AVTOVAZ GROUP

INTERNATIONAL FINANCIAL REPORTING STANDARDS
CONSOLIDATED FINANCIAL STATEMENTS
AND AUDITORS' REPORT

31 December 2006

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PRICEWATERHOUSECOOPERS

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INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Board of Directors of JSC AVTOVAZ:

1 We have audited the accompanying consolidated financial statements of JSC AVTOVAZ and its subsidiaries (the "Group") set out on pages 3 to 36 which comprise the consolidated balance sheet as at 31 December 2006 and the consolidated statement of income, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

3 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 financial statements are free from material misstatement.

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

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

Opinion

6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

ZAO PricewaterhouseCoopers Audit
Moscow, Russian Federation
16 October 2007

AVTOVAZ GROUP
Consolidated Balance Sheet at 31 December 2006
(In millions of Russian Roubles)
(Amounts translated into U.S. dollars for convenience purposes, Note 2.2)

		RR million		Additional information Unaudited US$ million
	Note	**31 December 2006**	31 December 2005	31 December 2006
ASSETS				
Current assets:				
Cash and cash equivalents	8	**13,512**	13,644	513
Trade receivables, net	7, 9	**6,610**	7,571	251
Financial assets	10	**3,440**	4,012	131
Other current assets	11	**10,944**	11,973	416
Inventories	12	**25,729**	20,861	977
Total current assets		**60,235**	58,061	2,288
Long-term assets:				
Property, plant and equipment	13	**102,056**	102,991	3,876
Financial assets	15	**5,501**	4,070	209
Investments in associates	16	**1,903**	1,680	72
Development costs	14	**4,496**	3,532	171
Other long-term assets	17	**772**	1,127	29
Total assets		**174,963**	171,461	6,645
LIABILITIES & EQUITY				
Current liabilities:				
Trade payables	7, 18	**22,235**	17,488	845
Other payables and accrued expenses	19	**7,883**	5,892	299
Income tax liability		**155**	165	6
Taxes other than income tax	22	**3,214**	3,360	122
Provisions	20	**2,850**	1,024	108
Debt	21	**26,417**	17,559	1,003
Advances from customers		**3,235**	10,727	123
Total current liabilities		**65,989**	56,215	2,506
Long-term liabilities:				
Debt	21	**11,584**	18,252	440
Taxes other than income tax	22	**2,654**	2,741	101
Provisions	20	**286**	229	11
Deferred income tax liabilities	32	**10,840**	11,209	412
Lease payables	33	**113**	59	4
Total liabilities		**91,466**	88,705	3,474
Equity				
Share capital	23	**27,447**	30,134	1,042
Currency translation adjustment		**996**	1,093	38
Retained earnings		**53,279**	49,537	2,024
Equity holders' of the Company		**81,722**	80,764	3,104
Minority interest		**1,775**	1,992	67
Total equity		**83,497**	82,756	3,171
Total liabilities and equity		**174,963**	171,461	6,645

I.N. Gubin
Vice-President, Finance and Economics,
AVTOVAZ GROUP Ltd.

N.B. Lisovskaya
Acting Chief Accountant,
JSC AVTOVAZ

16 October 2007

The accompanying notes on pages 7 to 36 are an integral part of these consolidated financial statements.

AVTOVAZ GROUP
Consolidated Income Statement for the year ended 31 December 2006
(In millions of Russian Roubles, except for earnings per share)
(Amounts translated into U.S. dollars for convenience purposes, Note 2.2)

	Note	RR million		Additional information Unaudited US$ million
		Year ended 31 December		
		2006	2005	2006
Net sales	24	**184,093**	159,614	6,771
Cost of sales	25,31	**(152,894)**	(135,033)	(5,623)
Gross profit		**31,199**	24,581	1,148
Administrative expenses	26, 31	**(14,263)**	(12,823)	(525)
Distribution costs	27, 31	**(7,673)**	(7,049)	(282)
Research expenses	28, 31	**(205)**	(448)	(8)
Other operating income, net	29, 31	**310**	724	11
Operating income		**9,368**	4,985	344
Finance costs, net	30	**(3,208)**	(4,390)	(118)
Share of associates' income	16	**535**	104	20
Net gain from forgiveness of tax debt		**-**	791	-
Profit before taxation		**6,695**	1,490	246
Income tax expense	32	**(3,171)**	(2,163)	(116)
Profit/(loss) for the year		**3,524**	(673)	130
Attributable to:				
Equity holders' of the Company		**3,100**	(1,205)	114
Minority interest		**424**	532	16
		3,524	(673)	130
Weighted average number of shares outstanding during the period ('000)		**1,402,296**	1,448,535	
Earnings/(loss) per ordinary share (basic/diluted) (in Roubles and US$)	34	**2.21**	(0.83)	0.08
Earnings/(loss) per preference share (basic/diluted) (in Roubles and US$)	34	**2.21**	(0.83)	0.08

Consolidated Statement of Cash Flows for the year ended 31 December 2006
(In millions of Russian Roubles)
(Amounts translated into U.S. dollars for convenience purposes, Note 2.2)

		RR million		Additional information Unaudited US$ million
		Year ended 31 December		
	Note	**2006**	2005	2006
Cash flows from operating activities:				
Profit before taxation		**6,695**	1,490	246
Adjustments for:				
Depreciation and amortisation	31	**7,272**	6,395	267
Provision for impairment of trade receivables	26	**(254)**	121	(9)
Provision for impairment of other current assets	26	**194**	122	7
Taxation provision	29	**1,591**	(286)	59
Interest expense	30	**4,153**	4,079	153
Reversal of provision for impairment of property, plant and equipment	13	**(484)**	(464)	(18)
Net gain from forgiveness of tax debt		**-**	(791)	-
(Gain)/loss on disposal of property, plant and equipment	29	**(237)**	168	(9)
Loss on impairment of financial assets	29	**125**	45	5
Share of associates' income	16	**(535)**	(104)	(20)
Loss on impairment of property, plant and equipment	13	**252**	382	9
Gain on disposal of long- term financial assets, subsidiaries and associates	29	**(200)**	(170)	(7)
Unrealised foreign exchange effect on non-operating balances		**(849)**	369	(31)
Operating cash flows before working capital changes		**17,723**	11,356	652
Decrease/(increase) of gross trade receivables		**1,215**	(144)	45
Decrease/(increase) in current financial and other assets		**1,213**	(2,907)	45
Increase in inventories		**(4,868)**	(119)	(179)
Increase/(decrease) in trade payables, other payables and accrued expenses		**6,640**	(1,089)	244
Decrease in tax liabilities		**(146)**	(778)	(5)
(Decrease)/increase in advances from customers		**(7,492)**	2,520	(276)
Loans issued		**(51,435)**	(38,323)	(1,892)
Loans repaid		**50,808**	36,312	1,868
Cash generated from operations		**13,658**	6,828	502
Income tax paid		**(3,062)**	(1,832)	(113)
Interest paid		**(3,217)**	(3,053)	(118)
Net cash generated from operating activities		**7,379**	1,943	271
Cash flows from investing activities:				
Purchase of property, plant and equipment and development costs additions		**(8,033)**	(8,212)	(295)
Proceeds from the sale of property, plant and equipment		**482**	335	18
Purchase of financial assets		**(3,934)**	(536)	(145)
Proceeds from sale of financial assets		**3,529**	35	130
Dividends received		**201**	322	7
Irrevocable letter of credit issued for the purchase of equipment		**(290)**	(31)	(11)
Net cash used in investing activities		**(8,045)**	(8,087)	(296)
Cash flows from financing activities:				
Proceeds from debt		**156,859**	102,946	5,769
Repayment of debt and restructured taxes		**(153,810)**	(95,378)	(5,657)
Dividends paid		**(73)**	(256)	(3)
Proceeds from sale of treasury shares		**-**	445	-
Purchase of treasury shares		**(2,446)**	(55)	(90)
Purchase of minority interest in existing subsidiaries		**(170)**	(212)	(6)
Net cash provided from financing activities		**360**	7,490	13
Effect of exchange rate changes		**(85)**	(64)	(3)
Effect of translation		**-**	-	44
Net (decrease)/increase in cash and cash equivalents		**(391)**	1,282	29
Cash and cash equivalents at the beginning of the period		**13,613**	12,331	473
Cash and cash equivalents at the end of the period	8	**13,222**	13,613	502

AVTOVAZ GROUP
Consolidated Statement of Changes in Equity for the year ended 31 December 2006
(In millions of Russian Roubles)
(Amounts translated into U.S. dollars for convenience purposes, Note 2.2)

RR million	Note	Share capital	Treasury shares	Currency translation adjustment	Retained earnings	Attributable to equity holders' of the Company	Minority interest	Total equity
Balances as of 31 December 2004		**64,251**	**(35,361)**	**1,338**	**51,646**	**81,874**	**1,616**	**83,490**
Currency translation adjustment		-	-	(245)	-	(245)	-	(245)
Loss for the year		-	-	-	(1,205)	(1,205)	532	(673)
Total recognised loss for 2005		**-**	**-**	**(245)**	**(1,205)**	**(1,450)**	**532**	**(918)**
Purchase of treasury shares		-	(156)	-	101	(55)	-	(55)
Sale of treasury shares		-	1,400	-	(1,009)	391	54	445
Dividends	23	-	-	-	(438)	(438)	107	(331)
Purchase of minority interest in existing subsidiaries		-	-	-	442	442	(562)	(120)
Minority interest of newly formed subsidiaries		-	-	-	-	-	248	248
Disposal of subsidiaries		-	-	-	-	-	(3)	(3)
Balances as of 31 December 2005	23	**64,251**	**(34,117)**	**1,093**	**49,537**	**80,764**	**1,992**	**82,756**
Currency translation adjustment		-	-	(97)	-	(97)	-	(97)
Profit for the year		-	-	-	3,100	3,100	424	3,524
Total recognised income for 2006		**-**	**-**	**(97)**	**3,100**	**3,003**	**424**	**3,427**
Purchase of treasury shares	6.1	-	(2,687)	-	918	(1,769)	(677)	(2,446)
Dividends	23	-	-	-	(106)	(106)	28	(78)
Purchase of minority interest in existing subsidiaries	6	-	-	-	(170)	(170)	36	(134)
Disposal of subsidiaries		-	-	-	-	-	(28)	(28)
Balances as of 31 December 2006	23	**64,251**	**(36,804)**	**996**	**53,279**	**81,722**	**1,775**	**83,497**

Additional information

(Unaudited) US$ million	Share capital	Treasury shares	Currency translation adjustment	Retained earnings	Attributable to equity holders' of the Company	Minority interest	Total equity
Balances as of 31 December 2006	2,440	(1,398)	38	2,024	3,104	67	3,171

The statutory accounting reports of JSC AVTOVAZ (the "Company") are the basis for profit distribution and other appropriations. Russian legislation identifies the basis of distribution as the net profit. For the year ended 31 December 2006, the current net statutory profit for the Company as reported in its statutory reporting forms was RR 2,512 (year ended 31 December 2005: RR 1,400). However, this legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and accordingly management believes at present it would not be appropriate to disclose an amount for the distributable reserves in these consolidated financial statements.

