(6,725)	(5,547)
Other operating expenses	7	(27,411)	(26,088)
Other operating income	8	9,029	284
Foreign exchange gain/(loss), net		13,005	(14,627)
Finance costs	9	(76,502)	(78,184)
Finance income		15,819	1,837
Profit before tax		**618,489**	**350,048**
Income tax expense	11	(157,885)	(95,880)
Net profit		**460,604**	**254,168**
Attributable to:			
Equity holders of the parent entity		**441,264**	**244,273**
Minority interests		**19,340**	**9,895**
		460,604	**254,168**
Earnings per share attributable to equity holders of the parent entity – basic and diluted (in US dollars)	12	**0.51**	**0.28**

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED BALANCE SHEET

at December 31, 2006	Notes	2006		2005	
ASSETS					
Current assets					
Cash and cash equivalents	13	143,735		47,845	
Short-term investments	14	174,522		1,659	
Accounts receivable	15	273,871		124,996	
Accounts receivable from related parties	28	12,173		28,407	
Inventories	18	588,552		458,932	
Prepayments and input VAT	16	201,045		145,396	
Prepayments to related parties	28	1,027	**1,394,925**	18	**807,253**
Non-current assets					
Investments in associates and other long-term receivables	17	59,090		32,107	
Long-term receivables from related parties	28	46,339		8,486	
Property, plant and equipment	19	1,967,631		1,547,681	
Investment property	19	2,871		2,004	
Goodwill	20	46,944		37,180	
Deferred income taxes	11	14,297		5,432	
Intangible assets	20	15,678	**2,152,850**	12,835	**1,645,725**
TOTAL ASSETS			**3,547,775**		**2,452,978**
LIABILITIES AND EQUITY					
Current liabilities					
Accounts payable and advances from customers	21	349,137		196,819	
Accounts payable to related parties	28	6,702		478	
Accrued liabilities and provisions	22	103,484		108,690	
Finance lease liabilities, current maturities	23	187		1,309	
Borrowings	24	364,541		425,546	
Borrowings from related parties	28	–		31,394	
Dividends		1,383	**825,434**	3,012	**767,248**

(Continued next page.)

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars

CONSOLIDATED BALANCE SHEET / CONTINUED

(Continued.)

at December 31, 2006	Notes	2006		2005	
Non-current liabilities					
Borrowings	24	661,025		164,924	
Finance lease liabilities, net of current maturities	23	244		125	
Deferred income taxes	11	252,002		242,648	
Post-employment benefit	25	20,343		18,009	
Other liabilities	26	18,132	**951,746**	7,343	**433,049**
Total liabilities			**1,777,180**		**1,200,297**
EQUITY					
Parent shareholders' equity					
Issued capital	30	305,407		305,407	
Accumulated profits	30	1,014,443		638,631	
Reserve capital	30	15,387		15,387	
Additional paid-in capital	30	139,340		137,198	
Foreign currency translation reserve		223,729	1,698,306	85,920	1,182,543
Minority interests			72,289		70,138
Total equity			**1,770,595**		**1,252,681**
TOTAL EQUITY AND LIABILITIES			**3,547,775**		**2,452,978**

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT							
	Issued capital	Additional paid-in capital	Reserve capital	Accumulated profits	Foreign currency translation reserve	Total	Minority interests	TOTAL
At January 1, 2006	**305,407**	**137,198**	**15,387**	**638,631**	**85,920**	**1,182,543**	**70,138**	**1,252,681**
Effect of exchange rate changes	–	–	–	–	137,809	**137,809**	8,341	**146,150**
Total income and expense for the year recognised directly in equity	–	–	–	–	137,809	**137,809**	8,341	**146,150**
Net profit	–	–	–	441,264	–	**441,264**	19,340	**460,604**
Total income and expense for the year	–	–	–	441,264	137,809	**579,073**	27,681	**606,754**
Acquisition of Eurosinara S.r.L. (*Note 10*)	–	–	–	(4,876)	–	**(4,876)**	–	**(4,876)**
Excess of the fair value of ordinary shares sold to the Group's employees over the offer price of ordinary shares (*Note 30 vii*)	–	2,142	–	–	–	**2,142**	–	**2,142**
Dividends by subsidiaries of the Group to the minority owners in subsidiaries (*Note 30 vi*)	–	–	–	–	–	–	(476)	**(476)**
Acquisition of minority interests (*Note 30 v*)	–	–	–	(10,812)	–	**(10,812)**	(10,611)	**(21,423)**
De-recognition of minority interests in a subsidiary (*Note 30 viii*)	–	–	–	(12,663)	–	**(12,663)**	(14,443)	**(27,106)**
Dividends (*Note 30 iii*)	–	–	–	(17,101)	–	**(17,101)**	–	**(17,101)**
Other distributions to owners (*Note 30 iv*)	–	–	–	(20,000)	–	**(20,000)**	–	**(20,000)**
At December 31, 2006	**305,407**	**139,340**	**15,387**	**1,014,443**	**223,729**	**1,698,306**	**72,289**	**1,770,595**

(Continued next page.)

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY / CONTINUED

(Continued.)

	Attributable to equity holders of the parent							
	Issued capital	Additional paid-in capital	Reserve capital	Accumulated profits	Foreign currency translation reserve	Total	Minority interests	TOTAL
At January 1, 2005	305,407	135,770	2,376	439,856	127,844	1,011,253	74,103	1,085,356
Effect of exchange rate changes	–	–	–	–	(41,924)	**(41,924)**	(2,753)	**(44,677)**
Total income and expense for the year recognised directly in equity	–	–	–	–	(41,924)	**(41,924)**	(2,753)	**(44,677)**
Net profit	–	–	–	244,273	–	**244,273**	9,895	**254,168**
Total income and expence for the year	–	–	–	244,273	(41,924)	**202,349**	7,142	**209,491**
Appropriation of profit to reserve capital (*Note 30 ii*)	–	–	13,011	(13,011)	–	–	–	–
Dividends by subsidiaries of the Group to the minority owners in subsidiaries (*Note 30 vi*)	–	–	–	–	–	–	(1,192)	**(1,192)**
Dividends by subsidiaries of the Group to the former owner of the subsidiary (*Note 30 iv*)	–	–	–	(9,423)	–	**(9,423)**	–	**(9,423)**
Acquisition of minority interests (*Note 30 v*)	–	1,428	–	–	–	**1,428**	(9,915)	**(8,487)**
Dividends (*Note 30 iii*)	–	–	–	(2,592)	–	**(2,592)**	–	**(2,592)**
Other distributions to owners (*Note 30 iv*)	–	–	–	(20,472)	–	**(20,472)**	–	**(20,472)**
At December 31, 2005	**305,407**	**137,198**	**15,387**	**638,631**	**85,920**	**1,182,543**	**70,138**	**1,252,681**

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED CASH FLOW STATEMENT

December 31, 2006	Notes	2006	2005
Cash flows from operating activities			
Profit before income tax		618,489	350,048
Adjustments for:			
Depreciation of property, plant and equipment	*1*	112,345	104,842
Amortisation of intangible assets	*1*	2,347	809
Loss on disposal of property, plant and equipment	*7*	5,060	4,523
Foreign exchange (gain)/loss		(13,005)	14,627
Finance costs	*9*	76,502	78,184
Finance income		(15,791)	(1,837)
Gain on sale of investments		(28)	–
Excess of the fair value of ordinary shares sold to the Group's employees over the offer price of ordinary shares	*30 vii*	2,142	–
Profit share of the associate	*8*	(1,249)	–
Non-cash donations		–	1,693
Capitalization of previously expensed items		(1,696)	–
Inventory adjustments		(909)	2,325
Bad debt expense	*3*	1,428	1,555
Operating cash flow before working capital changes		**785,635**	**556,769**
Increase in inventories		(74,946)	(59,890)
(Increase) decrease in accounts receivable		(94,333)	49,019
(Increase) decrease in prepayments		(49,666)	10,933
Increase in accounts payable		24,541	22,284
(Decrease) increase in accrued liabilities		(32,613)	19,451
Increase (decrease) in advances from customers		41,320	(76,975)
Cash generated from operations		**599,938**	**521,591**
Income taxes paid		(170,196)	(107,278)
Net cash from operating activities		**429,742**	**414,313**

(Continued next page.)

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in thousands of US dollars, unless specified otherwise

CONSOLIDATED CASH FLOW STATEMENT / CONTINUED

(Continued.)

December 31, 2006	Notes	2006	2005
Cash flows from investing activities			
Purchase of property, plant and equipment		(335,894)	(139,173)
Proceeds from sale of property, plant and equipment		2,990	2,985
Proceeds from sale of investments		166	2,236
Acquisition of Eurosinara S.r.L., net of cash acquired	*10*	(669)	–
Payments for increases in ownership interests in subsidiaries		(21,719)	(6,755)
Deposits at banks		(140,007)	–
Loans granted		(29,960)	431
Proceeds from repayment of loans		–	663
Loans granted to the controlling shareholder		(783,136)	–
Proceeds from repayment of loans granted to the controlling shareholder		779,695	–
Interest received		8,900	1,505
Net cash used in investing activities		**(519,634)**	**(138,108)**
Cash flows from financing activities			
Proceeds from borrowings		1,458,565	1,079,628
Repayment of borrowings		(1,117,840)	(1,207,059)
Interest paid		(71,764)	(77,814)
Payment under finance lease liabilities		(1,406)	(4,113)
Distribution to owners		–	(472)
Prepayment to entities under common control for the transfer of ownership interest in a subsidiary	*28*	(45,512)	–
Payments to entities under common control for the transfer of ownership interest in subsidiaries	*30 iv*	(20,000)	(20,000)
Dividends paid to equity holders of the parent	*30 iii*	(17,101)	(2,592)
Dividends paid to minority shareholders		(2,351)	(9,328)
Net cash from (used in) financing activities		**182,591**	**(241,750)**
Effect of foreign exchange rate changes on cash and cash equivalents		3,191	(93)
Net increase in cash and cash equivalents		95,890	34,362
Cash and cash equivalents at the beginning of the year		47,845	13,483
Cash and cash equivalents at the end of the year		**143,735**	**47,845**

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Corporate Information

These consolidated financial statements of OAO "TMK" and its subsidiaries (the Group) for the year ended December 31, 2006 were authorised for issue in accordance with a resolution of the General Director on April 23, 2007. The parent company of the Group OAO "TMK" (the Company) is registered in the Russian Federation. The list of subsidiaries is disclosed in *Note 27*.

As of December 31, 2006, the Company's main shareholder was TMK Steel Limited, owning 77.02% in the share capital. TMK Steel Limited is ultimately controlled by D.A. Pumpyanskiy.

The Company was incorporated as a closed joint-stock company (ZAO) on April 17, 2001. The Company was re-registered as an open joint-stock company (OAO) on June 16, 2005. The registered office of the Company is 19/25 Alexander Nevsky Street, bldg. 1, Moscow, the Russian Federation. The principal office of the Company is 5th Podsosensky Lane, bldg. 1, Moscow, the Russian Federation.

In 2005 and 2006, there were transactions with an entity under common control with the Group as described below.

Title over 100% ownership interest in Sinara Trading AG, an entity registered in Switzerland, transferred to the Group and control was obtained on May 25, 2005. On February 1, 2006, Sinara Trading AG was re-registered as TMK Global Ltd. TMK Global Ltd. is the Group's distributor of pipe products in countries outside of Russia. This business combination has been accounted for using the pooling of interests method and, as such, the financial statements have been presented as if the transfer of ownership interest in TMK Global Ltd. had occurred from the date of the earliest period presented.

On June 10, 2005, the Group signed an agreement on the purchase of 100% ownership interest in Sinara Handel GmbH, an entity registered in Germany. Sinara Handel GmbH is the Group's distributor of pipe products in countries outside of Russia and the Group's supplier of certain types of raw materials and equipment. Sinara Handel GmbH owns controlling interests in a pipe plant and a metallurgical plant in Romania. Title transferred to the Group and control over Sinara Handel GmbH was obtained by the Group on March 1, 2006. The Group has also applied the pooling of interests method with respect to this acquisition and presented its consolidated financial statements as if the transfer of the controlling interest in Sinara Handel GmbH had occurred from the beginning of the earliest period presented.

