

Mechel OAO  
Form 20-F  
June 23, 2009

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Form 20-F**

- o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b)  
OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**
  - or**
- o ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2008**
  - or**
- o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**
  - or**
- o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission file number 333-119497**

**MECHEL OAO**

*(Exact name of Registrant as specified in its charter)*

**RUSSIAN FEDERATION**

*(Jurisdiction of incorporation or organization)*

**Krasnoarmeyskaya Street 1, Moscow 125993, Russian Federation**

*(Address of principal executive offices)*

**Securities registered or to be registered pursuant to Section 12(b) of the Act:**

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
AMERICAN DEPOSITARY SHARES, EACH ADS REPRESENTING ONE COMMON SHARE	NEW YORK STOCK EXCHANGE
COMMON SHARES, PAR VALUE 10 RUSSIAN RUBLES PER SHARE	NEW YORK STOCK EXCHANGE <sup>(1)</sup>

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

**NONE**

*(Title of Class)*

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

**NONE**

*(Title of Class)*

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

416,270,745 common shares (including 115,567,933 shares in the form of ADSs)

138,756,915 preferred shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.  Yes  No

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

US GAAP  International Financial Reporting Standards as issued by the International Accounting Standards Board  Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:  Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

(1) Listed, not for trading or quotation purposes, but only in connection with the registration of ADSs pursuant to the requirements of the Securities and Exchange Commission.



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Unless the context otherwise requires, references to "Mechel" refer to Mechel OAO, and references to "our group," "we," "us," or "our" refer to Mechel OAO together with its subsidiaries.

Our business consists of four segments: mining, steel, ferroalloys and power. References in this document to segment revenues are to revenues of the segment excluding intersegment sales, unless otherwise noted.

For purposes of calculating certain market share data, we have included businesses that are currently part of our group that may not have been part of our group during the period for which such market share data are presented.

References to U.S. dollars, \$ or cents are to the currency of the United States, references to rubles or RUR are to the currency of the Russian Federation and references to euro or are to the currency of the member states of the European Union (the E.U. ) that participate in the European Monetary Union.

The term tonne as used herein means a metric tonne. A metric tonne is equal to 1,000 kilograms or 2,204.62 pounds.

Certain amounts that appear in this document have been subject to rounding adjustments; accordingly, figures shown as totals in certain tables or in the text may not be an arithmetic aggregation of the figures that precede them.

CIS means the Commonwealth of Independent States, its member states being Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Matters discussed in this document may constitute forward-looking statements, as defined in the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. We wish to caution you that these statements are only predictions and that actual events or results may differ materially. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. The words believe, expect, anticipate, intend, estimate, forecast, project, will, may, should and similar expressions identify forward-looking statements. Forward-looking statements appear in a number of places including, without limitation, Item 3. Key Information Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects, and include statements regarding:

strategies, outlook and growth prospects;

future plans and potential for future growth;

liquidity, capital resources and capital expenditures;

growth in demand for our products;

economic outlook and industry trends;

developments in our markets;

the impact of regulatory initiatives; and

the strength of our competitors.

The forward-looking statements in this document are based upon various assumptions, many of which are based, in turn, upon further assumptions, including without limitation, management's examination of historical operating trends, data contained in our records and other data available from third parties. Although we believe that these assumptions were reasonable when made, these assumptions are inherently subject to significant uncertainties and contingencies which are difficult or impossible to predict and are beyond our control and we may not achieve or accomplish these expectations, beliefs or projections. In addition to these important factors and matters discussed elsewhere herein, important factors that, in our view, could cause actual results to differ materially from those discussed in the forward-looking statements include the achievement of the anticipated levels of profitability, growth, cost and synergies expected to result from our recent acquisitions, our ability to integrate successfully the ferroalloys segment of our business, the timely development and acceptance of new products, the impact of competitive pricing, the ability to obtain necessary regulatory approvals, the condition of the Russian economy, political stability in Russia, volatility in stock markets or in the price of our shares or American depository shares ( ADSs ), financial risk management, the impact of general business and global economic conditions and other important factors described herein and from time to time in the reports to be filed by us with the Securities and Exchange Commission (the SEC ).

Except to the extent required by law, neither we, nor any of our agents, employees or advisers intend or have any duty or obligation to supplement, amend, update or revise any of the forward-looking statements contained or incorporated by reference in this document.