1. JSC AVTOVAZ and subsidiaries

JSC AVTOVAZ and its subsidiaries' (the "Group") principal activities include the manufacture and sale of passenger vehicles. The Group's manufacturing facilities are primarily based in the Samara Oblast of Russia. The Group has a sales and service network spanning the Commonwealth of Independent States and some other countries. The parent company, JSC AVTOVAZ ("the Company" or "JSC AVTOVAZ"), was incorporated as an open joint stock company in the Russian Federation on 5 January 1993. At 31 December 2006 the Group employed 150,092 employees (31 December 2005: 154,846 employees). JSC AVTOVAZ is registered at Yuzhnoye Shosse, 36, Togliatti, 445633, Russian Federation.

These consolidated financial statements have been approved for issue by the Vice-President, Finance and Economics of AVTOVAZ GROUP Ltd. on 16 October 2007.

The individual executive body of JSC AVTOVAZ is represented by the management entity AVTOVAZ GROUP Ltd.

2. Basis of presentation of the consolidated financial statements

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

JSC AVTOVAZ and its subsidiaries resident in the Russian Federation, which account for approximately 94% of assets and liabilities of the Group, maintain their accounting records in Russian Roubles ("RR") and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. These consolidated financial statements are based on the statutory records, with adjustments and reclassifications recorded for the purpose of fair presentation in accordance with IFRS. Similarly, adjustments to conform with IFRS, where necessary, are recorded in the financial statements of companies not resident in the Russian Federation.

The consolidated financial statements have been prepared under the historical cost convention except for corporate and municipal bonds and shares, which are recognised as financial assets at fair value through profit or loss, bank promissory notes, which are recognised as assets available-for-sale. The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 5.

2.1 Accounting for the effect of inflation

Prior to 1 January 2003 the adjustments and reclassifications made to the statutory records for the purpose of IFRS presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with IAS 29 ("Financial Reporting in Hyperinflationary Economies"). IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation has ceased, effective from 1 January 2003 the Group no longer applies the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts in these consolidated financial statements.

2.2 Additional information

U.S. dollar ("US$") amounts shown in the accompanying consolidated balance sheet, consolidated income statement and consolidated statement of cash flows, are translated from RR as a matter of arithmetical computation only. The consolidated balance sheet has been translated at the official rate of the Central Bank of the Russian Federation at 31 December 2006 of RR 26.33 = US$ 1 (31 December 2005: RR 28.78 = US$ 1). The consolidated income statement and the consolidated statement of cash flows have been translated at the average exchange rate during the year ended 31 December 2006 of RR 27.19 = US$ 1 (2005: RR 28.29 = US$ 1). The US$ amounts are presented solely for the convenience of the reader as supplementary information, in order to facilitate comparability of the Group's financial position with those of similar companies that present their financial statements in US Dollars, and should not be construed as a representation that RR amounts have been, could have been, or would be converted to US$ at this rate, nor that the US$ amounts present fairly the financial position and results of operations and cash flows of the Group in accordance with IFRS.

2.3 Change in Accounting Policies

The Group changed its accounting policy with respect to the recognition of revenue from the construction and sale of real estate. Previously the Group had applied the percentage of completion method. Following a review of contracts and taking into account recent IFRS developments, the management has determined that it is more appropriate to recognise revenue and associated costs if all recognition criteria for the sale of goods under IAS 18 have been met. As a consequence of this change in accounting policy net sales and cost of sales decreased by RR 822 for the year ended 31 December 2005, advances to sub-contractors and costs of the subsidiary-real estate developer within other current assets and advances from investors of the subsidiary-real estate developer within other payables and accrued expenses increased by RR 449.

3. Summary of significant accounting policies

3.1 New accounting pronouncements

The following new standards, amendments to standards and interpretations are mandatory for periods beginning from 1 January 2006.

- Amendment to IAS 19, 'Employee Benefits', effective for annual periods beginning on or after 1 January 2006. This amendment is not relevant for the Group.
- Amendment to IAS 39, Amendment to 'The fair value option', effective for annual periods beginning on or after 1 January 2006. This amendment does not have any impact on the classification and valuation of the Group's financial instruments classified as at fair value through profit or loss prior to 1 January 2006 as the Group is able to comply with the amended criteria for the designation of financial instruments at fair value through profit and loss.
- Amendment to IAS 21, Amendment 'Net investment in a foreign operation', effective for annual periods beginning on or after 1 January 2006. This amendment did not have a significant impact on these consolidated financial statements.
- Amendment to IAS 39, Amendment 'Cash flow hedge accounting of forecast intragroup transactions', effective for annual periods beginning on or after 1 January 2006.This amendment did not have a significant impact on these consolidated financial statements.
- Amendment to IAS 39 and IFRS 4, Amendment 'Financial guarantee contracts', effective for annual periods beginning on or after 1 January 2006. Following the amendment, the Group has recognised at 31 December 2006 the financial guarantees issued to third parties, in the amount of RR 18 among its Other payables and accrued expenses.
- IFRS 6, 'Exploration for and evaluation of mineral resources', effective for annual periods beginning on or after 1 January 2006. This standard is not relevant for the Group.
- IFRIC 4, 'Determining whether an arrangement contains a lease', effective for annual periods beginning on or after 1 January 2006. This interpretation is not relevant for the Group.
- IFRIC 5, 'Rights to interests arising from decommissioning, restoration and environmental rehabilitation funds', effective for annual periods beginning on or after 1 January 2006. This interpretation is not relevant for the Group.
- IFRIC 6, 'Liabilities arising from participating in a specific market – waste electrical and electronic equipment', effective for annual periods beginning on or after 1 December 2005. This interpretation is not relevant for the Group.

The following new standards, amendments to standards and interpretations have been issued but are not effective for 2006 and have not been early adopted:

- IFRIC 7, 'Applying the Restatement Approach under IAS 29', effective for annual periods beginning on or after 1 March 2006. Management does not expect the interpretation to be relevant for the Group.
- IFRIC 8, 'Scope of IFRS 2', effective for annual periods beginning on or after 1 May 2006. Management is currently assessing the impact of the interpretation for the Group.
- IFRIC 9, 'Reassessment of Embedded Derivatives', effective for annual periods beginning on or after 1 June 2006. Management believes that this interpretation should not have a significant impact on the reassessment of embedded derivatives as the Group already assesses if embedded derivative should be separated using principles consistent with IFRIC 9. Management is currently assessing the impact of the interpretation for the Group.
- IFRIC 10 'Interim Financial Reporting and Impairment', effective for annual periods beginning on or after 1 November 2006. Management is currently assessing the impact of the interpretation for the Group.
- IFRIC 11, IFRS 2 'Group and Treasury Share Transactions', effective for annual periods beginning on or after 1 March 2007. Management is currently assessing the impact of the interpretation for the Group.
- IFRIC 12, 'Service Concession Arrangements', effective for annual periods beginning on or after 1 January 2008. Management is currently assessing the impact of the interpretation for the Group.
- IFRS 7, 'Financial instruments: Disclosures', effective for annual periods beginning on or after 1 January 2007. IAS 1, 'Amendments to capital disclosures', effective for annual periods beginning on or after 1 January 2007. The IFRS introduces new disclosures to improve the information about financial instruments. Specifically, it requires disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk including sensitivity analysis to market risk. It replaces some of the requirements in IAS 32, 'Financial Instruments: Disclosure and Presentation'. The Amendment to IAS 1 introduces disclosures about level of an entity's capital and how it manages capital. The Group is currently assessing what impact the new IFRS and the amendment to IAS 1 will have on disclosures in its consolidated financial statements.

3. Summary of significant accounting policies (continued)
3.1 New accounting pronouncements (continued)

- IFRS 8, 'Operating Segments', effective for annual periods beginning on or after 1 January 2009. The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. The Group is currently assessing what impact new standards will have on segment disclosures in the Group's consolidated financial statements.

- IAS 23 (Revised), 'Recognition of Borrowing Costs'. The revision removed the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. The revised standard applies to borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. The Group is currently assessing what impact this revision will have to the Group's consolidated financial statements.

- IFRIC 13, 'Customer Loyalty Programmes' (effective for annual periods beginning on or after 1 July 2008). IFRIC 13 addresses whether the entity's obligations to provide free or discounted goods or services in the future should be recognised and measured, and if consideration is allocated to the award credits how much should be allocated to them, when revenue should be recognised and if a third party supplies the awards, how revenue should be measured. IFRIC 13 is not relevant for the Group's financial statements.

- IFRIC 14, 'IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction'. (effective for annual periods beginning on or after 1 January 2008). IFRIC 14 addresses when refunds or reductions in future contributions should be regarded as available in accordance with paragraph 58 of IAS 19; how a minimum refunding requirement might affect the availability of reductions in future contributions, and when a minimum refunding requirement might give rise to a liability. IFRIC 14 is not relevant for the Group's financial statements.

- IAS 1, 'Presentation of Financial Statements' (effective for annual periods beginning on or after 1 January 2009). IAS 1 (revised) changes the presentation of financial statements and introduces new disclosure requirements. The Group is currently assessing the impact of these new requirements on the presentation of the Group's financial statements.

3.2 Group reporting
Subsidiaries
Subsidiaries are entities over which the Group has the power to govern the financial and operating policies. Control is generally assessed when the Group has a shareholding of more than one half of an entity's voting rights. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All inter-company transactions, balances and unrealised gains on transactions between the Group's companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Minority interest at the balance sheet date includes the minority shareholders' portion of the fair values of the identifiable assets and liabilities of subsidiaries at the acquisition date, and the minority's portion of movements in those subsidiaries' equity since the date of acquisition. Minority interest is presented in the consolidated balance sheet within equity, separately from the equity attributable to equity holders' of the Company. The Group does not attribute minority interest relating to cross shareholdings (see Note 6.2).

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of net assets of the subsidiary acquired, the difference is recognised directly in the consolidated income statement.

Purchases of minority interests
Difference, if any, between the carrying amount of a minority interest and the amount paid to acquire is recorded as an adjustment directly in equity.

3. Summary of significant accounting policies (continued)

3.2 Group reporting (continued)

Associates

Associates are all entities over which the Group has significant influence but not control, generally a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Associates' accounting policies have been changed where necessary to ensure consistency with the policies adopted by the Group.