As a result of the above-mentioned business combinations with entities under common control with the Group, the Group has re-presented its financial position, results of operations and cash flows for the year ended December 31, 2005.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ CORPORATE INFORMATION / COUNTINUED

On August 25, 2006, the Group signed an agreement on the purchase of 75% ownership interest in open joint-stock company "Orsky Machine Building Plant" for 45,512 thousand US dollars from an entity under common control with the Group. Title transferred to the Group and control over "Orsky Machine Building Plant" was obtained by the Group on January 31, 2007. This purchase of a subsidiary from an entity under common control with the Group will be accounted for using the pooling of interests method. More details are provided in *Note 32*.

The principal activities of the Group are the production and distribution of seamless and welded pipes for the oil and gas industry and for general use.

The Group employed 49,670 employees as of December 31, 2006 (December 31, 2005: 49,628 employees).

Basis of Preparation of the Financial Statements

Statement of Compliance

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

Basis of Accounting

The Group's companies maintain their accounting records in their local currency and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the country in which the particular subsidiary is resident. The consolidated financial statements are based on the statutory accounting records, with adjustments and reclassifications for the purpose of fair presentation in compliance with IFRS. The principal adjustments relate to (1) expense and revenue recognition, (2) valuation of unrecoverable assets, (3) depreciation and valuation of property, plant and equipment, (4) accounting for income taxes, (5) use of fair values, (6) business combinations and (7) translation to the presentation currency.

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below. For example, property, plant and equipment are accounted for at deemed cost at the date of transition to IFRS.

Functional and Presentation Currency

The presentation currency for the purpose of these consolidated financial statements of the Group is the US dollar because the presentation in US dollars is convenient for the major current and potential users of the Group's financial statements.

The functional currency of the Group's subsidiaries located in the Russian Federation, Kazakhstan and Switzerland is the Russian rouble. The functional currencies of other foreign operations of the Group are the euro, the United States dollar, the Romanian lei and the UAE dirham.

The Group has applied IAS 21 (revised), "The Effects of Changes in Foreign Exchange Rates", to translate the financial position of the Group as of December 31, 2006 and the results for the year then ended and corresponding figures into its presentation currency, US dollar, as follows:

(a) assets and liabilities for each balance sheet presented (including corresponding figures) are translated at the closing rate at the date of each respective balance sheet;

(b) income and expenses for each income statement (including corresponding figures) are translated at the weighted average exchange rate for each respective period; and

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS / COUNTINUED

(c) all resulting exchange differences arising from translation of opening net assets at the closing rate and translation of income and expenses at average exchange rates, are recognised as a separate component of equity.

Transactions in foreign currencies are initially recorded in the functional currency at the rate ruling at the date of transaction. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to profit and loss.

Estimates and Assumptions

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

Impairment of Property, Plant and Equipment

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Group estimates the asset's recoverable amount. This requires an estimation of the value in use of the cash-generating units (each individual subsidiary) to which the item is allocated. The determination of impairments of property, plant and equipment involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists. The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management. Methods used to determine the fair value in use include discounted cash flow-based methods, which require the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the fair value and ultimately the amount of any property, plant and equipment impairment. In 2006, no impairment losses were recognised or reversed (2005: nil).

Useful Lives of Items of Property, Plant and Equipment

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". In 2005, the change in estimate of useful lives of property, plant and equipment resulted in an additional depreciation expense of approximately 4,892.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ ESTIMATES AND ASSUMPTIONS / COUNTINUED

Fair Value of Assets and Liabilities Acquired in Business Combinations

The Group is required to recognise separately, at the acquisition date, the identifiable assets, liabilities and contingent liabilities acquired or assumed in the business combination at their fair values, which involves estimates. Such estimates are based on valuation techniques, which require considerable judgment in forecasting future cash flows and developing other assumptions. More details are provided in *Note 10*.

Impairment of Goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at December 31, 2006 was 46,944 (2005: 37,180). More details are provided in *Notes 10* and *20*.

Post-Employment Benefits

The Group uses the actuarial valuation method for measurement of the present value of post-employment benefit obligations and related current service cost. This involves the use of demographic assumptions about the future characteristics of current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, disability and early retirement, etc.) as well as financial assumptions (discount rate, future salary). In the event that further changes in the key assumptions are required, the future amounts of the post-employment benefit costs may be affected materially. More details are provided in *Note 25*.

Allowances

The Group makes allowances for doubtful accounts receivable. Significant judgment is used to estimate doubtful accounts. In estimating doubtful accounts such factors are considered as current overall economic conditions, industry-specific economic conditions, historical and anticipated customer performance. Changes in the economy, industry, or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the consolidated financial statements. As of December 31, 2006 and 2005, allowances for doubtful accounts have been made in the amount of 9,579 and 8,535, respectively (*Notes 15, 17*).

The Group makes allowances for obsolete and slow-moving raw materials and spare parts. As of December 31, 2006 and 2005, allowances for obsolete and slow-moving items were 8,113 and 5,897, respectively (*Note 18*). In addition, certain finished goods of the Group are carried at net realisable value. Estimates of net realisable value of finished goods are based on the most reliable evidence available at the time the estimates are made. These estimates take into consideration fluctuations of price or cost directly relating to events occurring subsequent to the balance sheet date to the extent that such events confirm conditions existing at the end of the period.

Litigation

The Group exercises considerable judgment in measuring and recognising provisions and the exposure to contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation, as well as other contingent liabilities. Judgment is necessary in assessing the likelihood that a pending claim will succeed, or a liability will arise, and to quantify the possible range of the final settlement. Because of the inherent uncertainties in this evaluation process, actual losses may be different from the originally estimated provision. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists, if available, or with the support of outside consultants, such as actuaries or legal counsel. Revisions to the estimates may significantly affect future operating results.

Current Taxes

Russian tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group's entities may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As of December 31, 2006 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. More details are provided in *Note 11*.

Deferred Tax Assets

Management judgment is required for the calculation of current and deferred income taxes. Deferred tax assets are recognised to the extent that their utilization is probable. The utilization of deferred tax assets will depend on whether it is possible to generate sufficient taxable income in the respective tax type and jurisdiction. Various factors are used to assess the probability of the future utilization of deferred tax assets, including past operating results, the operational plan, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from these estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that the assessment of future utilization of deferred tax assets must be reduced and this reduction recognised in profit or loss.

JUDGMENTS

In the process of applying the Group's accounting policies, management has made the following judgment, apart from those judgments involving estimates, which has a significant effect on the amounts recognised in the consolidated financial statements:

Consolidation of a Special Purpose Entity

The Group determined that the substance of the relationship between the Group and TMK Capital SA, a special purpose entity, indicates that TMK Capital SA is controlled by the Group. In September 2006, TMK Capital SA issued notes due September 2009 for the sole purpose of funding a loan to the Company (*Note 24*).

Changes in Accounting Policies

The accounting policies adopted are consistent with those of previous financial year except that the Group has adopted those new/revised standards mandatory for financial years beginning on or after January 1, 2006. The changes in accounting policies result from adoption of the following new or revised standards:

IAS 19 *(amended 2005) "Employee Benefits":*

As of January 1, 2006, the Group adopted the amendments to IAS 19. As a result, additional disclosures are made providing information about trends in the assets and liabilities in the defined benefit plans and the assumptions underlying the components of the defined benefit cost. This change has resulted in additional disclosures being included for the years ending December 31, 2006 and December 31, 2005 but has not had a recognition or measurement impact, as the Group chose not to apply the new option to recognise actuarial gains and losses outside of the income statement.

IAS 21 *(amended 2005) "The Effects of Changes in Foreign Exchange Rates":*

As of January 1, 2006, the Group adopted the amendments to IAS 21. As a result, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements regardless of the currency in which the monetary item is denominated and of which the Group entity transacts with the foreign operation. This change has had no significant impact as at 31 December 2006 or 31 December 2005.

IAS 39 *(amended 2005) "Financial Instruments: Recognition and Measurement":*

The amendment to IAS 39 in 2005:

– required the inclusion of financial guarantee contracts issued;

– permitted the foreign currency risk of a highly probable forecast intra-group transaction to qualify as the hedged item in cash flow hedge, provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and that the foreign currency risk will affect the financial statements;

– restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through profit and loss.

These amendments did not have an effect on the Group's financial statements.

IFRIC 4 *"Determining whether an Arrangement Contains a Lease":*

IFRIC 4 provides guidance for determining whether arrangements are, or contain, leases that should be accounted for in accordance with IAS 17, if the arrangements comprise a transaction or a series of related transactions, that does not take the legal form of a lease but conveys a right to use an asset in return for a payment or series of payments. The adoption of this IFRIC Interpretation as of 1 January, 2006 has not had a significant impact on the Group as at 31 December, 2006 or 31 December, 2005.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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IFRIC 5 *"Rights to Interests Arising from Decommissioning, Restoration and Environmental Rehabilitation Funds":*

IFRIC 5 explains how to treat expected reimbursements from funds set up to meet the costs of decommissioning assets or in undertaking environmental restoration or rehabilitation. As the Group does not currently operate in a country where such funds exist, this interpretation has had no impact on the financial statements.

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

IFRS 7 "Financial Instruments: Disclosures";

IAS 1 (amended 2005) "Presentation of Financial Statements – Capital Disclosures";

IFRIC 8 "Scope of IFRS 2";

IFRIC 9 "Reassessment of Embedded Derivatives";

IFRIC 10 "Interim Financial Reporting and Impairment";

IFRIC 11 "IFRS 2 – Group and Treasury Share Transactions".

The Group expects that the adoption of the pronouncements listed above will have no significant impact on the Group's result of operation and financial positions in the period of initial application. The adoption of IFRS 7 "Financial Instruments: Disclosures" will significantly affect the disclosures relating to financial instruments as presented in the notes to the financial statements. IFRS 7 replaces the disclosure requirements of IAS 32 and must be applied for annual reporting periods that commence on or after January 1, 2007.

SIGNIFICANT ACCOUNTING POLICIES
INDEX TO ACCOUNTING POLICIES

SIGNIFICANT ACCOUNTING POLICIES

A) Principles of Consolidation

Subsidiaries

A subsidiary is an entity in which the Group has an interest of more than one half of the voting rights or otherwise has power to exercise control over its operations.

Subsidiaries are consolidated from the date when control over their activities is transferred to the Company and are no longer consolidated from the date that control ceases.

All intragroup balances, transactions and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transactions provide evidence of an impairment of the asset transferred. Where necessary, accounting policies in subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Acquisition of Subsidiaries

The Group uses the purchase method to account for the acquisition of subsidiaries, except when the acquired entity is under common control with the Group. According to the purchase method, identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair value at the acquisition date, irrespective of the extent of any minority interest.

The excess of the purchase consideration over the fair value of the Company's share of the identifiable net assets is recorded as goodwill. If the cost of the acquisition is less than the fair value of the Company's share of the identifiable net assets of the subsidiary acquired the difference is recorded as a gain in the income statement.

Minority Interest

Minority interest is that portion of the profit or loss and net assets of subsidiaries attributable to equity interests that are not owned, directly or indirectly through subsidiaries, by the parent. Minority interests at the balance sheet date represent the minority shareholders' portion of the fair values of the identifiable assets and liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented within equity, separately from the parent's shareholders' equity.

Losses allocated to minority interest do not exceed the minority interest in the equity of the subsidiary. Any additional losses are allocated to the Group unless there is a binding obligation of the minority to fund the losses.

Increases in Ownership Interests in Subsidiaries

The differences between the carrying values of net assets attributable to interests in subsidiaries acquired and the consideration given for such increases is either added to additional paid-in capital, if positive, or charged to accumulated profits, if negative.

Entering into put options held by minority shareholders in respect of shares of the Group's subsidiaries are accounted for as increases in ownership interests in subsidiaries. Financial liabilities in respect of put options are recorded at fair value at the time of entering into the options, and are subsequently re-measured to fair value with the change in fair value recognised in the income statement.

Acquisition of Subsidiaries from Entities under Common Control

Purchases of subsidiaries from entities under common control are accounted for using the pooling of interests method.

The assets and liabilities of the subsidiary transferred under common control are recorded in these financial statements at the historical cost of the controlling entity (the Predecessor). Any difference between the total book value of net assets, including the Predecessor's goodwill, and the consideration paid is accounted for in these consolidated financial statements as an adjustment to equity.

These financial statements, including corresponding figures, are presented as if the Company had acquired the subsidiary on the date it was initially acquired by the Predecessor.

B) Cash and Cash Equivalents

Cash is comprised of cash in hand and cash at banks.