**Table of Contents****PART I****Item 1. Identity of Directors, Senior Management and Advisers**

Not applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not applicable.

**Item 3. Key Information****Selected Financial Data**

The financial data set forth below as of December 31, 2008, 2007, 2006, 2005 and 2004, and for the years then ended, have been derived from our consolidated financial statements. Our reporting currency is the U.S. dollar and we prepare our consolidated financial statements in accordance with accounting principles generally accepted in the United States ( U.S. GAAP<sup>(1)</sup>).

Our results of operations for the periods presented are significantly affected by acquisitions. Results of operations of these acquired businesses are included in our consolidated financial statements for the periods after their respective dates of acquisition. See note 1(a) to our consolidated financial statements in Item 18. Financial Statements. The financial data below should be read in conjunction with, and are qualified in their entirety by reference to, our consolidated financial statements and related notes included under Item 18. Financial Statements and Item 5. Operating and Financial Review and Prospects.

	<b>Year Ended December 31,</b>				
	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
	<b>(In thousands of U.S. dollars, except share and per share amounts)</b>				
<b>Consolidated statements of income and comprehensive income data:</b>					
Revenue, net	9,950,705	6,683,842	4,397,811	3,804,995	3,635,955
Cost of goods sold	(5,260,108)	(4,166,864)	(2,860,224)	(2,469,134)	(2,225,088)
Gross profit	4,690,597	2,516,978	1,537,587	1,335,861	1,410,867
Selling, distribution and operating expenses	(2,134,328)	(1,119,385)	(811,889)	(820,133)	(660,060)
Operating income	2,556,269	1,397,593	725,698	515,728	750,807
Other (expense) income, net	(1,208,001)	(12,146)	139,135	10,131	794,288
Income before tax, minority interest, discounted operations, extraordinary gain	1,348,268	1,385,447	864,833	525,859	1,545,095
Income tax expense	(118,887)	(356,320)	(230,599)	(136,643)	(175,776)
Minority interest in income of subsidiaries	(88,837)	(116,234)	(31,528)	(6,879)	(11,673)

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Income from continuing operations	1,140,544	912,893	602,706	382,337	1,357,646
Income (loss) from discontinued operations, net of tax		158	543	(1,157)	(15,211)
Extraordinary gain, net of tax					271
Net income	1,140,544	913,051	603,249	381,180	1,342,706
Currency translation adjustment	(227,618)	136,673	148,920	(53,822)	49,116
Change in pension benefit obligation	87,659	(14,365)			
Adjustment of available-for-sale securities	(6,571)	(5,059)	11,203	2,181	(2,350)
Additional minimum pension liability			(4,669)		
Comprehensive income	994,014	1,030,300	758,703	329,539	1,389,472

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	<b>Year Ended December 31,</b>				
	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
	<b>(In thousands of U.S. dollars, except share and per share amounts)</b>				
Earnings per share from continuing operations	2.74	2.19	1.48	0.95	3.63
Loss per share effect of discontinued operations	0.00	0.00	0.00	0.00	(0.04)
Earnings per share effect of extraordinary gain	0.00	0.00	0.00	0.00	0.00
Net income per share	2.74	2.19	1.48	0.95	3.59
Cash dividends per share	1.12	0.76	0.46	0.48	0.01
Weighted average number shares outstanding	416,270,745	416,270,745	408,979,356	403,118,680	373,971,312
<b>Steel segment statements of income and comprehensive income data:</b>					
Revenue, net <sup>(2)</sup>	5,773,719	4,414,492	3,083,654	2,767,028	2,832,189
Cost of goods sold <sup>(2)</sup>	(4,219,344)	(3,374,420)	(2,240,001)	(2,158,499)	(2,065,480)
Gross profit	1,554,375	1,040,072	843,653	608,529	766,709
Selling, distribution and operating expenses	(783,936)	(502,811)	(457,100)	(502,248)	(399,955)
Operating income	770,439	537,261	386,553	106,281	366,754
<b>Mining segment statements of income and comprehensive income data:</b>					
Revenue, net <sup>(2)</sup>	4,031,967	1,970,969	1,354,285	1,270,931	1,053,338
Cost of goods sold <sup>(2)</sup>	(1,229,631)	(1,008,485)	(830,632)	(565,126)	(409,385)
Gross profit	2,802,336	962,484	523,653	705,805	643,953
Selling, distribution and operating expenses	(1,001,796)	(391,015)	(332,612)	(295,512)	(235,876)
Operating income	1,800,540	571,469	191,041	410,293	408,077
<b>Power segment statements of income and comprehensive income data:</b>					
Revenue, net <sup>(2)</sup>	1,028,110	598,515	123,322	24,532	15,907