Equity accounting is discontinued when the carrying amount of the investment in an associate reaches zero, unless the Group has incurred obligations or guaranteed obligations in respect of the associate.

3.3 Financial assets

Classification of financial assets

The Group classifies its financial assets into the following measurement categories: financial assets at fair value through profit or loss, loans and receivables, held to maturity and available-for-sale.

Financial assets at fair value through profit or loss are financial assets held for trading and include corporate and municipal bonds and shares. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term.

Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Group intends to sell in the near term.

Held to maturity includes quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has both the intention and ability to hold to maturity. Management determines the classification of investment securities held to maturity at their initial recognition and reassesses the appropriateness of that classification at each balance sheet date.

All other financial assets are included in the available-for-sale category.

Available-for-sale financial assets

Available-for-sale financial assets are carried at fair value. Interest income on available-for-sale debt securities is calculated using the effective interest method and recognised in profit or loss.

Dividends on available-for-sale equity instruments are recognised in profit or loss when the Group's right to receive payment is established. All other elements of changes in the fair value are deferred in equity until the investment is derecognised or impaired at which time the cumulative gain or loss is removed from equity to profit or loss.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of available-for-sale financial assets. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through current period's profit or loss.

Initial recognition of financial instruments

All financial assets and liabilities are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial instruments that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Group commits to deliver a financial asset. All other purchases and sales are recognised on the settlement date with the change in value between the commitment date and settlement date not recognised for assets carried at cost or amortised cost; recognised in profit or loss for trading investments; recognised in equity for assets classified as available-for-sale.

3. Summary of significant accounting policies (continued)

3.3 Financial assets (continued)

Derecognition of financial assets

The Group derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets have otherwise expired or (ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Group has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

3.4 Revenue recognition

Revenues on sales of automobiles, spare parts, miscellaneous production and car technical services are recognised when goods are dispatched or services rendered to customers, as this is normally the date that the risks and rewards of ownership are transferred to the customers.

Sales of services are recognised in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Sales are shown net of value added tax (VAT) and discounts, and after eliminating sales within the Group.

3.5 Trade receivables

Trade receivables are carried at original invoice amount less provision made for impairment of these receivables and includes value added taxes. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, discounted at the market rate of interest for similar borrowers. The amount of the provision is recognised in the consolidated income statement.

3.6 Value added tax

Output value added tax related to sales is payable to tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognised in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

3.7 Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost of inventory is determined on the weighted average basis. The costs of finished goods and work in progress comprises material, direct labour and the appropriate indirect manufacturing costs (based on normal operating capacity). Obsolete and slow-moving inventories are written down, taking into account their expected use, to their future realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

3.8 Cash and cash equivalents

Cash comprises cash on hand, demand deposits held with banks, bank promissory notes, loans given by a subsidiary bank to banks, amounts due from other banks to a subsidiary bank, non-restricted balances with the Central Bank of the Russian Federation by a subsidiary bank and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method. Restricted balances are excluded from cash and cash equivalents for the purposes of the consolidated statement of cash flows. Bank overdrafts are included in debt within current liabilities in the consolidated balance sheet.

3.9 Property, plant and equipment

Property, plant and equipment are recorded at purchase or construction cost. Property, plant and equipment purchased before 31 December 2002 were recorded at purchase or construction cost restated to the equivalent purchasing power of the RR as at 31 December 2002. At each reporting date management assess whether there is any indication of impairment of property, plant and equipment. If any such indication exists, the management estimates the recoverable amount, which is determined as the higher of an asset's net selling price and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the consolidated income statement. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the assets recoverable amount.

(In millions of Russian Roubles)

3. Summary of significant accounting policies (continued)

3.9 Property, plant and equipment (continued)

Depreciation of the restated amounts of property, plant and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

	Number of years
Buildings	40 to 80
Foundry equipment	10 to 20
Plant, machinery and equipment	5 to 20
Other	5 to 13

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred. Major renewals and improvements are capitalised and the assets replaced are retired. Gains and losses arising from the retirement or disposal of property, plant and equipment are included in the consolidated income statement as incurred.

Assets under construction owned by the Group are not depreciated.

3.10 Finance leases

Leases of property, plant and equipment in which substantially all the risks and rewards incidental to ownership are transferred to the Group, are classified as finance leases. The assets leased are capitalised in property, plant and equipment at the commencement of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments.

Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in the consolidated balance sheet as lease payables.

The finance cost (interest) is charged to the consolidated income statement over the lease period so as to achieve a constant charge on the debt balance outstanding.

3.11 Intangible assets

Research and development expenditure

Research expenditure is recognised as an expense as incurred. Costs incurred for development projects related to a new range of vehicles are recognised as intangible assets if, and only if, it is probable that the future economic benefits exceeding costs beyond one year that are attributable to the asset will flow to the Group and the cost of the asset can be measured reliably. Development costs not yet available for use are tested for impairment annually. Development costs with a finite useful life that have been capitalised are amortised from the commencement of the commercial production of the new vehicles. The method and period of amortisation are determined by the Group for each finished work on the basis of economic feasibility over the period of its expected benefits.

The maximum period to use the results comprise no longer than 5 years.

3.12 Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment and whenever events or changes in circumstance indicate that the carrying amount may not be recoverable. Assets that are subject to amortisation are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

Cash-generating unit is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets.

3. Summary of significant accounting policies (continued)

3.13 Deferred income taxes

Deferred tax assets and liabilities are calculated in respect of temporary differences using the balance sheet liability method for financial reporting and accounting for deferred income taxes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit.

Deferred income taxes are provided for all temporary differences arising between the tax basis of assets and liabilities and their carrying values for financial reporting purposes. 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.

3.14 Debt and restructured taxes

Debt is recognised initially at cost which is the fair value of the proceeds received, net of transaction costs incurred. Debt is subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the debt using the effective interest method. All debt costs are expensed in the period in which they are incurred. Interest expense, which is currently due, is recorded within other payables and accrued expenses, whilst other interest that accrues is included within the restructured liabilities.

Debt is classified as current liability unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

Restructured taxes are recognised initially at their fair value (which is determined using the prevailing market rate of interest for a similar instrument). In subsequent periods, restructured taxes are stated at amortised cost.

3.15 Foreign currency transactions and translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in Russian Roubles, which is the Company's functional and presentation currency. U.S. dollar amounts have been provided as supplementary information only.

Monetary assets and liabilities, which are denominated in foreign currencies at the balance sheet date, are translated into the functional currency at the exchange rate prevailing at that date. Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transaction. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currency are recognised in the consolidated income statement.

Translation from functional to presentation currency

The results and financial position of each Group entity (functional currency of none of which is a currency of a hyperinflationary economy) are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

The principal rate of exchange as of 31 December 2006 used for translating foreign currency balances is stated in Note 2.2.

3.16 Product warranty costs

The Group recognises the estimated liability to repair or replace products sold still under warranty at the balance sheet date. This provision is calculated based on past history of the level of repairs and replacements.

3. Summary of significant accounting policies (continued)

3.17 Employee benefits

Social costs

The Group incurs costs on social activities, principally within the City of Togliatti. The Group provides medical services, maintains recreation departments, summer camps for children, community facilities and provides financing of kindergartens. These services represent a cost of employing principally production workers and, accordingly, have been charged to cost of sales in the consolidated income statement.

Pension costs

The Group's obligatory contributions to the Pension Fund of the Russian Federation are expensed as incurred.

3.18 Interest expense and interest income

Interest income and expenses are recognised on the accrual basis, as earned or incurred. Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised either as cash is collected or on a cost-recovery basis as conditions warrant.

3.19 Earnings/(loss) per share

Preference shares are considered to be participating shares, as their dividends may not be less than that given with respect to ordinary shares. Earnings per share is determined by dividing the net profit (loss) attributable to ordinary and preference shareholders by the weighted average number of participating shares outstanding during the reporting period.

In accordance with the IAS 33 (Revised) for those instruments that are not convertible into a class of ordinary shares, profit or loss for the period is allocated to the different classes of shares in accordance with their rights to participate in undistributed earnings. To calculate basic and diluted earnings per share:

(a) profit or loss attributable to equity holders of the parent entity is adjusted (a profit reduced and a loss increased) by the amount of dividends declared in the period for each class of shares.

(b) the remaining profit or loss is allocated to ordinary shares and preference shares to the extent that each instrument shares in earnings as if all of the profit or loss for the period had been distributed. The total profit or loss allocated to each class of equity instrument is determined by adding together the amount allocated for dividends and the amount allocated for a participation feature.

(c) the total amount of profit or loss allocated to each class of shares is divided by the number of outstanding shares to which the earnings are allocated to determine the earnings per share for each class of shares.

3.20 Use of promissory notes

Promissory notes are debt securities. The Group makes extensive use of both third party promissory notes and Group originated promissory notes in its operations. Bank promissory notes received are included in the consolidated balance sheet within cash and cash equivalents with original maturities of three months or less. Promissory notes issued by the Group, are included within trade payables until they are settled for cash.

3.21 Leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the consolidated income statement on a straight-line basis over the period of the lease.

3.22 Shareholders' equity

Share capital

Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction in equity from the proceeds. Any excess of the fair value of consideration received over the par value if shares issued is recognised as a share premium.

Treasury shares

Treasury shares are stated at nominal value, restated to the equivalent purchasing power of the RR as at 31 December 2002. Any difference between cost and nominal value on the purchase of treasury shares is included in equity attributable to the equity holders' of the Company. Any gains or losses arising on the disposal of treasury shares are recognised in equity attributable to the equity holders' of the Company.

3. Summary of significant accounting policies (continued)

3.22 Shareholders' equity (continued)

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 when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the date the financial statements are authorised for issue.

3.23 Provisions

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

3.24 Uncertain tax positions

The Group's uncertain tax positions are reassessed by management at every balance sheet date. Liabilities are recorded for tax positions that are determined by management as less likely than not to be sustained if challenged by tax authorities, based on the interpretation of tax laws that have been enacted or substantively enacted by the balance sheet date. Liabilities for penalties, interest and taxes other than income tax are recognised based on management's best estimate of the expenditure required to settle the obligations at the balance sheet date.

3.25 Comparative information

In order to achieve a more proper presentation consistent with the current reporting period, certain reclassifications have been made to the comparative figures. Certain reclassifications have been made to the corresponding amounts in the 2006 consolidated statement of cash flows. Main reclassifications relate to certain financing received by a subsidiary of the Group. As a consequence of this reclassification cash flows from financing activities and cash flows from operating activities have not changed. Additionally the Group has reclassified cash outflows in relation to development costs from operating to investing activities, the reclassification amounts to RR 804.