Cash equivalents are comprised of short-term, highly liquid investments (with original maturity date of less than 90 days) that are readily convertible to known amounts of cash and which are subject to insignificant risk of changes in value. Cash equivalents are carried at fair value.

C) Investments and Other Financial Assets

Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, and available-for-sale investments, as appropriate. When investments are recognised initially, they are measured at fair value plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

The Group determines the classification of its investments after initial recognition. All regular way purchases and sales of financial assets are recognised on the trade date, which is the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets classified as held for trading are included in the category "financial assets at fair value through profit or loss". Financial assets are classified as *held for trading* if they are acquired for the purpose of selling in the near term. Gains or losses on investments held for trading are recognised in the income statement. During the period the Group did not hold any investments in this category.

SIGNIFICANT ACCOUNTING POLICIES
/ C) INVESTMENTS AND OTHER FINANCIAL ASSETS / COUNTINUED

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as *held-to-maturity* when the Group has the positive intention and ability to hold to maturity. During the period the Group did not hold any investments in this category.

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

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition, available for sale financial assets are measured at fair value with gains or losses being recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement. Reversals of impairment losses in respect of equity instruments are not recognised in the income statement. Impairment losses in respect of debt instruments are reversed through profit or loss if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement.

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

D) Trade Receivables

Trade receivables, which generally have a short term, are carried at original invoice amount less an allowance for doubtful debts. An allowance for doubtful debts is established when there is objective evidence that the Group will not be able to collect amounts due according to the original terms of contract. The Group periodically analyses the aging of trade receivables and makes adjustments to the amount of the allowance. The amount of the allowance is the difference between the carrying and recoverable amount. The amount of the doubtful debts expense is recognised in the income statement.

E) Borrowings

Borrowings are initially recognised at cost, being the fair value of the proceeds received, net of directly attributable transaction costs. In subsequent periods, borrowings are measured at amortised cost using the effective interest rate method. Any difference between the initial fair value of the consideration (net of transaction costs) received and the redemption amount is recognised within interest expense over the period of the borrowings.

The finance cost of the loans, including the issue costs and any discount on issue, is dealt with as a profit and loss charge over the term of the debt at a constant rate on the carrying amount. The carrying amount of the loan is decreased by the unamortised balance of the issue costs.

SIGNIFICANT ACCOUNTING POLICIES / COUNTINUED

F) Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and costs necessary to make the sale. The cost of inventories is determined on the weighted average basis.

The costs of inventories are comprised of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present condition and location. The cost of work in progress and finished goods includes costs of raw materials, direct labor and other direct productions costs and related production overheads (not including borrowing costs).

The Group periodically analyses inventories to determine whether they are damaged, obsolete or slow-moving or if their net realisable value has declined, and makes an allowance for such inventories.

In preparing consolidated financial statements, unrealised profits resulting from intragroup transactions are eliminated in full.

G) Property, Plant and Equipment

Property, plant and equipment, except for the items acquired prior to January 1, 2003, are stated at historical cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any impairment in value. Such cost includes the cost of replacing part of plant and equipment when the cost is incurred if the recognition criteria are met.

The items of property, plant and equipment acquired prior to January 1, 2003, the date of transition to IFRS, were accounted for at deemed cost being their fair value at January 1, 2003.

Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

Land	Not depreciated
Buildings	8 – 100 years
Machinery and equipment	5 – 30 years
Transport and motor vehicles	4 – 15 years
Furniture and fixtures	2 – 10 years

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

When each major inspection is performed, its cost is recognised as a component in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

The Group has the title to certain non-production and social assets, primarily buildings and social infrastructure facilities. The items of social infrastructure do not meet the definition of an asset according to IFRS. Construction and maintenance costs of social infrastructure facilities are expensed as incurred.

H) Investment Property

Investment property is stated at historical cost, excluding the costs of day-to-day servicing less accumulated depreciation and any impairment in value. Such cost includes the cost of replacing part of such investment property when the cost is incurred if the recognition criteria are met.

Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

Land	Not depreciated
Buildings	8–100 years
Machinery and equipment	5–30 years
Transport and motor vehicles	4–15 years
Furniture and fixtures	2–10 years

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

I) Leases

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

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to interest expense in the income statement.

The depreciation policy for depreciable leased assets is consistent with that for depreciable assets, which are owned. If there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, the asset is fully depreciated over the shorter of the lease term or its useful life.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

SIGNIFICANT ACCOUNTING POLICIES
/ COUNTINUED

J) Goodwill

Goodwill is recognised as a non-current asset from the acquisition date. Goodwill represents the excess of the cost of an acquisition over the fair value of the Company's share of the net assets of the acquired subsidiary at the date of acquisition.

Goodwill is not amortised but is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that carrying amount may be impaired. As at the acquisition date, any goodwill is allocated to each of the cash-generating units (groups of cash-generating units), expected to benefit from the synergies of the combination. Impairment is determined by assessing the recoverable amount of the cash-generating unit (groups of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (groups of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation.

If the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate exceeds the cost of the business combination, the identifiable assets, liabilities and contingent liabilities are re-assessed and re-measured. Any excess remaining after reassessment is immediately recognised in profit or loss.

K) Other Intangible Assets

Intangible assets are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Amortisation is calculated on a straight-line basis over the expected useful life of an intangible asset. Intangible assets are amortised over their useful economic lives of 2 to 5 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation expense of intangible assets is recognised in the income statement in the expense category consistent with the function of the intangible asset.

Research and Development

Research costs are recognised as an expense as incurred. Costs incurred on development (relating to the design and testing of new or improved products) are recognised as intangible assets only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete and the ability to measure reliably the expenditure during the development. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs that have been capitalized are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of its expected benefit. The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use or more frequently when an indication of impairment arises during the reporting year.

Other Intangible Assets

Expenditure on acquired patents, trademarks, licenses and software is capitalised and amortised on a straight-line basis over their expected useful lives.

L) Impairment of Non-Financial Assets (Other than Goodwill)

An assessment is made at each balance sheet date to determine whether there is objective evidence that an asset or a group of assets may be impaired. When there is an indication that an asset may be impaired, the recoverable amount is assessed and, when impaired, the asset is written down immediately to its recoverable amount, which is the higher of the net selling price and value in use.

Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, after deducting any direct incremental disposal costs. Value in use is the present value of estimated future cash flows expected to arise from continuing use of an asset and from its disposal at the end of its useful life.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Impairment loss is recognised for the difference between the estimated recoverable amount and the carrying value. The carrying amount of the asset is reduced to its estimated recoverable amount either directly or through the use of an allowance account and the amount of the loss is included in the net profit and loss for the period.

An impairment loss is reversed if the subsequent increase in the recoverable amount can be related objectively to an event occurring after the impairment loss was recognised. An impairment loss is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

Intangible assets not yet available for use are tested for impairment annually.

M) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

N) Employee Benefits

Social and Pension Contributions

In the normal course of business the Group contributes to state pension, social insurance, medical insurance and unemployment funds at the statutory rates in force, based on gross salary payments. These contributions are made in compliance with statutory requirements of those countries where the Group's subsidiaries are located. The Group has no legal or constructive obligation to pay further contributions in respect of those benefits. Its only obligation is to pay contributions as they fall due. These contributions are expensed as incurred.

Post-Employment Benefits

The Group's companies provide additional pensions and other post-employment benefits to their employees in accordance with collective bargaining agreements. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age, the completion of a minimum service period and the amount of the benefits stipulated in the collective bargaining agreements.

The liability recognised in the balance sheet in respect of post-employment benefits is the present value of the defined benefit obligation at the balance sheet date less the fair value of the plan assets, together with adjustments for unrecognised actuarial gains or losses and past service costs. The defined benefit obligation is calculated annually using the projected unit credit method. The present value of the benefits is determined by discounting the estimated future cash outflows using interest rates of high-quality government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related obligations.

Actuarial gains and losses are recognised in the income statement in the period in which they occur. The past service cost is recognised as an expense on a straight line basis over the average period until the benefits become vested.

O) Value Added Tax

The Russian tax legislation permits settlement of value added tax (VAT) on a net basis.

Value Added Tax Payable

Prior to 2006, VAT was payable by the Group to tax authorities upon collection of receivables from customers. VAT on purchases, which had been settled at the balance sheet date, was deducted from the amount of VAT payable. In addition, VAT related to sales which had not been collected, and therefore currently not due, at the balance sheet date was included in the VAT payable line item.

Starting from 2006, VAT is payable upon invoicing and delivery of goods, performing work or rendering services, as well as upon collection of prepayments from customers. VAT on purchases, even if they have not been settled at the balance sheet date, is deducted from the amount of VAT payable.

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

Value Added Tax Recoverable

VAT recoverable arises when VAT related to purchases exceeds VAT related to sales.

In addition, prior to 2006, the VAT recoverable line item included VAT related to purchases, which had not been settled at the balance sheet date, and to property, plant and equipment not yet put into operation. However, this amount was reclaimable against VAT related to sales only upon payment for the purchases or putting property, plant and equipment into operation.

SIGNIFICANT ACCOUNTING POLICIES / COUNTINUED

P) Deferred Income Tax

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

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

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

Q) Equity

Share Capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity.

Dividends

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

R) Revenue Recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the amount of revenue can be measured reliably. Revenues from sales of inventory are recognised when the significant risks and rewards of ownership of the goods have passed to the buyer. Revenues from rendering of services are recognised in the period when the services are provided.

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, the revenue is measured at the fair value of the goods or services given up.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1) Segment Information

The consolidated financial statements of the Group are reported in two segment reporting formats: business and geographical.

There are no sales or other transactions between the business segments.

The Group's primary segment reporting format is the dominant source for disclosure of its operating activities in its financial statements. A business segment is a distinguishable component of the Group that is engaged in providing an individual product or service or a group of related products or services and that is subject to risks and returns that are different from those of other business segments. The Group discloses its sales revenue, gross profit, assets, liabilities and depreciation costs based on the main groups of products segregated into segments: seamless pipes, welded pipes, other operations, unallocated. Unallocated segment assets and liabilities include those assets and liabilities which can not be analyzed by segments, such as cash, short-term investments, goodwill, borrowings and deferred tax assets and liabilities. They also include assets of maintenance workshops servicing production processes of both seamless and welded pipes.

A geographical segment is the Group's secondary segment reporting format for disclosure of its operating activities in its financial statements. A geographical segment is a distinguishable component of the Group that is engaged in providing products or services within a particular economic environment and that is subject to risks and returns that are different from those components operating in other economic environments. The Group discloses its sales revenue, based on the location of the Group's customers. Segment assets, long-term investments and depreciation expenses are disclosed based on the location of the Group's assets.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 1) SEGMENT INFORMATION / COUNTINUED

Primary reporting format – business segments

year ended December 31, 2006

	Welded pipes	Seamless pipes	Other operations	Unallocated	TOTAL
Revenue	948,955	2,216,145	219,371	–	**3,384,471**
Gross profit	143,567	877,014	13,420	–	**1,034,001**
Segment assets	435,072	1,857,501	35,130	1,220,072	**3,547,775**
Segment liabilities	49,136	213,874	16,984	1,497,186	**1,777,180**
Additions to property, plant and equipment	5,942	251,181	1,936	112,921	**371,980**
Depreciation and amortisation	10,066	84,363	3,986	16,277	**114,692**

year ended December 31, 2005

	Welded pipes	Seamless pipes	Other operations	Unallocated	TOTAL
Revenue	912,877	1,788,045	237,271	–	**2,938,193**
Gross profit	128,792	594,836	22,797	–	**746,425**
Segment assets	277,360	1,419,965	40,199	715,454	**2,452,978**
Segment liabilities	14,370	156,162	7,160	1,022,605	**1,200,297**
Additions to property, plant and equipment	1,663	119,640	4,206	13,796	**139,305**
Depreciation and amortisation	9,817	77,143	4,080	14,611	**105,651**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 1) SEGMENT INFORMATION / COUNTINUED