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Cost of goods sold <sup>(2)</sup>	(714,094)	(393,153)	(110,273)	(20,242)	(13,576)
Gross profit	314,016	205,362	13,049	4,290	2,331
Selling, distribution and operating expenses	(284,610)	(192,735)	(4,400)	(2,172)	(694)
Operating income	29,406	12,627	8,649	2,118	1,637

**Ferroalloys segment statements of income and comprehensive income data:**

Revenue, net <sup>(2)</sup>	584,631	636,656	339,748	156,241	145,367
Cost of goods sold <sup>(2)</sup>	(571,162)	(253,725)	(174,675)	(150,749)	(147,493)
Gross profit (loss)	13,469	382,931	165,073	5,492	(2,126)
Selling, distribution and operating expenses	(63,986)	(32,824)	(17,777)	(20,201)	(23,533)
Operating (loss) income	(50,517)	350,107	147,296	(14,709)	(25,659)

**Consolidated balance sheet data (at period end):**

Total assets	12,009,634	9,227,643	4,457,404	3,600,083	3,678,268
Shareholders' equity	4,030,812	3,504,933	2,864,963	2,210,474	2,057,629
Long-term debt, net of current portion	219,816	2,321,922	322,604	45,615	216,113

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	<b>Year Ended December 31,</b>				
	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>
	<b>(In thousands of U.S. dollars, except share and per share amounts)</b>				
<b>Consolidated cash flows data:</b>					
Net cash provided by operating activities	2,229,941	904,969	554,923	620,875	296,137
Net cash (used in) provided by investing activities	(3,301,083)	(3,410,466)	(552,538)	(994,707)	455,716
Net cash provided by (used in) financing activities	1,298,969	2,549,881	(162,782)	(308,870)	252,269
<b>Non-U.S. GAAP measures<sup>(3)</sup>:</b>					
Consolidated EBITDA <sup>(4)</sup>	2,046,811	1,658,662	1,068,258	726,252	1,707,711
Steel segment EBITDA <sup>(4)</sup>	629,572	709,462	643,499	252,364	1,249,643
Mining segment EBITDA	1,897,012	713,624	277,647	455,528	473,042
Power segment EBITDA	51,769	26,212	9,190	3,211	2,131
Ferroalloys segment EBITDA	(420,074)	323,760	146,141	3,637	(17,105)

- (1) The value of property, plant and equipment pertaining to non-controlling shareholders in the accounting for minority interests resulting from acquisitions of various subsidiaries has been recorded at appraised values rather than at historical cost as required by U.S. GAAP.
- (2) Segment revenues and cost of goods sold include intersegment sales.
- (3) EBITDA represents net income before interest expense, income taxes and depreciation, depletion and amortization. We present EBITDA because we consider it an important supplemental measure of our operating performance and believe it is frequently used by securities analysts, investors and other interested parties in the evaluation of companies in our industry. We also present EBITDA by segment because our overall performance is best explained with reference to results of each segment.

EBITDA has limitations as an analytical tool, and should not be considered in isolation or as a substitute for analysis of our operating results as reported under U.S. GAAP. Some of these limitations are as follows:

EBITDA does not reflect the impact of financing costs, which are significant and could further increase if we incur more debt, on our operating performance.

EBITDA does not reflect the impact of income taxes on our operating performance.

EBITDA does not reflect the impact of depreciation, depletion and amortization on our operating performance. The assets of our businesses which are being depreciated, depleted and/or amortized (including, for example, our mineral reserves) will have to be replaced in the future and such depreciation, depletion and amortization expense may approximate the cost to replace these assets in the future. By excluding such expense from EBITDA, EBITDA does not reflect our future cash requirements for such replacements.

Other companies in our industry may calculate EBITDA differently or may use it for different purposes than we do, limiting its usefulness as a comparative measure.

We compensate for these limitations by relying primarily on our U.S. GAAP operating results and using EBITDA only supplementally. See our consolidated statements of income and comprehensive income and consolidated statements of cash flows included elsewhere in this document.