4. Financial risk management

The Group's activities are exposed to a variety of financial risks: market risk (including foreign exchange risk, fair value interest risk and price risk), credit risk, liquidity risk and cash flow interest-rate risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance.

(a) Market risk

Market risk for the Group is primarily associated with foreign exchange risk. The Group carries out manufacturing operations both within and outside the Russian Federation (see Note 24). Consequently the Group is exposed to foreign exchange risk primarily with respect to the U.S. dollar and the EURO. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities, receipt and repayment of debt and net investment in foreign operations. Foreign exchange risk arises when future commercial transactions, recognised assets and liabilities are denominated in a currency that is not the entity's functional currency. Risk management is carried out by JSC AVTOVAZ Finance Department, which identifies, evaluates and manages foreign exchange risks by analysing the net position in each foreign currency. The Group is not exposed to equity securities price risk. The Group has not entered into any hedging arrangements in respect of its foreign currency exposure.

(b) 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 trade receivables, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk. The Group has no other 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 provision already recorded.

Cash is placed in financial institutions, which are considered at time of plan and deposit to have minimal risk of default.

(c) Liquidity risk

The Group manages its liquidity risk by maintaining sufficient cash and marketable securities and available funding through an adequate amount of committed credit facilities.

(d) Cash flow and fair value interest rate risk

The Group's interest-rate risk arises from debt. The majority of interest rates on debt are fixed. Existing interest rates can be changed subject to agreement by the third parties. Assets are generally non-interest bearing; the Group's income and operating cash flows are substantially independent of changes in market interest rates. The Group has not entered into any hedging arrangements in respect of its interest rate exposures.

5. Critical accounting estimates and judgements

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the current circumstances.
The estimates and assumptions that have a risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

5.1 Taxation

The Group is subject to taxes. Significant judgement is required in determining the provision for taxes. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Group recognises liabilities for anticipated tax audit issues based on management's estimates of whether additional taxes will be due.

As at 31 December 2006 the balance of taxation provisions of RR 1,591 in Note 20 relates to JSC AVTOVAZ's ongoing legal proceedings in relation to decisions of tax authorities on additional taxes, fines and penalties accrued as a result management's assessment of recent tax audits. As disclosed in Note 38, after the balance sheet date the Russian Federation Tax Service following a review of appeals filed by JSC AVTOVAZ reduced the tax claim against JSC AVTOVAZ. This settlement has been treated as a non-adjusting post balance sheet event in accordance with IAS 10, 'Events after the balance sheet date'.

5.2 Remaining useful life of property, plant and equipment

Management assesses the remaining useful life of property, plant and equipment in accordance with the current technical conditions of assets and estimated period when these assets will bring economic benefit to the Group.

If the estimated remaining useful life of buildings had been 5% higher or lower than management estimates, then the carrying value of buildings would be RR 1,832 higher or RR 2,025 lower respectively. If the estimated remaining useful life of plant and equipment had been 5% higher or lower than management estimates, then the carrying value of plant and equipment would be RR 3,712 higher or RR 4,103 lower respectively.

5.3 Fair values

In assessing the fair value of unquoted financial instruments the Group uses a variety of methods including estimated discounted value of future cash flows, and makes assumptions that are based on market conditions existing at each balance sheet date.

At 31 December 2006 and 31 December 2005, the fair value of certain financial liabilities was estimated by discounting the future contractual cash flows at the current market interest rate available to the Group for similar financial instruments with the same remaining maturity, and is disclosed in the relevant notes to these consolidated financial statements.

5.4 Subsidiaries and Associates

The Group holds more than 20% of the voting rights in OAO VAZINTERSERVICE but does not have the significant influence over the financial and operating policies of this entity. Consequently, OAO VAZINTERSERVICE has been accounted at cost and not consolidated by the equity method of accounting.

5.5 Non-accrual of provision in respect of certain payments to employees on retirement

Management has determined that certain one-off payments to employees on retirement do not result in a legal or constructive obligation to the Group. As a consequence, no provision in respect of these payments was provided.

(In millions of Russian Roubles)

6. Principal subsidiaries and associates

The principal subsidiaries of the Group and the degree of control exercised by the Group are as follows:

Entity	Country of Incorporation	Activity	**31 December 2006 % share**	31 December 2005 % share
OAO DAAZ	Russia	Car components	**100**	100
OAO SAAZ	Russia	Car components	**100**	100
OAO AvtoVAZtrans	Russia	Transport	**100**	100
OAO TEVIS	Russia	Utilities	**100**	100
OAO Elektroset	Russia	Power supply	**100**	100
ZAO CB Avtomobilny Bankirsky Dom (hereinafter – ZAO CB ABD)	Russia	Bank services	**100**	100
Delta Motor Group Oy	Finland	Car distribution	**100**	100
ZAO Ukravtovaz	Ukraine	Car distribution	**100**	100
ZAO Serdobsky Mashinostroitelny Zavod	Russia	Car components	**51**	51
Lada International Ltd.	Cyprus	Car distribution	**99.9**	99.9
OAO AVVA	Russia	Financial	**86**	86
ZAO Central Branch of Automobile Financial Corporation (hereinafter – ZAO CB AFC)	Russia	Investing and financial	**60**	60
OAO Piter-Lada	Russia	Car distribution	**52.4**	52.4
ZAO IFC	Russia	Investing and financial	**100**	51
OOO Eleks-Polus	Russia	Car distribution	**51**	51
OAO Avtocentre-Togliatti-VAZ	Russia	Maintenance	**51**	51
133 Technical Service Centres	Russia, CIS	Car service centres	**50.1-100**	50.1-100

All of the above subsidiaries have been consolidated.

In 2006 JSC AVTOVAZ acquired a 51% interest in OOO Audit Service for RR 170. ZAO CB ABD owns 49% of share capital of OOO Audit Service. Consequently, as at 31 December 2006 100% of share capital of OOO Audit Service is owned by the Group's entities. As OOO Audit Service owns 49% of ZAO IFC then through this transaction the Group acquired the full minority interest of 49% (effective minority interest amounted to 44.6%) in ZAO IFC. A loss on acquisition of additional shares in a subsidiary amounted to RR 170 and was recognised in the consolidated statement of changes in equity.

The principal associated companies and degree of significant influence by the Group are as follows:

Entity	Country of Incorporation	Activity	**31 December 2006 % share**	31 December 2005 % share
ZAO GM-AVTOVAZ	Russia	Vehicle production	**41.6**	41.6
OAO National Trade Bank	Russia	Bank services	**20.8**	20.8

6.1 Cross shareholding:

At 31 December 2006 OAO AVVA, an 86% owned subsidiary of JSC AVTOVAZ, owned 36.0% of the ordinary shares of JSC AVTOVAZ. ZAO CB AFC, in which JSC AVTOVAZ together with OAO AVVA owns 60% of shares, in turn owns 28.4% of the ordinary shares of JSC AVTOVAZ. Furthermore, ZAO IFC, a subsidiary of JSC AVTOVAZ, in which JSC AVTOVAZ together with OOO Audit Service owns 100% of shares, in turn owns 2.1% of the ordinary shares of JSC AVTOVAZ. As a result approximately 66.5% (2005: 61.6%) of the ordinary voting share capital of JSC AVTOVAZ is held by entities within the Group. The shares of JSC AVTOVAZ that are owned by subsidiaries are recognised as treasury shares in these consolidated financial statements. In accordance with Russian legislation JSC AVTOVAZ's shares owned by its subsidiaries have the right to vote at shareholders' meetings and participate in dividends distribution. Consequently, the ultimate controlling party of the Group is JSC AVTOVAZ (the parent company) itself.

In 2006 OAO AVVA acquired from third parties 660,000 ordinary shares (2.43% of ordinary shares) of JSC AVTOVAZ for RR 1,209, and 23,500 preference shares of JSC AVTOVAZ for RR 28. Also during 2006 OAO AVVA sold 660,000 ordinary shares (2.43% of ordinary shares) of JSC AVTOVAZ to ZAO CB AFC for RR 1,212. In 2006 ZAO CB AFC acquired from third parties 660,000 ordinary shares (2.43% of ordinary shares) of JSC AVTOVAZ for RR 1,209. As described in Note 21, 1,205,000 treasury shares were sold and repurchased under repo agreements and these transactions were accounted for as collaterised borrowings (see Note 21).

(In millions of Russian Roubles)

6. Principal subsidiaries and associates (continued)

6.2 Minority interest:

The minority interest in equity presented in the consolidated balance sheet does not include the holdings of OAO AVVA, ZAO CB AFC and ZAO IFC in JSC AVTOVAZ's share capital. The effective interest in JSC AVTOVAZ's ordinary capital, held by minority shareholders of these entities, amounts to 17.16% and their effective interest in JSC AVTOVAZ's share capital amounts to 14.84%.

7. Balances and transactions with related parties

7.1 Balances with related parties:

For the purposes of these consolidated financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Company's shareholding structure is disclosed in Note 6.1.

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 31 December 2006 are detailed below.

Consolidated balance sheet caption	Relationship	**31 December 2006**	31 December 2005
Trade receivables - gross	Associates	**960**	1,237
Provision for impairment of trade receivables	Associates	**(4)**	(4)
Trade payables	Associates	**328**	871
Cash and cash equivalents	Associates	**139**	887
Financial assets - current	Associates	**114**	191
Financial assets-long-term	Associates	**212**	92
Debt	Associates	**159**	132
Other payables and accrued expenses	Deposits by Key Management in a subsidiary bank	**-**	378

7.2 Transactions with related parties:

The income and expense items with related parties for 2006 and 2005 were as follows:

Consolidated income statement caption	Relationship	**2006**	2005
Sales	Associates	**7,267**	8,543
Purchases	Associates	**5,370**	6,723
Finance income	Interest receivable on deposits from an associate bank	**30**	6
Finance costs	Interest payable to Key Management on deposits in a subsidiary bank	**-**	36
Finance costs	Interest payable in an associate bank	**23**	27
Administrative expenses	Short term employee benefits - compensation of the Key Management – the Board of Directors and the Board of Management	**61**	167

Sales include sales of car kits to ZAO GM-AVTOVAZ and other sales.

(In millions of Russian Roubles)

8. Cash and cash equivalents

Cash and cash equivalents comprise the following:

	31 December 2006	31 December 2005
RR denominated short-term bank promissory notes and deposits	**6,538**	3,177
Foreign currency denominated short-term bank promissory notes and deposits	**2,442**	1,143
RR denominated cash on hand and balances with banks	**3,575**	7,705
Foreign currency denominated balances with banks	**667**	1,588
Foreign currency denominated letters of credit	**290**	31
	13,512	13,644

Restricted cash is included as a component of cash and cash equivalents but not included for the purpose of the consolidated statement of cash flows. Restricted cash at 31 December 2006 amounts to RR 290 (31 December 2005: RR 31) and includes irrevocable letters of credit which were opened in relation to equipment supplies expected in 2007.