Secondary reporting format – geographical segments

Distribution of the Group's revenue by geographical area based on the location of customers was as follows:

year ended December 31, 2006	Russia	Europe	Central Asia & Caspian Region	Middle East & Gulf Region	Africa	Americas	Asia & Far East	TOTAL
Revenue	2,308,545	586,190	177,648	183,027	12,853	102,421	13,787	**3,384,471**
Segment assets	3,057,774	465,566	4,494	454	–	19,487	–	**3,547,775**
Additions to property, plant and equipment	333,465	38,194	37	73	–	211	–	**371,980**

year ended December 31, 2005	Russia	Europe	Central Asia & Caspian Region	Middle East & Gulf Region	Africa	Americas	Asia & Far East	TOTAL
Revenue	2,041,502	514,323	77,130	127,410	3,501	126,701	47,626	**2,938,193**
Segment assets	2,061,433	380,292	11,253	–	–	–	–	**2,452,978**
Additions to property, plant and equipment	102,523	36,782	–	–	–	–	–	**139,305**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

2) Cost of Sales

	2006	2005
DIRECT COST		
Raw materials	1,575,639	1,481,500
Add-on materials of production	82,290	80,731
Labor cost	93,164	76,250
Contracted services	11,701	4,578
Energy	107,508	82,707
Total direct cost	**1,870,302**	**1,725,766**
PRODUCTION OVERHEADS		
Salaries and wages	178,332	150,607
Other compensation	8,587	7,669
Travel	1,331	756
Freight	5,822	3,135
Communications	674	356
Professional services	7,462	6,618
Rent/occupancy	310	253
Utilities	68,037	59,841
Depreciation	105,936	98,880
Insurance	285	114
Taxes	14,581	12,692
Repairs and maintenance	24,659	18,449
Supplies	96,420	86,740
Specialised tools	15,451	12,501
Other	563	2,062
Less: capitalized costs	(14,652)	(6,633)
Total production overhead charges	**513,798**	**454,040**
Changes in inventory	**(54,306)**	**(7,138)**
Cost of merchandise	**20,232**	**16,708**
INVENTORY ADJUSTMENT		
Book to physical	(1,125)	67
Obsolete and slow-moving	1,569	2,325
Total inventory adjustment	**444**	**2,392**
Total cost of sales	**2,350,470**	**2,191,768**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

3) Selling and Distribution Expenses

	2006	2005
Salaries and wages	32,591	23,756
Other compensation	864	397
Travel	3,346	2,360
Freight	104,402	88,905
Communications	1,417	1,115
Professional services	13,483	10,399
Rent/occupancy	4,614	4,050
Utilities	119	258
Depreciation	1,504	1,217
Insurance	682	619
Taxes	196	81
Repairs and maintenance	386	170
Supplies	12,967	11,504
Bad debt expense	1,428	1,555
Other	1,927	1,394
Total selling and distribution expenses	**179,926**	**147,780**

4) Advertising and Promotion Expenses

	2006	2005
Media	1,183	784
Exhibits and catalogues	3,094	1,928
Other	806	372
Total advertising and promotion expenses	**5,083**	**3,084**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

5) General and Administrative Expenses

	2006	2005
Salaries and wages	88,595	66,331
Other compensation	5,591	5,550
Travel	8,707	4,466
Freight	1,099	666
Communications	1,084	832
Professional services	26,268	22,344
Rent/occupancy	3,029	2,617
Utilities	3,495	3,445
Depreciation	6,876	5,569
Insurance	358	443
Taxes	2,764	2,367
Repairs and maintenance	2,667	1,550
Supplies	6,154	5,572
Other	1,031	1,436
Total general and administration expenses	**157,718**	**123,188**

6) Research and Development Expenses

	2006	2005
Salaries and wages	4,351	3,018
Other compensation	123	105
Travel	100	58
Freight	108	29
Communications	36	21
Professional services	1,021	866
Utilities	200	121
Depreciation	296	955
Repairs and maintenance	64	69
Supplies	420	297
Other	6	8
Total research and development expenses	**6,725**	**5,547**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

7) Other Operating Expenses

	2006	2005
Loss on disposal of property, plant and equipment	5,060	4,523
Social and social infrastructure maintenance expenses	10,597	11,124
Charitable donations	11,754	7,488
Other	–	2,953
Total other operating expenses	**27,411**	**26,088**

8) Other Operating Income

	2006	2005
Gain on sale of current assets	245	158
Profit share of the associate	1,249	–
Government grants	3,676	–
Other	3,859	126
Total other operating income	**9,029**	**284**

The Company's share in the profit of an associate in the amount of 1,249 represents a 20% interest in profit of the associate in 2006. In 2005 the associate did not conduct any selling or production activities.

In compliance with the Federal Act on partial reimbursement of loan interest expenses to Russian exporters of manufactured goods 3,676 were reimbursed by the federal authorities in 2006.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

9) Finance Costs

	2006	2005
Amortisation of ancillary costs incurred in connection with the arrangement of borrowings	8,038	2,540
Interest expense	68,464	75,644
Total finance cost	**76,502**	**78,184**

10) Acquisition of Eurosinara S.r.L.

As at December 31, 2005, the Group had 50% interest in Eurosinara S.r.L., an entity registered in Italy, which is the Group's distributor of pipe products in Southern Europe. On May 16, 2006, the Group purchased the remaining 50% interest in Eurosinara S.r.L. for 1,000 thousand euros (1,290 at the exchange rate as of the date of transfer), increasing its interest to 100%.

The acquisition of Eurosinara S.r.L. was accounted for based on provisional values, as the subsidiary, as of the date of authorisation for issue of these financial statements, has not completed the preparation of its IFRS financial statements.

The table below sets forth the fair values of Eurosinara's identifiable assets, liabilities and contingent liabilities at the date of acquisition:

	May 16, 2006
Property, plant and equipment	15
Deferred income tax assets	2,785
Other non-current assets	2
Inventories	4,087
Accounts and notes receivable, net	14,642
Cash	621
Other current assets	87
Total assets	**22,239**
Non-current liabilities	701
Current liabilities	31,290
Total liabilities	**31,991**
Net liabilities	**(9,752)**
Fair value of net liabilities attributable to 50% ownership interest additionally acquired on May 16, 2006	(4,876)
Goodwill arising on acquisition	6,166
Consideration paid	**1,290**

All amounts are in thousands of US dollars, unless specified otherwise

Eurosinara S.r.L.'s net profit for the period from May 16, 2006 to December 31, 2006 amounted to 1,051.

If the combination had taken place on January 1, 2006, the net revenue and net profit of the Group for the year ended December 31, 2006 would have been 3,383,896 and 460,212, respectively.

Net liabilities of Eurosinara S.r.L. as of May 16, 2006 of 4,876 relating to the 50% interest owned by the Group before the business combination were recorded as a reduction in accumulated profits in the consolidated financial statements for the year ended December 31, 2006.

11) Income Tax

	2006	2005
Current income tax	176,046	118,004
Deferred income tax benefit related to origination and reversal of temporary differences	(18,161)	(22,124)
Total income tax expense	**157,885**	**95,880**

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

	2006	2005
Income before taxation	618,489	350,048
Theoretical tax charge at statutory rate in Russia of 24%	148,437	84,011
Tax effect of items which are not deductable or assessable for taxation purposes:		
Reversal of provision for tax fines	–	(1,133)
Other non-deductible expenses	13,587	12,207
Effect of different tax rates in countries other than Russia	(1,680)	(48)
Effect of changes in tax legislation in Romania	(2,312)	–
Effect of currency translation	(516)	(152)
Deferred income tax provided for undistributed earnings of the Group's subsidiaries	369	995
Total income tax expense	**157,885**	**95,880**

In 2006, certain changes, introduced in the tax legislation in Romania, resulted in adjustments to the tax base of property, plant and equipment.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 11) INCOME TAX / COUNTINUED

Deferred income tax assets and liabilities at December 31 and their movements for the periods ended December 31 were as follows:

	2006	Change recognised in income statement	Change due to business combiation	Foreign currency translation reserve	2005	Change recognised in income statement	Foreign currency translation reserve	2004
Deferred income tax liabilities:								
Property, plant and equipment	(245,197)	22,132	26	(22,116)	(245,239)	18,496	9,495	(273,230)
Accounts receivable	(8,413)	–	–	(717)	(7,696)	–	287	(7,983)
Inventory	(2,091)	372	96	(205)	(2,354)	2,312	133	(4,799)
Undistributed earnings of subsidiaries	(644)	412	–	(78)	(978)	24	37	(1,039)
Other	(345)	(323)	–	(9)	(13)	689	14	(716)
	(256,690)	**22,593**	**122**	**(23,125)**	**(256,280)**	**21,521**	**9,966**	**(287,767)**
Deferred income tax assets:								
Tax losses available for offset	9,374	(1,939)	–	906	10,407	(655)	(401)	11,463
Accrued liabilities	1,932	(459)	–	190	2,201	(2,110)	(123)	4,434
Accounts receivable	4,166	(320)	2,663	200	1,623	605	(49)	1,067
Prepayments and other current assets	304	(243)	–	39	508	(571)	(30)	1,109
Provisions	7,845	1,468	–	586	5,791	3,371	(150)	2,570
Finance lease obligations	3	(312)	–	18	297	(1,263)	(35)	1,595
Trade and other payable	407	(2,627)	–	181	2,853	1,226	(83)	1,710
	24,031	(4,432)	2,663	2,120	23,680	603	(871)	23,948
Net tax effect of temporary differences	–	18,161	–	–	–	22,124	–	–
Less: not recognised deferred income tax asset	(5,046)	–	–	(430)	(4,616)	–	(5)	(4,611)
Net deferred income tax liability	**(252,002)**	**18,161**	**2,785**	**(21,435)**	**(242,648)**	**22,124**	**9,090**	**(271,508)**
Net deferred income tax assets	**14,297**	**–**	**–**	**–**	**5,432**	**–**	**–**	**2,901**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 11) INCOME TAX / COUNTINUED

The amounts shown in the balance sheet include the following:

	2006	2005
Deferred tax assets to be recovered after more than 12 months	4,162	5,745
Deferred tax liabilities to be settled after more than 12 months	(245,197)	(245,239)

In the context of the Group's current structure, tax losses and current tax assets of the different companies may not be set off against current tax liabilities and taxable profits of other companies and, accordingly, taxes may accrue even where there is a net consolidated tax loss. Therefore, a deferred tax asset of one company of the Group is not offsettable against the deferred tax liability of another company. As at December 31, 2006, a deferred tax asset in the amount of 5,046 (2005: 4,616) has not been recorded as it is not probable that sufficient taxable profit will be available to offset the deductible temporary differences to which the asset relates.

Deferred income tax asset not recognised represents a tax loss of one of the Group's subsidiaries incurred in transactions with securities. Such tax loss could be offset only against future taxable profits generated in transactions with securities over a period of 10 years. The Group believes that it is unlikely that this tax loss will be utilized.

As of December 31, 2006, the Group has not recognised deferred tax liability in respect of 886,918 (2005: 370,443) temporary differences associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

12) Earnings per Share

Earnings per share are calculated by dividing the net profit attributable to ordinary shareholders of the parent entity by the weighted average number of ordinary shares in issue during the period.

The Group has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal basic earnings per share.

	2006	2005
Weighted average number of ordinary shares outstanding	873,001,000	873,001,000
Net profit attributable to the equity holders of the parent entity	441,264	244,273
Earnings per share attributable to the equity holders of the parent entity:		
Basic and diluted (in US dollars)	**0.51**	**0.28**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

13) Cash and Cash Equivalents

Cash and cash equivalents in hand and balances with banks were denominated in the following currencies:

	December 31, 2006	December 31, 2005
Russian roubles	127,823	31,872
US dollars	10,220	10,962
Euros	3,955	4,391
Romanian lei	1,343	533
Kazakhstani tenge	326	82
Polish zloty	67	–
Swiss francs	–	5
Other	1	–
Total cash and cash equivalents	**143,735**	**47,845**

A cash deposit in the amount of 2,118 has been pledged as security for borrowings at December 31, 2006.

14) Short-Term Investments

	December 31, 2006	December 31, 2005
Bank deposits	141,961	–
Issued loans	30,382	–
Deposits to secure bank loans	1,318	1,188
Promissory notes	690	424
Miscellaneous	171	47
Total short-term investments	**174,522**	**1,659**

Bank deposits in the amount of 141,961 and issued loans in the amount of 30,382 are denominated in Russian roubles. The deposits to secure bank loans in the amount of 1,318 are denominated in euros.

All amounts are in thousands of US dollars, unless specified otherwise

15) Accounts Receivable

	December 31, 2006	December 31, 2005
Trade receivables	271,789	125,154
Officers and employees	2,170	1,563
Other accounts receivable	9,491	6,791
Gross accounts receivable	**283,450**	**133,508**
Allowance for doubtful debts	(9,579)	(8,512)
Net accounts receivable	**273,871**	**124,996**

Accounts receivable amounting to 26,508 and 16,470 are denominated in US dollars at December 31, 2006 and December 31, 2005, respectively. Accounts receivable amounting to 25,695 and 26,869 are denominated in euros at December 31, 2006 and December 31, 2005, respectively.