EBITDA is a measure of our operating performance that is not required by, or presented in accordance with, U.S. GAAP. EBITDA is not a measurement of our operating performance under U.S. GAAP and should not be considered as an alternative to net income, operating income or any other performance measures derived in accordance with U.S. GAAP or as an alternative to cash flow from operating activities or as a measure of our liquidity. In particular, EBITDA should not be considered as a measure of discretionary cash available to us to invest in the growth of our business.

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Reconciliation of EBITDA to net income is as follows for the periods indicated:

	<b>2008</b>	<b>Year Ended December 31,</b>			<b>2004</b>
		<b>2007</b>	<b>2006</b>	<b>2005</b>	
		<b>(In thousands of U.S. dollars)</b>			
<b>Consolidated EBITDA reconciliation:</b>					
Net income	1,140,544	913,051	603,249	381,180	1,342,706
Add:					
Depreciation, depletion and amortization	463,297	290,315	196,227	167,600	137,820
Interest expense	324,083	98,976	38,183	40,829	51,409
Income taxes	118,887	356,320	230,599	136,643	175,776
Consolidated EBITDA	2,046,811	1,658,662	1,068,258	726,252	1,707,711
<b>Steel segment EBITDA reconciliation:</b>					
Net income	229,522	375,115	387,763	59,830	1,014,356
Add:					
Depreciation, depletion and amortization	137,492	124,156	102,257	95,715	81,052
Interest expense	181,536	77,634	26,471	35,158	36,058
Income taxes	81,022	132,557	127,008	61,661	118,177
Steel segment EBITDA	629,572	709,462	643,499	252,364	1,249,643
<b>Mining segment EBITDA reconciliation:</b>					
Net income	1,200,445	403,525	117,803	317,411	351,438
Add:					
Depreciation, depletion and amortization	280,276	136,479	84,167	58,678	49,159
Interest expense	120,594	40,046	11,202	5,361	14,843
Income taxes	295,697	133,574	64,475	74,078	57,602
Mining segment EBITDA	1,897,012	713,624	277,647	455,528	473,042
<b>Power segment EBITDA reconciliation:</b>					
Net income (loss)	3,037	(13,597)	6,066	1,230	1,139
Add:					
Depreciation, depletion and amortization	22,791	16,314	579	1,322	517
Interest expense	31,585	20,332	448	286	
Income taxes	(5,644)	3,163	2,097	373	475

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Power segment EBITDA	51,769	26,212	9,190	3,211	2,131
<b>Ferroalloys segment EBITDA reconciliation:</b>					
Net (loss) income	(283,235)	222,024	99,458	(9,034)	(24,227)
Add:					
Depreciation, depletion and amortization	22,738	13,366	9,224	11,885	7,092
Interest expense	92,611	1,344	440	255	508
Income taxes	(252,188)	87,026	37,019	531	(478)
Ferroalloys segment EBITDA	(420,074)	323,760	146,141	3,637	(17,105)

(4) The 2004 amount includes a gain of \$800.0 million from the sale of our stake in Magnitogorsk Iron & Steel Works OAO ( MMK ).

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The following tables show, for the periods indicated, certain information regarding the exchange rate between the ruble and the U.S. dollar, based on data published by the Central Bank of the Russian Federation (the CBR ).

These rates may differ from the actual rates used in preparation of our financial statements and other financial information provided herein.

Year Ended December 31,	Rubles per U.S. Dollar			Period End
	High	Low	Average <sup>(1)</sup>	
2008	29.38	23.13	24.86	29.38
2007	26.58	24.26	25.58	24.55
2006	28.78	26.18	27.19	26.33
2005	29.00	27.46	28.29	28.78
2004	29.45	27.75	28.81	27.75

(1) The average of the exchange rates on the last business day of each full month during the relevant period.

	Rubles per U.S. Dollar	
	High	Low
May 2009	32.97	30.98
April 2009	34.10	33.17
March 2009	36.23	33.27
February 2009	36.43	34.56
January 2009	35.41	29.39
December 2008	29.38	27.52

The exchange rate between the ruble and the U.S. dollar on June 22, 2009 was 31.15 rubles per one U.S. dollar.

No representation is made that the ruble or U.S. dollar amounts in this document could have been or can be converted into U.S. dollars or rubles, as the case may be, at any particular rate or at all.