Cash on hand and rouble-denominated balances with banks consist of the following:

	31 Decembe r 2006	31 December 2005
Cash on hand and balances with banks	**3,087**	6,854
Corresponding accounts of a subsidiary bank in other banks	**488**	851
	3,575	7,705

Foreign currency denominated balances with banks consist of the following:

Currency	31 Decembe r 2006	31 December 2005
EURO	**441**	1,008
US$	**201**	567
Other currencies	**25**	13
	667	1,588

Cash deposits of RR 2,593 held by the Group at 31 December 2006 bear a weighted-average interest of 5.7% per annum (31 December 2005: RR 1,145 bear a weighted-average interest of 4.6% per annum). Bank promissory notes of RR 3,603 bear a weighted-average interest of 6.2% per annum (31 December 2005: RR 3,165 bear a weighted-average interest of 8.3% per annum). Cash and cash equivalents of RR 7,316 (31 December 2005: RR 9,334) held by the Group are not interest bearing.

(In millions of Russian Roubles)

9. Trade receivables, net

	31 December 2006	31 December 2005
Trade receivables		
Rouble denominated	**5,149**	6,167
Foreign currency denominated	**1,720**	1,917
	6,869	8,084
Less Provision for impairment of trade receivables		
Rouble denominated	**(223)**	(471)
Foreign currency denominated	**(36)**	(42)
	(259)	(513)
Trade receivables, net		
Rouble denominated	**4,926**	5,696
Foreign currency denominated	**1,684**	1,875
	6,610	7,571

Net trade receivables denominated in foreign currencies consist of the following:

Currency	**31 December 2006**	31 December 2005
EURO	**1,416**	1,543
US$	**255**	286
Other currencies	**13**	46
	1,684	1,875

As at 31 December 2006 the fair value of trade receivables was RR 6,610 (31 December 2005: RR 7,571).

10. Financial assets – current

	31 December 2006	31 December 2005
Rouble denominated loans and receivables less provision	**2,262**	3,116
Financial assets at fair value through profit or loss	**680**	137
Available-for-sale financial assets:		
Bank promissory notes (with original maturities of more than three months)	**318**	125
Promissory notes of third parties	**180**	634
	3,440	4,012

As at 31 December 2006 the fair value of current financial assets was RR 3,259 (31 December 2005: RR 3,673).

As at 31 December 2006 loans and receivables include RR 758 (31 December 2005: RR 761) of commercial loans given by subsidiary bank ZAO CB ABD to its customers for a period less than 12 months after the balance sheet date and RR 1,219 (31 December 2005: RR 2,026) of interest free short-term loans given by the Group's subsidiary OOO Eleks-Polus to third parties. Provision for impairment of commercial loans given by subsidiary bank ZAO CB ABD to its customers at 31 December 2006 amounts to RR 65 (31 December 2005: RR 59).

Financial assets at fair value through profit or loss include corporate and municipal bonds and shares at fair value quoted in open securities market in the amount of RR 597 with interest rates ranging between 7% and 14% per annum (2005: RR 50 with interest rates ranging between 7% and 14% per annum); and investments of a subsidiary bank ZAO KB ABD in securities (GKO/OFZ) of the Government of the Russian Federation in the amount of RR 83 (31 December 2005: RR 87).

Available-for-sale financial assets are represented by interest-free bank promissory notes in the amount of RR 133 and bank promissory notes in the amount of RR 185 with interest rates ranging between 5% and 9.5% per annum (31 December 2005: interest-free bank promissory notes in the amount of RR 125).

(In millions of Russian Roubles)

10. Financial assets – current (continued)

Average effective interest rates for commercial loans given by ZAO CB ABD to its customers are as follows:

Currency	**31 December 2006**	31 December 2005
RR	**16%**	17%
US$	**7%**	11%
EURO	**12%**	11%

Collateral (primarily cars) received for commercial loans given by subsidiary bank ZAO CB ABD to its customers at 31 December 2006 (see Notes 10 and 15) amount to RR 11,095 (31 December 2005: RR 12,261).

11. Other current assets

Other current assets consist of the following:

	31 December 2006	31 December 2005
Prepaid expenses and other receivables less provision	**5,452**	4,698
Value added tax	**4,128**	6,272
Advances to sub-contractors and costs of the subsidiary-real estate developer	**1,364**	1,003
	10,944	11,973

As at 31 December 2006 prepaid expenses and other receivables include RR 288 of taxes paid as a result of the tax audits (31 December 2005: RR 977). The Company is currently disputing the results of these audits in courts. The Company's management believes there is a high possibility of a favourable outcome for JSC AVTOVAZ. Therefore, no impairment provision for these assets has been made in these consolidated financial statements. Prepaid expenses and other receivables also include RR 1,768 of payables to ZAO IK Troika Dialogue for brokerage services in the over-the-counter market (31 December 2005: nil). As at 31 December 2006 no transactions were performed under this agreement.

As at 31 December 2006 impairment provision for other current assets was RR 295 (31 December 2005: RR 101).

12. Inventories

Inventories consist of the following:

	31 December 2006	31 December 2005
Raw materials	**9,790**	8,666
Work in progress	**4,294**	3,684
Finished goods	**11,645**	8,511
	25,729	20,861

Inventories are recorded net of impairment provision of RR 410 at 31 December 2006 (31 December 2005: RR 465).

The cost of inventories recognised as expense and included in cost of sales amounted to RR 116,749 (2005: RR 105,458).

(In millions of Russian Roubles)

13. Property, plant and equipment

Property, plant and equipment and related accumulated depreciation consist of the following:

	Buildings	Plant and equipment	Other property, plant and equipment	Assets under construction	Total
Cost					
Balance at 31 December 2004	77,253	118,706	12,290	15,234	223,483
Reclassification	(172)	(2,209)	(815)	3,196	-
Additions	-	-	-	7,137	7,137
Disposals	(690)	(2,139)	(374)	(115)	(3,318)
Transfers	1,605	8,580	594	(10,779)	-
Balance at 31 December 2005	**77,996**	**122,938**	**11,695**	**14,673**	**227,302**
Accumulated depreciation and impairment					
Balance at 31 December 2004	(35,353)	(71,558)	(10,119)	(3,295)	(120,325)
Depreciation charge	(1,864)	(4,757)	(262)	-	(6,883)
Disposals	484	2,022	309	-	2,815
Reversal of impairment provision	-	-	-	464	464
Transfer of provision	-	(4)	(331)	335	-
Impairment charge	(31)	(8)	(50)	(293)	(382)
Balance at 31 December 2005	**(36,764)**	**(74,305)**	**(10,453)**	**(2,789)**	**(124,311)**
Net book amount					
Balance at 31 December 2004	**41,900**	**47,148**	**2,171**	**11,939**	**103,158**
Balance at 31 December 2005	**41,232**	**48,633**	**1,242**	**11,884**	**102,991**
Cost					
Balance at 31 December 2005	77,996	122,938	11,695	14,673	227,302
Additions	-	-	-	6,888	6,888
Disposals	(218)	(1,891)	(283)	(44)	(2,436)
Transfers	545	8,042	869	(9,456)	-
Balance at 31 December 2006	**78,323**	**129,089**	**12,281**	**12,061**	**231,754**
Accumulated depreciation and impairment					
Balance at 31 December 2005	(36,764)	(74,305)	(10,453)	(2,789)	(124,311)
Depreciation charge	(1,892)	(5,521)	(397)	-	(7,810)
Disposals	206	1,876	109	-	2,191
Reversal of impairment provision	-	-	-	484	484
Transfer of provision	-	-	(62)	62	-
Impairment charge	(29)	(9)	(214)	-	(252)
Balance at 31 December 2006	**(38,479)**	**(77,959)**	**(11,017)**	**(2,243)**	**(129,698)**
Net book amount					
Balance at 31 December 2005	**41,232**	**48,633**	**1,242**	**11,884**	**102,991**
Balance at 31 December 2006	**39,844**	**51,130**	**1,264**	**9,818**	**102,056**

(In millions of Russian Roubles)

13. Property, plant and equipment (continued)

Assets Under Construction ("AUC") include the cost of property, plant and equipment which have yet to be put into production. The balance of accumulated depreciation of AUC represents an impairment provision against construction projects started but not expected to be completed as well as a provision against the construction of properties to be used by the local community.

Impairment provision for AUC was reversed due to previously unused assets to be put in production in the nearest future. A respective gain of RR 484 was recorded in the consolidated income statement for the year ended 31 December 2006 (2005: RR 464).

Management annually reviews assets under construction and impairs those assets that are likely not to be completed. Additionally, management reviews previous impairments and releases amounts if there is evidence that this project is to be completed.

The assets transferred to the Company upon privatisation do not include the land on which the Company's factory and buildings, comprising the Group's principal manufacturing facilities, are situated. Prior to 11 December 2001 the land on which the Group's manufacturing facilities are situated was provided to JSC AVTOVAZ by local authorities for unlimited use. As a result of changes in existing legislation, on 11 December 2001 rental agreements were made with local authorities in relation to this land for the period of 49 years. Lease payments for land related to the Group's production facilities can be changed subject to agreement by the parties. The future aggregate minimum lease payments under non-cancellable operating leases of land are disclosed in Note 35.1.

Included in Property, plant and equipment and assets under construction are properties used by the local community (such as recreation departments, kindergartens, sports and medical facilities) with a gross carrying value of RR 2,704 and RR 3,246 as of 31 December 2006 and 31 December 2005, respectively. These properties are fully provided for. The impairment provision was based on value in use.

An increase of the impairment provision for property, plant and equipment of RR 252 and RR 382 for the years ended 31 December 2006 and 2005, respectively, relate predominantly to the acquisition of assets intended for use by the local community.

All impairment charges and reversals relate to the automotive segment.

As at 31 December 2006 and 31 December 2005, the gross carrying value of fully depreciated property, plant and equipment was RR 45,857 and RR 44,915, respectively.

Plant and equipment held by the Group under finance leases include:

	31 December 2006	31 December 2005
Cost – finance leases capitalised	**438**	529
Accumulated depreciation	**(174)**	(32)
Net book amount	**264**	497

14. Development costs

	31 December 2006	31 December 2005
Carrying amount	**3,532**	2,818
Additions	**1,176**	804
Amortisation for the reporting period	**(212)**	(90)
Carrying amount	**4,496**	3,532

Development costs relating to a new range of vehicles amounting to RR 1,176 were capitalised in 2006 (2005: RR 804). As of 31 December 2006 the cost and accumulated amortisation of development costs amounted to RR 4,798 (31 December 2005: RR 3,622) and RR 302 (31 December 2005: RR 90), respectively.