The following summarizes the changes in the allowance for doubtful current debts:

	2006	2005
Balance at the beginning of the year	8,512	8,645
Utilized during the year	(1,262)	(1,219)
Additional increase in allowance	1,452	1,539
Currency translation adjustment	877	(453)
Balance at the end of the year	**9,579**	**8,512**

Bank borrowings are secured by accounts receivable with the carrying value of 54,218 (December 31, 2005: 717) (*Note 24*).

16) Prepayments and Input VAT

	December 31, 2006	December 31, 2005
Prepayment for services, inventories	58,555	21,739
Prepayment for rent	562	387
Deferred charges	629	1,566
Prepayment for VAT, input VAT	137,417	119,649

(Continued next page.)

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 16) PREPAYMENTS AND INPUT VAT / COUNTINUED

(Continued.)

	December 31, 2006	December 31, 2005
Prepayment for income tax	2,236	119
Prepayment for property tax	–	213
Prepayment for other tax	1,205	942
Prepayment for insurance	438	545
Miscellaneous	3	236
Total prepayments	**201,045**	**145,396**

Input VAT, representing amounts payable or paid to suppliers, is recoverable from the tax authorities via offset against VAT payable to the tax authorities on the Group's revenue or via direct cash receipts from the tax authorities. Management periodically reviews the recoverability of the balance of input value added tax and believes it is fully recoverable within one year.

17) Investments in Associates and Other Long-Term Receivables

	December 31, 2006	December 31, 2005
Prepayment for property, plant and equipment	36,764	24,018
Investments in associates	5,079	28
Advances to employees	4,032	3,002
Long-term input VAT	3,882	–
Borrowing costs relating to unused borrowing facilities	1,604	2,025
Restricted cash balances for fulfilment guarantees	3,996	1,122
Trade receivables	66	664
Other	3,667	1,271
Gross investments and other long-term receivables	**59,090**	**32,130**
Allowance for doubtful debts	–	(23)
Net investments and other long-term receivables	**59,090**	**32,107**

Cash balances of 3,996 and 1,122 have been pledged for a fulfilment guarantee at December 31, 2006 and December 31, 2005, respectively.

Non-current accounts receivables amounting to 19,393 and 7,850 are denominated in foreign currency, mainly euros, US dollars and Romanian lei, at December 31, 2006 and December 31, 2005, respectively.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 17) INVESTMENTS IN ASSOCIATES AND OTHER LONG-TERM RECEIVABLES / COUNTINUED

The following summarises the changes in the allowance for doubtful non-current debts:

	2006	2005
Balance at the beginning of the year	23	7
Additional (reversal)/increase in allowance	(24)	16
Currency translation adjustment	1	–
BALANCE AT THE END OF THE YEAR	**–**	**23**

18) INVENTORIES

	December 31, 2006	December 31, 2005
Raw materials	184,409	161,582
Work in process	149,435	96,307
Finished goods	75,264	72,754
Goods in transit	61,325	43,359
Consigned goods	769	–
Supplies	125,463	90,827
Gross inventories	**596,665**	**464,829**
Allowance for obsolescence and slow-moving	(8,113)	(5,897)
NET INVENTORIES	**588,552**	**458,932**

As of December 31, 2006, inventories carried at net realisable value were 29,341 (December 31, 2005: 41,176).

As of December 31, 2006, certain items of inventory with a carrying amount of 90,046 (December 31, 2005: 26,457) were pledged as security for borrowings (*Note 24*).

The following summarises the changes in the allowance for obsolescence and slow-moving inventories:

	2006	2005
Balance at the beginning of the year	5,897	3,776
Additional increase in allowance	1,569	2,325
Currency translation adjustments	647	(204)
Balance at the end of the year	8,113	5,897

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

19) Property, Plant and Equipment and Investment Property

The movement in property, plant and equipment for the year ended December 31, 2006 was as follows:

	Land and buildings	Machinery and equipment	Transport and motor vehicles	Furniture and fixtures	Construction in progress	TOTAL
COST						
Balance at January 1, 2006	751,801	865,837	33,694	14,501	147,457	**1,813,290**
Additions	–	2,145	99	283	369,447	**371,974**
Assets put into operation	21,520	185,277	7,340	6,389	(220,526)	**–**
Transfer to investment property	(863)	(40)	(23)	(102)	(10)	**(1,038)**
Disposals	(4,727)	(15,293)	(360)	(575)	(2,620)	**(23,575)**
Increase due to business combination (*Note 10*)	–	–	–	36	–	**36**
Currency translation adjustments	78,103	92,547	4,833	1,566	25,683	**202,732**
Balance at December 31, 2006	**845,834**	**1,130,473**	**45,583**	**22,098**	**319,431**	**2,363,419**
ACCUMULATED DEPRECIATION						
Balance at January 1, 2006	(54,229)	(196,216)	(9,207)	(5,957)	–	**(265,609)**
Depreciation charge	(21,632)	(83,219)	(3,969)	(3,337)	–	**(112,157)**
Transfer to investment property	45	16	5	42	–	**108**
Disposals	1,299	9,818	273	441	–	**11,831**
Increase due to business combination (*Note 10*)	–	–	–	(21)	–	**(21)**
Currency translation adjustments	(6,457)	(21,611)	(1,187)	(685)	–	**(29,940)**
Balance at December 31, 2006	**(80,974)**	**(291,212)**	**(14,085)**	**(9,517)**	**–**	**(395,788)**
Net book value at December 31, 2006	**764,860**	**839,261**	**31,498**	**12,581**	**319,431**	**1,967,631**
Net book value at January 1, 2006	**697,572**	**669,621**	**24,487**	**8,544**	**147,457**	**1,547,681**

Bank borrowings are secured by properties and equipment with the carrying value of 146,409 (December 31, 2005: 175,143) (*Note 24*).

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 19) PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY / COUNTINUED

The movement in property, plant and equipment for the year ended December 31, 2005 was as follows:

	Land and buildings	Machinery and equipment	Transport and motor vehicles	Furniture and fixtures	Construction in progress	TOTAL
COST						
Balance at January 1, 2005	772,084	876,729	28,088	12,387	73,973	**1,763,261**
Additions	1,571	291	233	121	137,011	**139,227**
Assets put into operation	16,085	29,230	7,201	3,688	(56,204)	–
Transfer to investment property	(1,979)	(102)	–	(308)	–	**(2,389)**
Disposals	(6,934)	(7,181)	(334)	(868)	(1,722)	**(17,039)**
Currency translation adjustments	(29,026)	(33,130)	(1,494)	(519)	(5,601)	**(69,770)**
Balance at December 31, 2005	**751,801**	**865,837**	**33,694**	**14,501**	**147,457**	**1,813,290**
ACCUMULATED DEPRECIATION						
Balance at January 1, 2005	(34,483)	(128,233)	(5,914)	(4,067)	–	**(172,697)**
Depreciation charge	(22,413)	(76,562)	(3,771)	(2,867)	–	**(105,613)**
Transfer to investment property	220	11	–	59	–	**290**
Disposals	672	2,467	158	721	–	**4,018**
Currency translation adjustments	1,775	6,101	320	197	–	**8,393**
Balance at December 31, 2005	**(54,229)**	**(196,216)**	**(9,207)**	**(5,957)**	**–**	**(265,609)**
NET BOOK VALUE AT DECEMBER 31, 2005	**697,572**	**669,621**	**24,487**	**8,544**	**147,457**	**1,547,681**
NET BOOK VALUE AT JANUARY 1, 2005	**737,601**	**748,496**	**22,174**	**8,320**	**73,973**	**1,590,564**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 19) PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY / COUNTINUED

The movement in investment property for the year ended December 31, 2006 was as follows:

COST	
Balance at January 1, 2006	2,424
Transfer from property, plant and equipment	1,038
Additions	6
Disposals	(2)
Currency translation adjustments	277
Balance at December 31, 2006	**3,743**
ACCUMULATED DEPRECIATION	
Balance at January 1, 2006	(420)
Transfer from property, plant and equipment	(108)
Depreciation charge	(291)
Disposals	2
Currency translation adjustments	(55)
Balance at December 31, 2006	**(872)**
NET BOOK VALUE AT DECEMBER 31, 2006	**2,871**
NET BOOK VALUE AT JANUARY 1, 2006	**2,004**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 19) PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY / COUNTINUED

The movement in investment property for the year ended December 31, 2005 was as follows:

COST	
Balance at January 1, 2005	–
Transfer from property, plant and equipment	2,389
Additions	78
Disposals	(1)
Currency translation adjustments	(42)
Balance at December 31, 2005	**2,424**
ACCUMULATED DEPRECIATION	
Balance at January 1, 2005	–
Transfer from property, plant and equipment	(290)
Depreciation charge	(138)
Currency translation adjustments	8
Balance at December 31, 2005	**(420)**
NET BOOK VALUE AT DECEMBER 31, 2005	2,004
NET BOOK VALUE AT JANUARY 1, 2005	–

The fair value of investment property approximates its carrying amount.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

20) Goodwill and Other Intangible Assets

	Patents and trademarks	Goodwill	Information system projects (software SAP R\3)	Other	TOTAL
COST					
Balance at January 1, 2006	338	37,180	11,210	2,661	**51,389**
Additions	25	–	1,726	2,376	**4,127**
Assets put into operation	–	–	245	(245)	–
Disposals	(2)	–	–	(504)	**(506)**
Increase due to business combination (*Note 10*)	–	6,166	–	–	**6,166**
Currency translation adjustments	42	3,598	1,122	401	**5,163**
Balance at December 31, 2006	**403**	**46,944**	**14,303**	**4,689**	**66,339**
ACCUMULATED AMORTISATION					
Balance at January 1, 2006	(88)	–	(381)	(905)	**(1,374)**
Amortisation charge	(30)	–	(1,758)	(564)	**(2,352)**
Disposals	1	–	–	282	**283**
Currency translation adjustments	(13)	–	(85)	(176)	**(274)**
Balance at December 31, 2006	**(130)**	**–**	**(2,224)**	**(1,363)**	**(3,717)**
Net book value at December 31, 2006	**273**	**46,944**	**12,079**	**3,326**	**62,622**
Net book value at January 1, 2006	**250**	**37,180**	**10,829**	**1,756**	**50,015**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 20) GOODWILL AND OTHER INTANGIBLE ASSETS / COUNTINUED

	Patents and trademarks	Goodwill	Information system projects (software SAP R3)	Other	Total
COST					
Balance at January 1, 2005	327	38,565	8,422	3,104	**50,418**
Additions	25	–	3,160	974	**4,159**
Disposals	–	–	(16)	(1,291)	**(1,307)**
Currency translation adjustments	(14)	(1,385)	(356)	(126)	**(1,881)**
Balance at December 31, 2005	**338**	**37,180**	**11,210**	**2,661**	**51,389**
ACCUMULATED AMORTISATION					
Balance at January 1, 2005	(66)	–	–	(551)	**(617)**
Amortisation charge	(26)	–	(387)	(421)	**(834)**
Disposals	–	–	–	17	**17**
Currency translation adjustments	4	–	6	50	**60**
Balance at December 31, 2005	**(88)**	**–**	**(381)**	**(905)**	**(1,374)**
NET BOOK VALUE AT DECEMBER 31, 2005	**250**	**37,180**	**10,829**	**1,756**	**50,015**
NET BOOK VALUE AT JANUARY 1, 2005	**261**	**38,565**	**8,422**	**2,553**	**49,801**

21) ACCOUNTS PAYABLE AND ADVANCES FROM CUSTOMERS

	December 31, 2006	December 31, 2005
Trade and other payables	178,639	122,910
Advances from customers	101,845	56,412
Accounts payable for property, plant and equipment	66,722	14,871
Issued notes to third parties	342	–
Other	1,589	2,626
TOTAL ACCOUNTS PAYABLE	**349,137**	**196,819**

Trade payables amounting to 134,993 and 69,538 are denominated in foreign currency, mainly US dollars, euros and Romanian lei, at December 31, 2006 and December 31, 2005, respectively.