**Recent Developments*****Dividends***

As established in March 2006, our dividend policy is to declare and pay an annual dividend on our common shares equal to at least 50% of our annual net income, as determined under U.S. GAAP, subject to any applicable Russian legal restrictions. See Item 8. Financial Information Dividend Distribution Policy for more information. Though we consider our previously announced dividend policy to be still in effect, on June 2, 2009, our Board of Directors recommended to our annual general shareholders meeting an annual dividend of 5.53 rubles per one common share

and 50.55 rubles per one preferred share based on Mechel's operational results for 2008, with the dividend amount allocated to common shares representing approximately 6.6% of net income for 2008. This recommendation is subject to shareholders' approval at our annual general shareholders' meeting scheduled for June 30, 2009.

In ruble terms, the recommendation issued by our Board of Directors breaks down as follows: dividends on outstanding common shares in the amount of 2.3 billion rubles, dividends on outstanding preferred shares in the amount of 7.0 billion rubles and remaining undistributed net profit in the amount of 38.7 billion rubles.

Shareholders are not permitted under Russian law to issue a decision to pay dividends in amounts higher than those recommended by the Board of Directors. If the annual general shareholders' meeting decides to pay dividends, such dividends must be paid in cash by wire transfer not later than December 31, 2009.

**Table of Contents*****Preferred shares***

On April 30, 2008, at an extraordinary shareholders meeting our shareholders adopted amendments to our charter, which were registered with the Russian state unified register of legal entities (as required for the amendments to become effective) on May 7, 2008. Pursuant to our amended charter we are authorized to issue 138,756,915 preferred shares with a nominal value of 10 rubles per share. The authorized preferred shares are not convertible into bonds or other securities, including common shares, of Mechel. Pursuant to a resolution dated May 14, 2008, our Board of Directors decided to increase our charter capital by authorizing Mechel's issuance of 55,000,000 preferred shares with a nominal value of 10 rubles per share. On September 19, 2008, our Board of Directors amended its resolution by increasing the size of the authorized issuance to up to 138,756,915 preferred shares with a nominal value of 10 rubles each and we registered this change with the Russian Federal Financial Markets Service (the "FFMS"). See Item 10. Additional Information Description of Capital Stock and note 20 to our consolidated financial statements in Item 18. Financial Statements.

On April 2, 2009, we placed all 138,756,915 of the preferred shares authorized for issuance at a placement price of 10 rubles per share. All the preferred shares were taken up by our wholly-owned subsidiary Skyblock Limited, ( "Skyblock" ) which was the sole offeree. A report on the placement of the preferred shares was registered with the FFMS on April 14, 2009. On May 7, 2009, we transferred 83,254,149 preferred shares, representing 15% of our share capital, to the sellers of 100% of the shares and interests of U.S. entities Bluestone Industries, Inc., Dynamic Energy, Inc., JCJ Coal Group, LLC, and certain of its West Virginia affiliates as a part of the consideration we provided for our acquisition of the BCG companies. See Acquisition of BCG companies. The remaining preferred shares, representing 10% of our share capital, are held by Skyblock and are considered treasury shares under U.S. GAAP.

***Acquisition of BCG companies***

On May 7, 2009, our subsidiaries closed a transaction to acquire 100% of the shares and interests of U.S. entities Bluestone Industries, Inc., a West Virginia corporation, Dynamic Energy, Inc., a West Virginia corporation, JCJ Coal Group, LLC, a Delaware limited liability company, and certain of its West Virginia affiliates (together the "BCG companies" ), which are privately-held West Virginia-based coal businesses engaged in the mining, processing and sale of premium quality hard coking coal. The aggregate consideration was \$436.4 million paid in cash, approximately 83.3 million preferred shares, plus the assumption of approximately \$132.0 million of net debt. Other business activities conducted by the owners of Bluestone Coal Corp., including steam coal operations in Kentucky and other non-coal operations, are not included in the transaction.

The transaction also includes a contingent share value right ( "CVR" ) that guarantees a target total shareholder return from the preferred shares after five years from May 7, 2009, the closing date. In addition, the transaction consideration includes the obligation to make a contingent cash payment based on additional coal reserves and resources identified within two years under a planned drilling program. Any potential CVR cash payment due to the actual total return from the preferred shares not meeting or exceeding the target return will be paid on the fifth anniversary of the closing date and will equal the amount by which the target value exceeds the sum of the aggregate market value of the preferred shares and all dividends received. The starting target value is \$986.1 million, which could be increased up to \$1.6 billion and/or decreased by amount of any damages (capped at \$200.0 million for CVR purposes) and setoffs effected by Mechel. This increase is based on the additional tonnes of mineral reserves or mineral deposits discovered during the drilling program on certain territories leased or owned by BCG companies.