15. Financial assets – long-term

	31 December 2006	31 December 2005
Loans and receivables of subsidiary bank ZAO CB ABD less provision	**4,600**	3,178
Loans issued	**440**	72
Available-for-sale financial assets	**244**	284
Financial assets held to maturity	**217**	97
Financial assets at fair value through profit or loss	**-**	439
	5,501	4,070

(In millions of Russian Roubles)

15. Financial assets – non-current (continued)

Loans and receivables of subsidiary bank ZAO CB ABD at 31 December 2006 bear interest of 16% per annum (2005: RR 17% per annum). Provision for impairment of commercial loans given by subsidiary bank ZAO CB ABD to its customers at 31 December 2006 amounts to RR 208 (31 December 2005: RR 169).

As at 31 December 2006 loans issued include RR 370 (31 December 2005: RR nil) loans given by ZAO CB AFC to third parties with interest rate of 8.4% per annum and interest-free loans given by JSC AVTOVAZ to third parties in the amount of RR 70 (31 December 2005: RR 72).

As at 31 December 2006 available-for-sale financial assets represent RR 244 (2005: RR 284) of investments in shares of other companies. The investees have not published recent financial information about their operations, their shares are not quoted. Management could not reliably estimate fair value of financial assets. Therefore, the investments are carried at actual acquisition cost.

As at 31 December 2006 financial assets held to maturity include long-term bank deposits with interest rate of 8% per annum (2005: 8% per annum).

In 2005 financial assets at fair value through profit or loss represent RR 439 of corporate and municipal bonds and shares at fair value quoted in open securities market with interest rates ranging between 7% and 14% per annum.

16. Investments in associates

	31 December 2006	31 December 2005
Beginning of the period	**1,680**	1,898
Share of income/losses, net	**535**	104
Disposals	**(111)**	-
Dividends received	**(201)**	(322)
End of the period	**1,903**	1,680

Investments in associates consist of the following:

	31 December 2006	31 December 2005
ZAO GM-AVTOVAZ	**1,217**	932
Other	**686**	748
Total	**1,903**	1,680

The shareholders of ZAO GM-AVTOVAZ are JSC AVTOVAZ (41.6%), General Motors (41.6%) and EBRD (16.8%). During 2006 the associate produced 48 thousand vehicles (2005: 52 thousand vehicles) and generated revenues of RR 12,784 and a profit of RR 793.

The following amounts represent the Group's share in assets and liabilities, and sales and financial results of associates, which have been consolidated using the equity method:

	31 December 2006	31 December 2005
Assets:		
Long-term assets	**2,626**	2,647
Current assets	**3,628**	3,533
Liabilities:		
Long-term liabilities	**(410)**	(252)
Current liabilities	**(2,326)**	(2,784)
Net assets	**3,518**	3,144

	2006	2005
Revenue	**9,527**	10,385
Expenses	**(8,992)**	(10,281)
Profit after income tax	**535**	104

(In millions of Russian Roubles)

16. Investments in associates (continued)

Assets and liabilities of ZAO GM-AVTOVAZ include provisions for discontinued operations. The Group's share in these provisions recorded within long-term assets amounted to RR 56 (31 December 2005: RR 89), within current assets - RR 65 (31 December 2005: RR 98), within long-term liabilities - RR 12 (31 December 2005: RR 12), within current liabilities - RR 97 (31 December 2005: RR 181).

The share of the Group's tax provision and claims of suppliers in ZAO GM-AVTOVAZ current liabilities amounted to RR 47 (31 December 2005: RR 14).

17. Other long-term assets

	31 December 2006	31 December 2005
Long-term receivables	**315**	335
Advances for property, plant and equipment	**186**	367
Intangible assets	**143**	275
Software	**128**	150
	772	1,127

18. Trade payables

	31 December 2006	31 December 2005
Trade payables	**21,907**	16,617
Payables to associates	**328**	871
	22,235	17,488

The majority of the above balances are RR denominated and do not incur interest.

19. Other payables and accrued expenses

Other payables and accrued expenses include the following:

	31 December 2006	31 December 2005
Salaries payable and vacation accrual	**3,520**	2,811
Advances from investors of the subsidiary-real estate developer	**1,359**	449
Insurance provisions	**877**	622
Dividends payable	**149**	107
Accrued interest	**131**	190
Other	**1,847**	1,713
	7,883	5,892

The majority of the above balances are RR denominated and do not incur interest.

20. Provisions

During 2006 the following movements of provisions took place:

	Warranty		Taxation provision		Total	
	31 December 2006	31 December 2005	**31 December 2006**	31 December 2005	**31 December 2006**	31 December 2005
Beginning of the period	**1,253**	1,208	**-**	286	**1,253**	1,494
Utilised	**(1,302)**	(1,367)	**-**	(286)	**(1,302)**	(1,653)
Additional provision	**1,594**	1,412	**1,591**	-	**3,185**	1,412
End of the period	**1,545**	1,253	**1,591**	-	**3,136**	1,253
Short-term portion	**1,259**	1,024	**1,591**	-	**2,850**	1,024
Long-term portion	**286**	229	**-**	-	**286**	229
	1,545	1,253	**1,591**	-	**3,136**	1,253

The Group undertakes to repair vehicles or replace certain components that fail to perform satisfactorily during two years after sale or until a mileage of 35,000 kilometres is reached, whichever comes first. At 31 December 2006 a warranty provision was made based on the past experience of the level of repair and returns.

(In millions of Russian Roubles)

20. Provisions (continued)

As at 31 December 2006 the balance of taxation provisions of RR 1,591 relates to JSC AVTOVAZ's ongoing legal proceedings in relation to decisions of tax authorities on additional taxes, fines and penalties accrued as a result of management's assessment of recent tax audits. As disclosed in Note 38, after the balance sheet date the Russian Federation Tax Service following a review of appeals filed by JSC AVTOVAZ reduced the tax claim against JSC AVTOVAZ. This settlement has been treated as a non-adjusting post balance sheet event in accordance with IAS 10, 'Events after the balance sheet date'.

21. Debt

Short-term debt by currency consists of the following:

Currency	Effective interest rate	**31 December 2006**	31 December 2005
RR	12.9%	**24,407**	12,834
EURO	4.9%	**1,898**	1,102
CHF	6.5%	**98**	99
US$	15.5%	**14**	3,524
		26,417	17,559

Fair value of short-term debt is not materially different from its carrying value.

Included in short-term debt are issued bonds of JSC AVTOVAZ for a total of RR 7,960. In 2004 the Company completed the issue of RR 3,000 Rouble denominated documentary coupon bearer bonds maturing in 2008. The bonds were issued at a par value of 1,000 Roubles each. These bonds carried nine half yearly coupons. The rate of the first coupon, which was determined at the auction, was 11.78% per annum, the second coupon's rate is 11.28%, the rate of the third coupon is 10.78%, and the rate of the fourth, the fifth and the sixth coupons is determined at 9.2% each. Following an offer on 16 February 2007 substantially all of the convertible interest-bearing documentary coupon bearer bonds for a total of RR 2,960 were acquired. As a result, these bonds in the amount of RR 2,960 were recorded within short-term debt as at 31 December 2006. The Group determined the interest rate for the bonds amounting to RR 40, which was 1%.

On 28 June 2005, the Company completed the issue of RR 5,000 Rouble denominated documentary coupon bearer bonds. The bonds are issued at par value of 1,000 Roubles each and mature in 5 years. The rate for the first two coupons, which was determined at the auction, was 9.7% per annum, the rate of the third and the fourth coupons was 7.8% each, and the rate of the fifth and the sixth coupons was 7.7% each. The coupon rates of the seventh to tenth coupons are set by the Company. Each time the Group is setting a new interest rate, bond holders have an option to redeem the securities. In June 2007 the Group set a new interest rate for two coupon periods (fifth and the sixth) ending in June 2008 for the RR 5,000 bonds.

Since the Group does not have an unconditional right to defer settlement of the liability for at least twelve months after the balance sheet date, the above bonds were classified as short-term debt as at 31 December 2006. Though these bonds have been classified as short-term, it is the Group's intention to manage the interest rates on these bonds so that there will be no cash outflow from the Group in relation to these bonds before their maturity dates.

Long-term debt by currency consists of the following:

Currency	Effective interest rate	**31 December 2006**	31 December 2005
US$	8.5%	**6,584**	7,196
RR	9.1%	**3,630**	9,373
EURO	4.9%	**1,175**	1,385
CHF	6.5%	**195**	298
		11,584	18,252

Short-term and long-term debt comprises debt at fixed interest rates.

(In millions of Russian Roubles)

21. Debt (continued)

Long-term debt is repayable as follows:

	31 December 2006	31 December 2005
Current portion of debt	**10,700**	5,204
1 to 2 years	**9,639**	5,656
2 to 3 years	**842**	10,967
3 to 4 years	**347**	948
4 to 5 years	**360**	354
Over 5 years	**396**	327
Total long-term debt	**22,284**	23,456
Less portion of current debt	**(10,700)**	(5,204)
Long-term portion of debt	**11,584**	18,252

Included in long-term debt are rouble denominated interest-free bearer promissory notes maturing between 2017 and 2030. These notes are recorded at amortised cost of RR 396 (31 December 2005: RR 320) and calculated using original effective interest rates ranging between 21% and 30%. Their gross nominal value is RR 9,129 (31 December 2005: RR 9,129).

As at 31 December 2006, the fair value of long-term and short-term debt was estimated to be RR 39,856 including RR 31,858 of fair value calculated using current market interest rates of 10% and RR 7,998 using the market value of the Company's bonds. As at 31 December 2005, the fair value of these liabilities was estimated to be RR 37,223 including RR 29,103 of fair value calculated using current market interest rates of 10% and RR 8,120 using the market value of the Company's bonds.

As at 31 December 2006 and 2005 the Group's debt of RR 15,032 and RR 16,559, respectively, including short-term debt was guaranteed by inventories, equipment, buildings, promissory notes, securities and receivables. The carrying amounts of inventories pledged as security are RR 4,800 and RR 3,242, respectively; of equipment pledged as security are RR 5,456 and RR 4,265, respectively; of buildings pledged as security are RR 3,527 and RR 2,880, respectively; of promissory notes and securities pledged as security are RR 797 and RR 1,038, respectively; and of receivables pledged as security are RR 170 and RR 548, respectively, other of RR 1,772 and RR 1,784 respectively.

During 2006 the Group has also sold and repurchased 1,205,000 ordinary shares (see Note 6.1) under repo agreements. Total funds borrowed and repaid under these repo agreements, which were accounted for as a collaterised borrowings, amounted to RR 1,729.