All amounts are in thousands of US dollars, unless specified otherwise

22) Accrued Liabilities and Provisions

	December 31, 2006	December 31, 2005
Payroll liabilities	27,371	19,945
Accrued and withheld taxes on payroll	10,791	7,312
Liabilities for VAT	8,895	18,187
Liabilities for income tax	17,976	12,154
Liabilities for property tax	2,401	989
Liabilities for other taxes	2,306	745
Deferred VAT	437	37,810
Liabilities for unused annual leave, current portion	2,365	1,322
Current portion of non-current liability	716	–
Accrual for tax fines	659	607
Accrual for long-service benefit	4,451	3,318
Environmental provision	–	2,614
Liabilities under put options in a subsidiary (*Note 30 viii*)	21,387	–
Miscellaneous	3,729	3,687
Total accrued liabilities	**103,484**	**108,690**

Deferred value added tax is only payable to the tax authorities when the underlying receivable is recovered or written off. The rules apply to transactions arranged prior to December 31, 2005.

23) Finance Lease Liabilities

Starting from 2001, the Group entered into lease agreements under which they have a bargain option to acquire the leased assets at the end of lease term ranging from 2 to 7 years. The estimated average remaining useful life of leased assets varies from 6 to 30 years.

The leases were accounted for as finance leases in the consolidated financial statements. The carrying value of the leased assets was as follows as at December 31:

	2006	2005
Machinery and equipment	–	8,325
Transport and motor vehicles	657	287
	657	**8,612**

All amounts are in thousands of US dollars, unless specified otherwise

The leased assets are included in property, plant and equipment in the consolidated balance sheet (*Note 19*).

Future minimum lease payments were as follows at December 31, 2006:

	Principal	Interest	TOTAL
2007	187	18	205
2008–2009	244	5	249
	431	**23**	**454**

In the years ended December 31, 2006 and December 31, 2005, the average interest rates under the finance lease liabilities were 6% and 13%, respectively.

The finance lease liabilities were denominated in the following currencies at December 31:

	2006	2005
US dollars	23	1,246
Romanian lei	408	188
	431	**1,434**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ COUNTINUED

24) Borrowings

Short-term and long-term borrowings were as follows as of December 31:

	2006	2005
Current:		
Russian banks	80,524	198,097
International banks	100,011	118,969
Raiffeisen Leasing liability	592	576
Interest payable	16,431	5,166
Current portion of non-current borrowings	168,453	103,100
Unamortised debt issue costs	(1,470)	(362)
	364,541	**425,546**
Non-current:		
Russian banks	198,481	83,630
International banks	51,728	12,171
Bearer coupon debt securities	587,236	173,718
Raiffeisen Leasing liability	151	785
Unamortised debt issue costs	(8,118)	(2,280)
Less: current portion of non-current borrowings	(168,453)	(103,100)
	661,025	**164,924**

Some of the loan agreements provide for certain covenants in respect of the Company and its subsidiaries. The covenants impose restrictions in respect of certain transactions and financial ratios, including restrictions in respect of indebtedness, profitability and guarantees issued to other parties. The Group pledged its rights under some contracts in Russia as collateral under loan agreements for 15,600. Proceeds from sales pursuant to these contracts can be used to satisfy the obligations under the loan agreements in the event of a default.

Loans for 268,062 as of December 31, 2006 and 77,203 as of December 31, 2005, inclusive of short-term borrowings, were guaranteed by collateral of property, plant and equipment, inventories, deposits, accounts receivable (*Notes 13, 15, 18, 19*) and, as of December 31, 2005, by shares of a subsidiary of the Group representing net assets with the carrying amount of 39,213.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 24) BORROWINGS / COUNTINUED

Long-term debt is repayable as follows:

	December 31, 2006	December 31, 2005
1 to 2 years	302,322	45,920
2 to 3 years	338,382	10,758
3 to 4 years	11,656	105,169
Over 4 years	16,783	5,357
Unamortised debt issue costs	(8,118)	(2,280)
	661,025	**164,924**

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	Interest rates	December 31, 2006	December 31, 2005
Russian rouble	6–10.09%	434,917	327,550
US dollar	6,77–20.94%		
	Libor 1M + 3.75%	471,851	211,279
Euro	4.038–9.043%		
	Euribor 3M + 2.75%		
	Euribor 6M + 3.5%		
	Euribor 6M + 5%		
	5.6–8.75%	118,798	42,055
Romanian lei	Bubor 1M + 4% (*)	–	9,586
		1,025,566	**590,470**

(*) *Bubor is the Bucharest bid offer rate.*

Bank Loans

In April 2006, the Group repaid early its liabilities under long-term loans to Moscow Narodny Bank in the amount of 47,143. These liabilities were included in non-current borrowings in the amount of 27,788 (net of current portion) in the consolidated balance sheet as of December 31, 2005. The full amount was financed by short-term borrowings.

On August 25, 2005, the Group entered into a 25,000 facility agreement with Moscow Narodny Bank with a maturity date of September 30, 2007. This liability was included in non-current borrowings in the amount of 11,497 (net of current portion) in the consolidated balance sheet as of December 31, 2005. The facility was repaid on August 31, 2006.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 24) BORROWINGS / COUNTINUED

In connection with the funding of the TMK Steel Loan (*Note 28*), the Group incurred the following debt:

On September 29, 2006, the Group entered into a facility agreement with Dresdner Bank that provided for a bridge loan facility in the principal amount of 160,000, with a term of 364 days from the date of signing. The facility was repaid on November 8, 2006.

On September 25, 2006, the Group entered into a syndicated facility agreement with Bank Natexis, as arranger, in an aggregate principal amount of up to 155,000. The facility has a term of 30 months from the date of the first drawdown, which occurred on September 26, 2006. The maturity date of the facility may be extended in certain circumstances at the election of the Group. As of December 31, 2006, the Group has drawn the equivalent of 155,000 under this facility.

On October 2, 2006, the Group entered into a medium term facility with Moscow Narodny Bank and Commerzbank in the principal amount of 140,000. The term of the facility was 24 months. The facility was fully drawn. The facility was repaid on November 10, 2006.

Loan Participation Notes

On September 29, 2006, the Group issued 3,000 8.5% loan participation notes with a nominal value of USD 100,000 each, due September 2009. The notes were issued by TMK Capital SA, a Luxemburg special purpose vehicle, for the sole purpose of funding a loan to the Company. The notes have been admitted to trading on the London Stock Exchange. The terms of the notes provide for certain restrictions on the Company's ability to incur liens, to engage in assets sales, to engage in transactions with affiliates and to engage in mergers and similar transactions.

Bearer Coupon Debt Securities

On October 21, 2003, the Group issued 2,000,000 bonds with a nominal value of 1,000 roubles (USD 33.31 at the exchange rate as of the date of issuance) each. The bonds mature on October 21, 2006. The interest rate for the first, second and third semi-annual coupons is 14% per annum. The interest rate for the fourth, fifth and sixth semi-annual coupons will be established and announced by the Company within 14 days before the third coupon due date. Early redemption of bonds was made available within 14 days of the third coupon period, from the 534th to the 547th days from the date of issuance. None of the bondholders used their right to recall their bonds. On October 20, 2006, the Group repaid its liabilities under the debt securities.

On March 29, 2005, the Group issued 3,000,000 bonds with a nominal value of 1,000 roubles (USD 35.95 at the exchange rate as of the date of issuance) each. The bonds mature on March 24, 2009. The interest rate for the first and second semi-annual coupons is 11.09% per annum. The interest rate for the third and fourth semi-annual coupons is 10.09% per annum. The interest rate for the fifth, sixth, seventh and eighth semi-annual coupons will be established and announced by the Company within

5 days before the fourth coupon due date. Early redemption of bonds was available within 5 days of the fourth coupon period, from the 724th to the 728th days from the date of issuance. In December 2006, the Company bought out early the bonds from bondholders for the total amount of 16,587.

On February 21, 2006, the Group issued 5,000,000 bonds with a nominal value of 1,000 roubles (USD 35.53 at the exchange rate of the date of issuance) each, with ten coupon periods of

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 24) BORROWINGS / COUNTINUED

182 days each. The maturity date is February 15, 2011. The interest rate for the first, second, third and forth semi-annual coupons is 7.95% per annum. The interest rate for the fifth, sixth, seventh, eighth, ninth and tenth semi-annual coupons will be established and announced by the Company within 15 days before the fourth coupon due date. Early redemption of bonds is available within 15 days of the fourth coupon period, from the 714th to 728th days from the date of issuance.

Unamortised Debt Issue Costs

Unamortised debt issue costs represent agent commission and arrangement costs paid by the Group in relation to the arrangement of loans and issue of notes.

Liability to Raiffeisen Leasing

The liability to Raiffeisen Leasing relates to a lease contract between the Group and Raiffeisen Leasing. The contract was a part of a sale-leaseback transaction. Under the contract, the Group sold certain items of equipment to Raiffeisen Leasing and immediately leased them back. The substance of the transaction represented a borrowing by the Group from Raiffeisen Leasing and has been accounted for as such in the consolidated financial statements.

Unutilised Borrowing Facilities

As of December 31, 2006, the Group had unutilised borrowing facilities in the amount of 310,323 (December 31, 2005: 151,749).

25) Post-Employment Benefits

The Group's companies provide additional pensions and other post-employment benefits to their employees in accordance with collective bargaining agreements. Defined benefits consist of lump-sum amounts payable at the retirement date and certain regular post-retirement payments. These benefits generally depend on years of service, level of compensation and amount of pension payment under the collective bargaining agreement. The Group pays the benefits when they fall due for payment.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 25) POST-EMPLOYMENT BENEFITS / COUNTINUED

The components of net benefit expense recognised in the consolidated income statement for the years ended December 31, 2006 and 2005 and amounts recognised in consolidated balance sheets as of December 31, 2006 and 2005 were as follows:

	2006	2005
Movement in the benefit liability:		
At January 1	(18,009)	(11,649)
Benefit expense	(1,957)	(7,429)
Benefit paid	755	518
Less: current portion of non-current post-employment liability	706	–
Currency translation adjustment	(1,838)	551
At December 31	**(20,343)**	**(18,009)**
Net benefit expense (recognised in cost of sales):		
Current service cost	1,318	1,164
Past service cost	190	–
Net actuarial (gain) loss recognised in the period	(1,033)	5,352
Interest cost on benefit obligation	1,482	913
Net benefit expense	**1,957**	**7,429**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 25) POST-EMPLOYMENT BENEFITS / COUNTINUED

The following table summarises the components of net benefit expense recognised in the consolidated income statement and amounts recognised in consolidated balance sheets by country:

	Russia		Romania	
	2006	2005	2006	2005
Movement in the benefit liability:				
At January 1	(17,396)	(11,088)	(613)	(561)
Benefit expense	(1,378)	(7,295)	(579)	(134)
Benefit paid	694	471	61	48
Less: current portion of non-current liability	706	–	–	–
Currency translation adjustment	(1,651)	516	(187)	34
At December 31	**(19,025)**	**(17,396)**	**(1,318)**	**(613)**
Net benefit expense (recognised in cost of sales):				
Current service cost	1,017	1,090	301	73
Past service cost	190	–	–	–
Interest cost on benefit obligation	1,416	843	66	71
Net actuarial (gain) loss recognised in the period	(1,245)	5,362	212	(10)
Net benefit expense	**1,378**	**7,295**	**579**	**134**

The principal actuarial assumptions used in determining pension obligations for the Group's plan are shown below:

	Russia		Romania	
	2006	2005	2006	2005
Discount rate	7.8%	7.8%	decreasing from 7.49 to 3.53% in the long term	decreasing from 12.14 to 3.53% in the long term
Average long-term rate of compensation increase	6.3%	6.3%	decreasing from 6.0 to 2.0% in the long term	decreasing from 8.6% to 2.0% in the long term

The Group had no plan assets and unrecognised actuarial gains or losses in the year ended December 31, 2006.