The contingent cash payment based on the drilling program is an amount based on certain mineral reserves and mineral resources discovered during the drilling program, multiplied by an agreed price of \$3.04 per tonne, which will be paid on the fifth anniversary of the closing date.

The transaction documents contemplate that the parties will conduct a public offering of the preferred shares within four years of the closing date as soon as market conditions are favorable. Mechel Mining will guarantee certain obligations of our subsidiaries. These guarantee obligations are supported by a pledge of the shares of the BCG companies and the newly created Mechel entities that will hold those shares. For a more detailed description of

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the BCG companies acquisition transaction, see note 27 to our consolidated financial statements in Item 18. Financial Statements.

The BCG companies will be included in our mining reporting segment.

## **Risk Factors**

*An investment in our shares and ADSs involves a high degree of risk. You should carefully consider the following information about these risks, together with the information contained in this document, before you decide to buy our shares or ADSs. If any of the following risks actually occurs, our business, financial condition, results of operations or prospects could be materially adversely affected. In that case, the value of our shares or ADSs could also decline and you could lose all or part of your investment.*

### ***Risks Relating to Our Financial Condition and Financial Reporting***

*There is substantial doubt about our ability to continue as a going concern.*

As discussed in detail in note 2 to our consolidated financial statements in Item 18. Financial Statements, because we have significant debt that we do not have the ability to repay without refinancing or restructuring, and our ability to do so is dependent upon continued negotiation with our banks, there is substantial doubt about our ability to continue as a going concern. We also note that we have been in material noncompliance with certain covenants of our major loan agreements with our banks. Our plans concerning these matters, including steps being taken to refinance and/or restructure the terms and conditions of our existing debt to extend maturities beyond 2009, are discussed in note 2 to our consolidated financial statements in Item 18. Financial Statements. Our future is dependent on our ability to refinance or restructure our indebtedness successfully or otherwise address these matters. If we fail to do so for any reason, we would not be able to continue as a going concern and could potentially be forced to seek relief under applicable bankruptcy or insolvency procedures, in which case our shares and ADSs would lose all or a substantial amount of their value. However, given management's plans as outlined in note 2 to our consolidated financial statements in Item 18. Financial Statements, our consolidated financial statements have been prepared on the basis that we will continue as a going concern entity, and no adjustments have been made in our consolidated financial statements to the carrying value of assets and/or liabilities relating to any potential impact of our not being able to refinance our debt obligations.

*Servicing and refinancing of our indebtedness may materially adversely affect our cash flow.*

We have a substantial amount of outstanding indebtedness, primarily consisting of the obligations we entered into in connection with the refinancing of our acquisition of Yakutugol and our acquisition of Oriel Resources. As of December 31, 2008, our consolidated total debt, including capital lease obligations, was \$5,438.3 million, with a short-term portion of \$5,164.3 million (including \$4,233.8 million with a loan covenant violation out of which \$1,563.6 million of the long-term debt was reclassified as short-term debt due to loan covenant violations). Our interest expense for the year ended December 31, 2008 was \$324.1 million, net of the amount capitalized.

Our leverage and the limits imposed by our debt obligations could have significant negative consequences, including limiting our ability to obtain additional financing, constricting our ability to invest in our business and placing us at a possible competitive disadvantage relative to less leveraged competitors which have greater access to capital resources.

We must generate sufficient cash flow in order to meet our debt service obligations and we cannot assure you that we will be able to meet such obligations. If we are unable to generate sufficient cash flow or otherwise obtain funds

necessary to make required payment, we would be in default under our indebtedness, including under cross-default provisions in our loan agreements.

If we do not generate sufficient cash flow from operations in order to meet our debt service obligations, we may have to undertake alternative financing plans to alleviate liquidity constraints, such as refinancing or restructuring our debt, reducing or delaying our capital expenditures or seeking additional capital. We cannot assure that any refinancing or additional financing would be available on acceptable terms. Our inability to generate sufficient cash

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flow to satisfy our debt service obligations or to refinance debt on commercially reasonable terms could materially adversely affect our business, financial condition, results of operations and prospects.