22. Taxes other than income tax

Taxes payable – current other than income tax

Current taxes payable comprise the following:

	31 December 2006	31 December 2005
Current portion of restructured taxes	**1,503**	1,562
Property and other taxes	**711**	570
Social taxes	**621**	514
Value added tax	**228**	565
Penalties and interest on property and other taxes	**151**	149
	3,214	3,360

The principal tax liabilities past due accrue interest at one three hundredth of the current refinancing rate of the Central Bank of Russia. At 31 December 2006 the effective interest rate which was used to accrue penalties amounted to 14% per annum (31 December 2005: 16% per annum). At 31 December 2006 there are no tax liabilities (fines, penalties) past due.

Long-term taxes payable

Long-tem taxes payable comprise various taxes payable to the Russian Government which were previously past due and which have been restructured to be repaid over a period of up to 10 years following the application of the Russian Government Resolutions No. 1002 dated 3 September 1999 "Terms of the restructuring of payables to the Federal Budget" and No. 927 dated 29 December 2001 "On changes of terms of JSC AVTOVAZ's tax liabilities and accrued fines and interest payable to the Federal Budget", as discussed further.

(In millions of Russian Roubles)

22. Taxes other than income tax (continued)

Long-term taxes payable (continued)

The present value of this debt and its maturity profile is as follows:

	31 December 2006	31 December 2005
Current portion of restructured taxes	**1,503**	1,562
1 to 2 years	**468**	538
2 to 3 years	**664**	404
3 to 4 years	**1,514**	582
4 to 5 years	**-**	1,211
Thereafter	**8**	6
Total restructured taxes	**4,157**	4,303
Less current portion of restructured taxes	**(1,503)**	(1,562)
Long-term portion of restructured taxes	**2,654**	2,741

The above liability is carried at amortised cost, calculated by applying the interest rates at inception ranging between 21% and 30%, except for the portion of the tax debt owed to the Federal budget for which the terms were significantly modified during 2005. The carrying value at 31 December 2006 was RR 1,722 calculated by the application of interest rates ranging between 9.6% and 10.7% (31 December 2005: RR 1,859).

As at 31 December 2006, fair value of the long-term portion of restructured taxes was estimated to be RR 2,953 using current market interest rate of 10%. As at 31 December 2005, fair value of these liabilities was estimated to be RR 3,168 using current market interest rates of 10%.

In the event of the Company's failure to make current tax payments and payments of restructured tax liabilities by the end of each quarter, the Ministry of Taxes and Duties may, within one month, recommend to the Government to cancel the restructuring agreement and call the entire liability.

23. Share capital

The carrying value of share capital and the legal share capital value subscribed, authorised, issued and fully paid up, consists of the following classes of shares:

	31 December 2006			31 December 2005		
	No. of shares	**Legal statutory value**	**Carrying amount**	No. of shares	Legal statutory value	Carrying amount
Class A preference	4,930,340	2,465	9,861	4,930,340	2,465	9,861
Ordinary	27,194,624	13,597	54,390	27,194,624	13,597	54,390
Total share capital	32,124,964	16,062	64,251	32,124,964	16,062	64,251
Less: treasury share capital						
Class A preference	(314,697)	(157)	(629)	(291,197)	(146)	(582)
Ordinary	(18,087,316)	(9,044)	(36,175)	(16,767,316)	(8,384)	(33,535)
Total treasury share capital	(18,402,013)	(9,201)	(36,804)	(17,058,513)	(8,530)	(34,117)
Total outstanding share capital	**13,722,951**	**6,861**	**27,447**	15,066,451	7,532	30,134

Ordinary shares give the holders the right to vote on all matters within the remit of the General Shareholders' Meeting.

(In millions of Russian Roubles)

23. Share capital (continued)

Class A preference shares give the holders the right to participate in general shareholders' meetings without voting rights except in instances where decisions are made in relation to re-organisation and liquidation of the Company, and where changes and amendments to the Company's charter which restrict the rights of preference shareholders are proposed. Preference shares obtain the right to vote on all matters within the remit of the General Shareholders' Meeting if at the previous Annual Shareholders' Meeting it was decided not to pay a dividend on preference shares even though the Company had statutory net profit for the year.

Preference shareholders are equally entitled to dividends along with holders of ordinary shares on the basis of a resolution of the General Shareholders' Meeting. A resolution regarding the payment and the amount of dividends is taken by the General Shareholders' Meeting upon recommendations of the Board of Directors in view of financial results for the year.

Transactions with treasury shares are described in Note 6.1.

If a dividend paid on one ordinary share in the current year exceeds a dividend that is payable on one preference share, then a dividend paid on one preference share should be increased to a dividend paid on one ordinary share. As such, the preference holders share in earnings along with ordinary holders and thus the preference shares are considered participating shares for the purpose of the calculation of earnings per share.

In 2006, a dividend was declared and paid in respect of 2005 to holders of preference shares of 5.7 Roubles per preference share (2005: 23 Roubles) and to holders of ordinary shares of 5.7 Roubles per ordinary share (2005: 23 Roubles).

24. Net sales

The components of net sales revenue were as follows:

	2006	2005
Finished vehicles and assembly kits of own production	**138,337**	120,480
Automotive components of own production	**11,993**	10,633
Dealership sales of other producers' vehicles	**20,001**	16,742
Other sales	**13,762**	11,759
	184,093	159,614

	2006	2005
Domestic sales	**141,524**	124,331
Sales in EU countries	**20,943**	18,344
Other sales	**21,626**	16,939
	184,093	159,614

25. Cost of sales

The components of cost of sales were as follows:

	2006	2005
Materials and components, goods for resale	**120,493**	106,217
Labour costs	**20,413**	16,548
Production overheads and other expenses	**8,030**	6,400
Depreciation	**6,737**	5,774
Social expenditure	**1,197**	935
Reversal of provision for impairment of property, plant and equipment (see Note 13)	**(484)**	(464)
Loss on impairment of property, plant and equipment (see Note 13)	**252**	382
Changes in inventories of finished goods and work in progress	**(3,744)**	(759)
	152,894	135,033

(In millions of Russian Roubles)

26. Administrative expenses

Administrative expenses comprise:

	2006	2005
Labour costs	**7,597**	6,591
Local and regional taxes	**2,066**	1,633
Third parties services	**843**	550
Materials	**736**	770
Transportation	**629**	761
Bank services	**398**	287
Depreciation	**409**	474
Repair expenses	**223**	278
Provision for impairment of trade receivables	**(254)**	121
Provision for impairment of other current assets	**194**	122
Other	**1,422**	1,236
	14,263	12,823

27. Distribution costs

Distribution costs comprise:

	2006	2005
Transportation	**3,634**	3,289
Advertising	**1,326**	1,540
Labour costs	**902**	715
Materials	**733**	526
Depreciation	**95**	69
Other	**983**	910
	7,673	7,049

28. Research expenses

Research expenses comprise:

	2006	2005
Labour costs	**106**	234
Amortisation	**31**	78
Materials	**15**	51
Other	**53**	85
	205	448

29. Other operating income, net

The components of other operating income/(expenses) were as follows:

	2006	2005
Interest income – subsidiary bank ZAO CB ABD	**968**	845
Interest income – other	**373**	174
Gain from loan interest expenses refund from Federal Budget	**278**	-
Gain/(loss) from disposal of property, plant and equipment	**237**	(168)
Gain on disposal of long-term financial assets, subsidiaries and associates	**200**	170
Extinguishment of payables	**127**	40
Taxation provision	**(1,591)**	286
Loss on impairment of financial assets	**(125)**	(45)
Net foreign exchange loss	**(96)**	(58)
Other operating income/(expenses)	**(61)**	(520)
	310	724

(In millions of Russian Roubles)

30. Finance costs, net

Finance costs, net, charged to the consolidated income statement comprise:

	2006	2005
Interest expense	**4,153**	4,079
Foreign exchange loss	**120**	804
Foreign exchange gain	**(1,065)**	(493)
	3,208	4,390

31. Expenditure/(income) by nature

	2006	2005
Materials and components, goods for resale	**121,977**	107,564
Labour costs	**29,018**	24,088
Production overheads	**8,030**	6,400
Depreciation and amortisation	**7,272**	6,395
Transportation	**4,032**	4,050
Local and regional taxes	**2,066**	1,633
Taxation provision	**1,591**	(286)
Advertising	**1,326**	1,540
Social expenditure	**1,197**	935
Third parties services	**843**	550
Bank services	**398**	287
Repair expenses	**223**	278
Provision for impairment of trade receivables	**(254)**	121
Provision for impairment of other current assets	**194**	122
Changes in inventories of finished goods and work in progress	**(3,744)**	(759)
Interest income – subsidiary bank ZAO CB ABD	**(968)**	(845)
Reversal of provision for impairment of property, plant and equipment	**(484)**	(464)
Loss on impairment of property, plant and equipment	**252**	382
(Gain)/loss from disposal of property, plant and equipment	**(237)**	168
Other	**1,993**	2,470
	174,725	154,629

32. Income tax

	2006	2005
Income tax expense – current	**3,540**	1,963
Deferred tax (income)/expense	**(369)**	200
	3,171	2,163

(In millions of Russian Roubles)

32. Income tax (continued)

The tax charge of the Group is reconciled as follows:

	2006	2005
IFRS profit before taxation in the Group's consolidated financial statements	**6,695**	1,490
Theoretical tax charge at statutory rate of 24% (2005: 24%)	**1,607**	358
Tax effect of items which are not deductible or assessable for taxation purposes:		
Non-taxable income:		
Net gain from forgiveness of tax debt	**-**	(190)
Share of associates' income	**(128)**	(25)
Non-deductible expenses:		
Losses of non-production divisions of the Company and other expenses	**773**	1,001
Social expenses	**437**	332
Taxation provision	**382**	-
Amortisation of the long-term portion of restructured tax	**70**	194
Non-deductible research and development costs	**39**	294
Provision for deferred tax asset	**(9)**	199
Income tax expense	**3,171**	2,163

During 2006 most of the Group's entities were subject to tax rates of 24% on taxable profits. Deferred tax assets/liabilities are measured at the rate of 24% as at 31 December 2006 (24% as at 31 December 2005).