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ COUNTINUED

26) Other Non-Current Liabilities

	December 31, 2006	December 31, 2005
Unused annual leave	12,835	7,022
Other long-term liabilities	5,297	321
Balance at the end of year	**18,132**	**7,343**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

27) Principal Subsidiaries

Company	Location	Main activity	Actual ownership interest December 31, 2006	Effective ownership interest December 31, 2006	Actual ownership interest December 31, 2005	Effective ownership interest December 31, 2005
OAO "Sinarsky Pipe Plant"	Russia	Manufacturing of seamless steel pipes, sale of electric and heating power and other services	92.43%	92.43%	91.12%	91.12%
OAO "Seversky Pipe Plant"	Russia	Manufacturing of seamless steel pipes, welded steel pipes, sale of electric and heating power and other services	92.97%	92.97%	91.60%	91.60%
OAO "Volzhsky Pipe Plant"	Russia	Manufacturing of seamless steel pipes, welded steel pipes and other products	100.00%	100.00%	100.00%	100.00%
OAO "Taganrog Metallurgical Plant"	Russia	Manufacturing of seamless steel pipes, welded steel pipes, sale of steel ingots and other products	95.74%	95.74%	95.32%	95.32%
ZAO "Trade House TMK"	Russia	Sale of steel pipes	100.00%	99.92%	100.00%	99.91%
OOO "Skladskoy Kompleks TMK"	Russia	Sale of steel pipes	100.00%	100.00%	100.00%	100.00%
TOO "TMK-Kazakhstan"	Kazakhstan	Sale of steel pipes	100.00%	100.00%	100.00%	100.00%
OOO "TMK-Trans"	Russia	Transportation services	100.00%	100.00%	100.00%	100.00%
OOO "Blagoustroystvo"	Russia	Services	100.00%	99.99%	100.00%	100.00%
OOO "Sinarsky Trubnik"	Russia	Services	100.00%	100.00%	100.00%	100.00%
OOO "SinaraTransAvto"	Russia	Services	100.00%	100.00%	100.00%	100.00%
OOO "Sinaraproekt"	Russia	Services	100.00%	100.00%	100.00%	100.00%
TMK Global AG	Switzerland	Sale of steel pipes	100.00%	100.00%	100.00%	100.00%
TMK Sinara North America Inc.	USA	Sale of steel pipes	100.00%	100.00%	100.00%	100.00%
Eurosinara S.r.L.	Italy	Sale of steel pipes	100.00%	100.00%	–	–
TMK Middle East	UAE	Sale of steel pipes	100.00%	100.00%	–	–
Pokrovka 40	Russia	Assets holding	100.00%	100.00%	–	–
TMK Sinara Handel GmbH	Germany	Sale of pipes, raw materials and equipment	100.00%	100.00%	100.00%	100.00%
SC TMK-ARTROM SA	Romania	Manufacturing of seamless steel pipes	80.56%	80.56%	80.56%	80.56%
SC TMK-RESITA SA	Romania	Manufacturing of billets and other pipe-related goods	99.49%	99.49%	99.49%	99.49%
TMK Eastern Europe	Romania	Sale of pipes and other goods	95.00%	95.00%	95.00%	95.00%
WRJ INWESTYCJE SP Z O.O.	Poland	Investment company	80.00%	80.00%	–	–
TMK Capital SA	Luxembourg	Finance raising	0.00%	0.00%	–	–

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS / COUNTINUED

28) Related Parties Disclosures

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

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

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions or had significant balances outstanding at December 31, 2006 and 2005 is detailed below.

In the year ended December 31, 2006, transactions with related parties constituted approximately 1% of the total volume of the Group's sales of goods (2005: 3%).

Interest rates on borrowings from related parties in 2006 were from 4% to 15% (2005: from 7% to 14%).

The following table provides outstanding balances with related parties at the year-end:

	December 31, 2006	December 31, 2005
Cash		
Entities under common control with the Group	50,567	12,489
Entities under control of the minority shareholders of the Company	–	5
	50,567	**12,494**
Accounts receivable – current		
Entities under common control with the Group	12,173	28,284
Entities under control of the minority shareholders of the Company	–	123
	12,173	**28,407**
Prepayments – current		
Entities under common control with the Group	1,027	–
Entities under control of the minority shareholders of the Company	–	18
	1,027	**18**
Accounts receivable – non-current		
Entities under common control with the Group	**46,339**	**8,486**
Accounts payable – current		
Entities under common control with the Group	**6,702**	**478**
Borrowings from related parties		
Entities under control of the minority shareholders of the Company	**–**	**31,394**

All amounts are in thousands of US dollars, unless specified otherwise

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 28) RELATED PARTIES DISCLOSURES / COUNTINUED

Accounts receivable from related parties amounting to 45,564 and 23,922 are denominated in foreign currency, mainly US dollars and euros, at December 31, 2006 and December 31, 2005, respectively.

The following table provides the total amount of transactions with related parties for the years ended December 31:

	2006	2005
Sales revenue		
Entities under common control with the Group	34,333	82,521
Purchases of goods and services		
Entities under common control with the Group	42,141	32,059
Entities under control of the minority shareholders of the Company	52	1,318
	42,193	33,377
Interest expenses from loans and borrowings		
Entities under common control with the Group	–	911
Entities under control of the minority shareholders of the Company	760	1,472
	760	2,383
Interest income from loans and borrowings		
Entities under common control with the Group	2,147	1,135

On October 1, 2006, as a result of the acquisition by TMK Steel Limited of all ordinary shares held by Dalecone Limited, MDM-Bank ceased to be a related party with the Company.

On October 6, 2006, the Group granted loans to TMK Steel Limited in the aggregate principal amount of 780,000 for the term of up to five years. The loans bore interest of 8.51% per annum and were unsecured. In November 2006, TMK Steel Limited repaid the loans to the Group together with accrued interest of 5,473.

Non-current accounts receivable from related parties include advances paid for the purchase of 75% ownership interest in Orsky Machine Building Plant in the amount of 45,512 as of December 31, 2006.

Non-current accounts receivable from related parties also include a long-term portion of receivables for securities sold in the amount of 4,986 as of December 31, 2005. The nominal value of the current portion of the receivables for securities sold was 6,304 as of December 31, 2006 and 2,779 as of December 31, 2005.

Compensation of Key Management Personnel of the Group

Key management personnel comprise members of the Board of Directors, the Management Board and certain executives of the Group, totalling 33 persons as at December 31, 2006 (2005: 31). Total compensation to key management personnel included as part of the general and administrative expenses in the income statement amounted to 14,620 for the year ended December 31, 2006 (2005: 7,782), including 1,278 in respect of shares sold by TMK Steel Limited (*Note 30 vii*).

Compensation to key management personnel consists of contractual salary, performance bonus depending on operating results and payments for medical insurance.

29) Contingencies, Commitments and Operating Risks

Operating Environment of the Group

The Group's principal assets are located in the Russian Federation, therefore, its significant operating risks are related to the activities of the Group in this country.

Whilst there have been improvements in the Russian economic situation, such as an increase in gross domestic product and a reduced rate of inflation, Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

Taxation

The major part of the Group tax expense relates to taxation in the Russian Federation.

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome.

Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Management believes that it has paid or accrued all taxes that are applicable. Where uncertainty exists, the Group has accrued tax liabilities based on management's best estimate of the probable outflow of resources embodying economic benefits, which will be required to settle these liabilities.

Contractual Commitments and Guarantees

As of December 31, 2006, the Group had contractual commitments for the acquisition of property, plant and equipment from third parties for 1,844,993 thousand roubles (70,069 thousand US dollars), 192,897 thousand euros (254,181 thousand US dollars), 10,087 thousand US dollars and 8,828 thousand Romanian lei (3,435 thousand US dollars) for the total amount 337,772 (all amounts of contractual commitments are expressed net of VAT). The Group had paid advances of 32,299 with respect to such commitments.

Under contractual commitments disclosed above, the Group opened unsecured letters of credit in the amount of 47,301 (2005: 57,505).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
/ 29) CONTINGENCIES, COMMITMENTS AND OPERATING RISKS / COUNTINUED

Insurance Policies

The Group maintains obligatory insurance policies required by the Russian Law and insurance policies in respect of certain assets pledged under loan agreements. The Group holds no insurance policies in relation to its major production facilities, or in respect of public liability.

Legal Claim

During the period, the Company was involved in a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Company and which have not been accrued or disclosed in these consolidated financial statements.

Guarantees of Debts of Others

The Group had guarantees of debts of others outstanding at December 31, 2006 in the amount of 4,562 with maturity in 2007.

30) Equity

I) *Share Capital*

As of December 31, 2006, the authorised number of ordinary shares of the Company was 873,001,000 (2005: 873,001,000) with a nominal value per share of 10 roubles. All these shares are issued and fully paid.

II) *Reserve Capital*

According to Russian Law, the Company must create a reserve capital in the amount of 5% of the share capital per the Russian statutory accounts by annual appropriations that should be at least 5% of the annual net profit per the statutory financial statements. The reserve capital can be used only for covering losses and for the redemption of the Company's bonds and purchase of its own shares if there are no other sources of financing.

III) *Dividends*

In July 2006, the Company paid dividends in respect of 2005 in the amount of 17,101 or 0.542 roubles per share. In May 2005, the Company paid interim dividends in respect of 2005 in the amount of 2,592 or 0.084 roubles per share.

In accordance with Russian legislation, dividends may only be declared to the shareholders from accumulated undistributed and unreserved earnings as shown in the Company's Russian statutory financial statements. The Company had 457,583 and 327,139 of undistributed and unreserved earnings as of December 31, 2006 and 2005, respectively. In addition, the Group's share in the undistributed and unreserved earnings of its subsidiaries was 889,177 and 381,749 as of December 31, 2006 and 2005, respectively.

IV) *Transfers of Ownership Interests in Subsidiaries and Distributions to Owners*

In December 2004, the Group signed an agreement with an entity under common control with the Group for the purchase of 100% ownership interest in Sinara Trading AG, an entity registered in Switzerland, for the consideration of 8,787 thousand Swiss francs (7,753 at the exchange rate as of December 31, 2004). The title transferred to the Group and control over Sinara Trading was obtained by the Group on May 25, 2005. An amount of 7,717 was paid by the Group prior to December 31, 2004. The Group additionally paid an amount of 472 in 2005. These payments were recorded as a reduction in accumulated profits in the consolidated financial statements.

In June 2005, the Group signed an agreement with an entity under common control with the Group for the purchase of 100% ownership interest in Sinara Handel GmbH, an entity registered in Germany, for the consideration of 40,000. The title to the 100% ownership interest in Sinara Handel GmbH was transferred to the Group on March 1, 2006. An amount of 20,000 was paid by the Group prior to December 31, 2005 and an amount of 20,000 was paid by the Group on March 3, 2006.

Sinara Trading paid dividends in the amount of 7,593 for 2005 in May 2005 to its former owner, before the transfer of Sinara Trading shares to the Group. Sinara Handel accrued dividends to its former owner in the amount of 1,830 for 2004 in the year ended December 31, 2005. The corresponding liability in the amount of 1,758 was included into dividends payable in the consolidated financial statements as at December 31, 2005.

V) *Acquisition of Minority Interests in Subsidiaries*

In the year ended December 31, 2006, the Company purchased 1.31% of OAO "Sinarsky Pipe Plant" shares, 1.37% of OAO "Seversky Pipe Plant" shares and 0.42% of OAO "Taganrog Metallurgical Plant" shares. The total amount paid for the shares was 21,423.

In the year ended December 31, 2005, the Company purchased 2.43% of OAO "Sinarsky Pipe Plant" shares, 0.48% of OAO "Seversky Pipe Plant" shares and 0.73% of OAO "Taganrog Metallurgical Plant" shares. The total amount paid for the shares was 8,487.

VI) *Dividends by Subsidiaries of the Group to the Minority Owners in Subsidiaries*

Dividends declared by subsidiaries of the Group to the minority owners in subsidiaries were recorded as a reduction in minority interests of 476 and 1,192 in the consolidated financial statements for the years ended December 31, 2006 and 2005, respectively.

VII) *Excess of the Fair Value of Ordinary Shares Sold to the Group's Employees over the Offer Price of Ordinary Shares*

TMK Steel Limited sold 2,650,000 ordinary shares, amounting to approximately 0.3% of the issued and outstanding ordinary shares, to the Group's employees at a price of RUB 123 (approximately USD 4.67 as of December 31, 2006) per ordinary share in the employee offering.

The excess of the fair value of ordinary shares sold to the Group's employees over the offer price of ordinary shares in the total amount of 2,142 is recorded as an increase in additional paid-in capital and as salaries and wages in general and administrative expenses in the consolidated financial statements for the year ended December 31, 2006.

VIII) *De-recognition of Minority Interests in a Subsidiary*

In 2006, new regulations were introduced in the Russian Federation in respect of joint-stock companies in which a controlling shareholder owns not less than 95% of the share capital as of July 1, 2006. These amendments oblige a controlling shareholder to acquire the company's shares in the case when the minority shareholders are willing to sell their stakes. On the other hand, a controlling shareholder can initiate a forced disposal of the shares held by minority shareholders.

At July 1, 2006, the Group had a 95.74% ownership interest in OAO "Taganrog Metallurgical Plant". At this date, the Group derecognised minority interests of 14,443 and accrued a liability to minority shareholders in the amount of 27,106. The liability was measured based on the highest price for the shares during the period of six months up to the date of its recognition as required by the regulations. The excess of the amount of the liability over the carrying value of the derecognised minority interests amounting to 12,663 was charged to accumulated profits.

31) Financial Risk Management

The Group's principal financial instruments comprise bank loans and overdrafts, bonds issued, finance leases, loans given, and cash and cash equivalents. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial assets and liabilities such as trade receivables and trade payables, which arise directly from its operations. During the year the Group did not undertake trading in financial instruments.

Credit Risk

Financial assets, which potentially subject Group entities to credit risk, consist principally of trade receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. The carrying amount of accounts receivable, net of allowance for impairment of receivables, represents the maximum amount exposed to credit risk.

The Group has no significant concentrations of credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance already recorded.

The Group maintains its available cash in Russian affiliates of international banks and major Russian banks. Management periodically reviews the creditworthiness of the banks in which it deposits cash.

Foreign Exchange Risk

The Group exports production and attracts substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated assets (*Notes 13, 14, 15, 16, 17*) and liabilities (*Notes 21, 23, 24*) give rise to foreign exchange exposure.

The Group does not have formal arrangements to mitigate foreign exchange risks of the Group's operations. However, management believes that the Group is secured from foreign exchange risks as foreign currency denominated sales are used to cover repayment of foreign currency denominated borrowings.

Interest Rate Risk

The Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group is exposed to interest rate risk through market value fluctuations of interest bearing long-term borrowings.

Interest rates on long-term borrowings are fixed, except for 176,394 of variable-rate debt. Interest rates are disclosed in *Note 24*.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 31) FINANCIAL RISK MANAGEMENT / COUNTINUED

Fair Value of Financial Instruments

The carrying amounts of financial instruments, consisting of cash, short-term and long-term investments, short-term accounts receivable and payable, long-term accounts receivable, short-term and long-term loans payable, approximate their fair value.

The fair value of the bonds issued by the Group in March 2005 with a nominal amount of 2,563,241 thousand Russian roubles (97,346) is equal to 2,583,747 thousand Russian roubles (98,125) as of December 31, 2006.

The fair value of the bonds issued by the Group in February 2006 with a nominal amount of 5,000,000 thousand Russian roubles (189,890) is equal to 5,020,500 thousand Russian roubles (190,668) as of December 31, 2006.

The fair value of the bonds issued by the Group in September 2006 with a nominal amount of 300,000 is equal to 310,620 as of December 31, 2006.

The fair value of the bonds was determined based on market quotations.

32) Events after the Balance Sheet Date

On February 20, 2007, Sinara Handel GmbH was re-registered as TMK Sinara Handel GmbH.

On August 25, 2006, the Group signed an agreement on the purchase of 75% ownership interest in open joint-stock company "Orsky Machine Building Plant" for 45,512 from an entity under common control with the Group. Title transferred to the Group and control over Orsky Machine Building Plant was obtained by the Group on January 31, 2007. On February 1, 2007, a management agreement was signed under which the Company took over the authority of the sole executive body of Orsky Machine Building Plant. Prepayment for 75% ownership interest in the amount of 45,512 was made on November 9, 2006 and is included in long-term receivables from related parties in the consolidated financial statements (*Note 28*).

On March 5, 2007, the Company purchased 76.33% ownership interest of joint-stock company "Russian Research Institute of the Tube and Pipe Industries" (RosNITI) for 3,067. RosNITI is a scientific research institution engaged in the scientific and technological development of the Russian pipe industry.

In addition to the information disclosed in respect of these acquisitions, IFRS 3 "Business Combinations" requires the Group to disclose the amounts to be recognised at the acquisition date for each class of the acquirees' assets, liabilities and contingent liabilities. It is impracticable for the Group to disclose this information because the acquired subsidiaries have not completed purchase price allocation in accordance with IFRS 3 "Business Combinations".

In January 2007, the Company purchased additional 0.1% of OAO "Seversky Pipe Plant" shares for 19,990 thousand Russian roubles (759 at the exchange rate at December 31, 2006). The Company's interest in the subsidiary increased to 93.07%.

On February 20, 2007, the Company paid interest in the amount of 7,024 (198,200 thousand roubles at the exchange rate as of the date of payment) for the second semi-annual coupon of 5,000,000 bonds issued on February 21, 2006.

On March 27, 2007, the Company paid interest in the amount of 5,246 (136,805 thousand roubles at the exchange rate as of the date of payment) for the fourth semi-annual coupon of 3,000,000 bonds issued on March 29, 2005.

In March 2007, the Group repaid early its liabilities under long-term loans to Gazprombank in the amount of 4,286 thousand euros (5,648 at the exchange rate at December 31, 2006). These

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

/ 32) EVENTS AFTER THE BALANCE SHEET DTE / COUNTINUED

liabilities were included in non-current borrowings in the consolidated balance sheet as of December 31, 2006.

In November 2006, the Group entered into a long-term pre-export finance facility with VTB Bank Europe Plc. in the principal amount of 30,000 with a maturity in 2007–2010. On January 18, 2007, the facility was fully drawn.

In March 2007, the Group entered into a loan agreement with Banca Comersiala Romana in the principal amount of 19.7 million euros (25,959 at the exchange rate at December 31, 2006) with a maturity in January 2008.

Share Options Programme

On March 2, 2007, the Group adopted a share options programme (the Programme). Under the Programme, the members of the Board of Directors, senior executives and certain employees (the Participants) are granted options to acquire shares in the Company. The Programme provides for the grants of options to acquire up to 9,603,011 shares, representing 1.1% of the Company's shares outstanding as of December 31, 2006. All the options were granted to the Participants in March 2007. The options will be exercisable in three phases in June 2007, June 2008 and June 2009, representing 25%, 35% and 40%, respectively, of the total amount of shares subject to the Programme.

The exercise price for options under the first phase was fixed at USD 8.25 per share. The exercise price for options under the second and third phases will be determined based on the average market price of the shares for the periods from March 2007 to June 2007 and from June 2007 to June 2008, respectively.

The fair value of options granted to be recognised as an expense over the vesting period is 12,683.

In February and March 2007, the Group purchased 491,980 shares of the Company for the total amount of 4,914 (at the exchange rate as of the date of transactions), including 463,180 shares purchased from an entity under common control with the Group for 3,977, for the purpose of realisation of the Programme.

11 Contacts

Corporate information

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WebSite

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Russian version:	http://www.tmk-group.ru

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12(1) Appendices

THE METHOD OF CALCULATING THE KEY FINANCIAL INDICATORS

EBITDA IS A MEASURE OF TMK'S OPERATING PERFORMANCE THAT IS NOT REQUIRED BY, or presented in accordance with IFRS. EBITDA represents profit before interest (financing cost and financing income), taxes, depreciation and amortisation. EBITDA is not a measurement of TMK's operating performance under IFRS and should not be considered as an alternative to gross profit, net profit or any other performance measures derived in accordance with IFRS or as an alternative to cash flow from operating activities or as a measure of liquidity. In particular, EBITDA should not be considered as a measure of discretionary cash available to TMK for investment in the growth of the business.

EBITDA has limitations as an analytical tool and potential investors should not consider it in isolation or as a substitute for analysis of operating results as reported under IFRS. Some of these limitations include:

EBITDA does not reflect the impact of financing or financing costs on operating performance which can be significant and could further increase if TMK was to incur more debt.

EBITDA does not reflect the impact of income taxes on operating performance.

EBITDA does not reflect the impact of depreciation and amortisation on operating performance. The assets of TMK's businesses which are being depreciated and/or amortised will have to be replaced in the future and, in the absence of inflation, such depreciation and amortisation expense may approximate the cost to replace these assets in the future. By excluding this expense, EBITDA does not reflect future cash requirements for these replacements.

Other companies in the pipe industry may calculate EBITDA differently or may use it for purposes different from TMK limiting its usefulness as a comparative measure.

TMK compensates for these limitations by relying primarily on the IFRS operating results and only using EBITDA in a supplemental manner. Please refer to the consolidated statements of income and consolidated statements of cash flows included elsewhere in this Annual Report.

Reconciliation of EBITDA to net profit is as follows:

December 31	2006	2005	2004
Net profit	460.6	254.2	115.2
Income tax expense	157.9	95.9	13.1
Depreciation and amortisation	114.7	105.6	95.4
Finance costs	76.5	78.2	100.9
Finance income	(15.8)	(1.8)	(3.3)
EBITDA	793.9	532.1	321.3

MLN USD

NET DEBT IS A MEASURE OF TMK'S OPERATING PERFORMANCE THAT IS NOT REQUIRED BY, or presented in accordance with, IFRS. Net debt represents long-term loans and borrowings plus short-term loans and borrowings plus financing lease liabilities less cash and cash equivalents. Although net debt is a non-IFRS measure, it is widely used to assess liquidity and the adequacy of a company's financial structure. TMK believes Net Debt provides an accurate indicator of its ability to meet its financial obligations, represented by gross debt, from available cash. Net Debt allows TMK to show investors the trend in the net financial condition over the periods presented. The use of Net Debt, however, effectively assumes that gross debt can be reduced by cash. In fact, it is unlikely that all of the cash would be used to reduce gross debt all at once, as cash must also be available to pay employees, suppliers and taxes and to meet other operating needs and capital expenditure requirements. Net Debt and its ratio to equity, or leverage, are used to evaluate the financial structure in terms of sufficiency and cost of capital, level of debt, debt rating, funding cost and whether the financial structure is adequate to achieve TMK's business and financial targets. TMK's management monitors the Net Debt and leverage or similar measures as reported by other companies in Russia or abroad in order to assess TMK's liquidity and financial structure relative to such companies. TMK's management also monitors the trends in Net Debt and leverage in order to optimise the use of internally generated funds versus funds from third parties.

NET DEBT has been calculated as follows:

December 31	2006	2005	2004
Net Debt calculation			
Add:			
Short-term loans and borrowings and current portion of long-term loans and borrowings	364.5	456.9	646.1
Finance lease liabilities, current portion	0.2	1.3	3.8
Long-term loans and borrowings, net of current portion	661.0	164.9	117.1
Finance lease liabilities, net of current portion	0.3	0.1	1.2
Less:			
Cash and cash equivalents	285.7	47.8	13.5
Net Debt	**740.3**	**575.4**	**754.7**

MLN USD

WORKING CAPITAL has been calculated as follows:

		2006	2005	2004
(1) Revenue		3,384	2,938	1,984
(2) COGS (incl. depreciation)		(2,350)	(2,192)	(1,598)
(3) Accounts receivable		286	153	206
(4) Inventory		589	459	413
(5) Prepayments		202	145	171
(6) Accounts payable		356	197	249
(7) Accruals (+ deferred revenue+ customer advances)		103	109	102
(8) Accounts receivable (days)	(3/1×365)	24	22	30
(9) Inventory (days)	(4/2×365)	81	73	73
(10) Prepayments (days)	(5/2×365)	27	26	29
(11) Accounts payable (days)	(6/2×365)	43	37	46
(12) Accruals (days)	(7/2×365)	16	18	16
(13) Working Capital Turnover (days)	(9+10+11-12-13)	73	66	70

MLN USD, DAYS

ROE is equal to profit after tax divided by average balance of equity expressed as a percentage.

ROCE is calculated as profit before interest and tax divided by the difference between average balances of assets and current liabilities expressed as a percentage.

The average balance is calculated as one half of sum of the balances as of the first and the last days of the year.

12(2) Appendices

ADDITIONAL INFORMATION

A DETAILED LIST OF SUBSIDIARIES AND ASSOCIATES OF OAO "TMK" at the end of 2006 is provided on the company web-site in the section

Investor relations /Financial statements/ Non-consolidated Financial statements (RAS)

http://www.tmk-group.com/ras.php

A DETAILED LIST OF MAJOR TRANSACTIONS AND RELATED-PARTY TRANSACTIONS is provided on the company web-site in the section

Investor relations /Financial statements/ Non-consolidated Financial statements (RAS)

http://www.tmk-group.com/ras.php