Deferred tax assets and liabilities

	31 December 2004	Movement for 2005	31 December 2005	Movement for 2006	31 December 2006
Tax effects of temporary differences:					
Provision for impairment of trade receivables	105	71	176	(117)	59
Tax losses carried forward	183	16	199	(9)	190
Non-recognised deferred tax assets	-	(199)	(199)	9	(190)
General and overhead expenses allocation on inventories	(23)	(67)	(90)	(70)	(160)
Effect of inflation and different depreciation rates of property, plant and equipment	(11,173)	(119)	(11,292)	466	(10,826)
Provision for impairment of property, plant and equipment	1,186	20	1,206	(247)	959
Impairment loss on financial assets	(40)	74	34	(3)	31
Accounts payable and provisions	676	(6)	670	263	933
Discounting of long-term debt	(2,141)	(17)	(2,158)	60	(2,098)
Other temporary differences	218	27	245	17	262
Deferred tax liabilities, net	(11,009)	(200)	(11,209)	369	(10,840)

Tax loss carry-forwards, for which a deferred tax asset was recorded, include tax losses in respect of the Company's transactions with securities and operating losses of certain subsidiaries.

The temporary differences associated with undistributed earnings of subsidiaries amount to RR 8,967 and RR 8,190 as of 31 December 2006 and 31 December 2005, respectively. A deferred tax liability on these temporary differences was not recognised because management controls the timing of the utilisation of the temporary differences and believes that they will not be utilised in the foreseeable future.

(In millions of Russian Roubles)

33. Lease payables

Finance lease liabilities - minimum lease payments are as follows:

	31 December 2006	31 December 2005
Not later than one year	**201**	168
1 to 3 years	**148**	64
	349	232
Finance lease servicing	**(90)**	(36)
Present value of finance lease liabilities	**259**	196

Present value of finance lease liabilities and their maturity periods are as follows:

	31 December 2006	31 December 2005
Not later than one year	**146**	137
1 to 3 years	**113**	59
	259	196

Current portion of finance lease liabilities is recorded within Trade payables. The Group purchases computer equipment, packing materials and auto-loaders under finance lease arrangements.

34. Earnings per share

Earnings per share is calculated by dividing the net income attributable to participating shareholders by the weighted average number of ordinary and preference shares in issue during the period, excluding the weighted average number of ordinary shares and preference shares purchased by the Group and held as treasury shares (see Note 23).

Earnings per share has been calculated after taking into account the share split as discussed in post balance sheet events (see Note 38).

	31 December 2006	31 December 2005
Weighted average number of preference shares outstanding (thousands)	**493,034**	493,034
Weighted average number of ordinary shares outstanding (thousands)	**2,719,462**	2,719,462
Adjusted for weighted average number of treasury shares (thousands)	**(1,810,200)**	(1,763,961)
Weighted average number of ordinary and preference shares outstanding (thousands)	**1,402,296**	1,448,535
Profit/(loss) attributable to equity holders	**3,100**	(1,205)
Earnings/(loss) per ordinary share (basic/diluted) (in Roubles)	**2.21**	(0.83)
Earnings/(loss) per preference share (basic/diluted) (in Roubles)	**2.21**	(0.83)

There are no dilution factors therefore basic earnings per share equal diluted earnings per share.

35. Contingencies, commitments and guarantees

35.1 Contractual commitments and guarantees

As at 31 December 2006 the Group had contractual commitments for the purchase of property, plant and equipment from third parties of RR 1,132 (31 December 2005: RR 941). Following IAS 39 and IFRS 4 amendments, the Group has recognised at 31 December 2006 the financial guarantees issued to third parties, in the amount of RR 18 (31 December 2005: RR nil) among its Other payables and accrued expenses. Other than these commitments, there are no other commitments and guarantees in favour of third parties or related companies that are not disclosed in these consolidated financial statements.

The future aggregate minimum lease payments under non-cancellable operating leases of land are as follows:

	2006	2005
Not later than 1 year	**254**	231
Later than 1 year and not later than 5 years	**820**	635
Later than 5 years	**1,901**	725
	2,975	1,591

The amount of lease payments recognised as an expense for the year ended 31 December 2006 was RR 254 (2005: RR 231).

As at 31 December 2006 the Group has other operating lease commitments of RR 626 (31 December 2005: RR 551).

35. Contingencies, commitments and guarantees (continued)

35.2 Tax contingencies

Russian tax 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 authorities.

The Russian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. The Supreme Arbitration Court issued guidance to lower courts on reviewing tax cases providing a systemic roadmap for anti-avoidance claims, and it is possible that this will significantly increase the level and frequency of tax authorities scrutiny.

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

The Group includes companies incorporated outside of Russia. Tax liabilities of the Group are determined on the assumptions that these companies are not subject to Russian profits tax because they do not have a permanent establishment in Russia. Russian tax laws do not provide detailed rules on taxation of foreign companies. It is possible that with the evolution of the interpretation of these rules and the changes in the approach of the Russian tax authorities, the non-taxable status of some or all of the foreign companies of the Group in Russia may be challenged. The impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial condition and/or the overall operations of the entity.

Russian tax legislation does not provide definitive guidance in certain areas. From time to time, the Group adopts interpretations of such uncertain areas that reduce the overall tax rate of the Group. As noted above, such tax positions may come under heightened scrutiny as a result of recent developments in administrative and court practices; the impact of any challenge by the tax authorities cannot be reliably estimated; however, it may be significant to the financial condition and/or the overall operations of the entity.

35.3 Insurance policies

The Group holds no insurance policies in relation to its assets, operations, or in respect of third party liability or other insurable risks.

35.4 Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Expenditures which extend the life of the related property or mitigate or prevent future environmental contamination are capitalised. Potential liabilities which might arise as a result of stricter enforcement of existing regulations, civil litigation or changes in legislation or regulation cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believe that there are no significant liabilities for environmental damage.

35.5 Legal proceedings

During 2006, the Group 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 adverse effect on the result of operations or financial position of the Group.

36. Operating environment of the Group

Whilst there have been improvements in the economic trends in the country, the Russian Federation continues to display certain characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside the Russian Federation, currency controls, and relatively high inflation. The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and changes, which can occur frequently.

The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

37. Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. Transactions between the business segments are on normal commercial terms and conditions. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

(In millions of Russian Roubles)

37. Segment reporting (continued)

The following separate business segments are reported in these consolidated financial statements:

- Automotive - production and sale of vehicles, assembly kits and automotive components of own production and other producers and resale of other producers' vehicles; and
- Banking - Banking activity of ZAO CB ABD and Group's share in OAO National Trade Bank (an associate which is accounted for under the equity method).

Primary segment – operating segments

	Automotive		Banking		Elimination		Total	
	2006	2005	2006	2005	2006	2005	2006	2005
Revenue	184,093	159,614		-	-	-	184,093	159,614
Interest income – subsidiary bank ZAO CB ABD	-	-	968	845	-	-	968	845
less inter-segment income	-	-	87	63	(87)	(63)	-	-
			1,055	908	(87)	(63)	968	845
Segment results	8,618	4,414	750	571	-	-	9,368	4,985
Finance costs, net	(3,208)	(4,390)	-	-	-	-	(3,208)	(4,390)
Share of associates' income	505	72	30	32	-	-	535	104
Net gain from forgiveness of tax debt	-	791	-	-	-	-	-	791
Income tax							(3,171)	(2,163)
Profit / (loss) for the year							3,524	(673)
Other								
Depreciation and amortisation	(7,268)	(6,391)	(4)	(4)	-	-	(7,272)	(6,395)
Capital expenditure	6,879	7,134	9	3	-	-	6,888	7,137
Charge for impairment provision and other provisions	(4,378)	(2,082)	(838)	(2,031)	-	-	(5,216)	(4,113)
Reversal of impairment provision and other provisions	3,152	2,162	765	2,076	-	-	3,917	4,238
Segment assets	168,216	167,530	7,582	6,314	(2,738)	(4,063)	173,060	169,781
Investments in associates	1,782	1,590	121	90	-	-	1,903	1,680
Total consolidated assets							174,963	171,461
Segment liabilities	39,848	41,017	4,853	3,954	(2,231)	(3,451)	42,470	41,520
Unallocated liabilities							48,996	47,185
Total consolidated liabilities							91,466	88,705

Segment assets consist primarily of property, plant and equipment and current assets. Segment liabilities comprise operating liabilities and exclude items such as income taxes. Capital expenditures comprise additions to property, plant and equipment.

Substantially all of the Group operation assets are located in the Russian Federation. Sales to different geographical regions are disclosed in Note 24.

38. Post balance sheet events

In May 2007 the Company's Annual Shareholders' Meeting made the following decisions in respect of JSC AVTOVAZ operating results in 2006:

- to pay dividends of 10.3 Roubles per ordinary share and 10.3 Roubles per preference share. Total approved dividends are RR 331;
- to split the Company's shares as a result of which each ordinary registered share of JSC AVTOVAZ with a nominal value of 500 Roubles is converted into 100 (one hundred) ordinary registered shares of JSC AVTOVAZ with nominal value of 5 Roubles and each preference registered share of JSC AVTOVAZ with nominal value of 500 Roubles is converted into 100 (one hundred) preference registered shares of JSC AVTOVAZ with nominal value of 5 Roubles. The shares will be placed through conversion of the stock resulting from the above share split. As of the date of approval of these financial statements the conversion has been carried out and the earnings per share has been adjusted accordingly (see Note 34).

In May 2007 the Annual Shareholders' Meeting of ZAO GM-AVTOVAZ voted for redemption of 65,524 shares and payment to JSC AVTOVAZ RR 804.

On 29 May 2007 the Company issued RR 5,000 Rouble denominated documentary coupon bearer bonds. The bonds are issued at par value of 1,000 Roubles each and mature in 7 years. The rate of the first four coupons was 7.8% per annum. The rates of other coupons are to be determined by the Company.

The Company was fully in compliance with its restructured tax obligations in relation to insurance contributions, penalties payable to state social non-budget funds, having settled the last payment in December 2006 in accordance with the schedule. In accordance with the Russian Government Resolutions No. 699 dated 1 October 2001 and Decision of penalties and fines write off No. 11 dated 16 April 2007 registered by the Interregional Inspectorate of the Federal Tax Service No. 2 for Samarskaya Oblast, restructured penalties payable to the Russian Federation Government Pension Fund and the Russian Federation Government Employment Fund in the amount of RR 1,140 were forgiven.

In accordance with Russian Government Resolution No. 254 dated 5 March 1997, Russian Government Resolution No. 927 dated 29 December 2001 and Decision of penalties and fines write off No. 1 dated 31 May 2007 registered by Interregional Inspectorate of the Federal Tax Service No. 2 for Samarskaya Oblast, restructured fines and penalties on profits tax in amount of RR 500 were forgiven.

On 25 May 2007, the Russian Federation Tax Service following a review of appeals filed by JSC AVTOVAZ reduced the tax claim against JSC AVTOVAZ to RR 255. In June 2007 JSC AVTOVAZ paid RR 255 in respect of this reduced claim. A taxation provision of RR 1,591 is reflected on the consolidated balance sheet as of 31 December 2006 (see Note 20). This matter is considered to a non-adjusting post balance sheet event.