*We will require a significant amount of cash to fund our capital improvements program.*

Our ability to generate cash or obtain financing depends on many factors beyond our control, and we need cash and/or financing to carry out our capital improvements program, which is an important part of our business strategy. We spent \$1.2 billion during 2008 and expect to spend approximately \$840.0 million in 2009 on our capital improvements program. These capital expenditures include investments in Yakutugol OAO ( Yakutugol ), including those required to be made pursuant to the terms of the subsoil license for the undeveloped Elga coal deposit. We plan to spend about \$2.9 billion on our capital improvements program for the four-year period of 2009-2012. See Item 4. Information on the Company Capital Improvements Program. Our ability to fund planned capital expenditures will, in part, depend on our ability to generate cash in the future and possibility for obtaining banking financing. This, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control.

Most of our current borrowings are from Russian and international banks and financial institutions. In the future, we may rely to a greater extent than currently on domestic sources of financing; however, we do not rule out the possibility of attracting financing from foreign capital markets and other foreign financing sources for our capital needs. It is possible that these international sources of financing, as well as Russian sources, may not be available in the future in the amounts we require or may be expensive. To meet our requirements, we will likely need to secure debt financing. However, we may not be able to access international capital markets or attract additional financing to enable us to fund our capital improvements program or fund our other liquidity needs.

International credit markets have experienced, and may continue to experience, high volatility and severe liquidity disruptions stemming from the effects of the current international financial and economic crisis. These and other related events have had a significant impact on the global capital markets, and the reduced liquidity in the global capital markets could limit our ability to diversify our funding sources. Increased funding costs or greater difficulty in diversifying our funding sources might have an adverse effect on our business, financial condition and results of operations. See Risks Relating to the Russian Federation and Other Countries Where We Operate Emerging markets such as Russia are subject to greater risks than more developed markets, and financial turmoil in any emerging market could disrupt our business, as well as cause the price of our shares and ADSs to suffer and Risks Relating to the Russian Federation and Other Countries Where We Operate Economic risks The Russian banking system is still developing, and another banking crisis could place severe liquidity constraints on our business.

*Inflation could increase our costs and decrease operating margins.*

In 2008, the inflation rate was 13.3%, according to the Russian Federal State Statistics Service ( Rosstat ), the highest rate in any of the last five years, including 2007's rate of 11.9%. The prices for many of our products are denominated in U.S. dollars. As we tend to experience inflation-driven increases in certain of our ruble-denominated costs, including salaries, rents and fuel and energy costs, which are sensitive to rises in the general price level in Russia, our costs in U.S. dollar terms will rise, assuming the ruble-to-dollar exchange rate remains constant. See Further volatility in the exchange rate of the ruble against the U.S. dollar may materially adversely affect our results of operations. In this situation, due to competitive pressures, we may not be able to raise the prices we charge for our products sufficiently to preserve operating margins. Accordingly, high rates of inflation in Russia could increase our costs and have the effect of decreasing operating margins.

Wage inflation in Russia has increased our cost of doing business. According to Rosstat, the nominal average monthly wage from January through December 2008 was 25.2% higher than the corresponding period in 2007, and the

inflation-adjusted average monthly wage grew by 9.7% from January through December of 2008, compared to a 17.2% increase during the same period in 2007. If wage inflation in Russia continues to increase, our labor costs will rise and our advantages with respect to our competitors with foreign operations that have historically had to pay higher average wages than those paid by us in Russia will be reduced or eliminated. See The steel, mining and ferroalloy industries are highly competitive, and we may not be able to compete successfully.

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*If we are unable to obtain adequate capital, we may have to limit our operations substantially, which could have a material adverse effect on our business, financial condition and results of operations.*

Among other things, increased levels of indebtedness, and particularly increases in the level of secured indebtedness, could potentially: (1) limit our ability to obtain additional financing; (2) limit our flexibility in planning for, or reacting to, changes in the markets in which we compete; (3) place us at a competitive disadvantage relative to our competitors with superior financial resources; (4) lead to a loss of collateral pledged as security; (5) render us more vulnerable to general adverse economic and industry conditions; (6) require us to dedicate all or a substantial part of our cash flow to service our debt; and (7) limit or eliminate our ability to pay dividends. Our ability to make payments on our indebtedness depends upon our ability to maintain our operating performance at a certain level, which is subject to general economic and market conditions and to financial, business and other factors, many of which we cannot control.

In addition, Russian companies are limited in their ability to effect share placements and have shares in circulation outside of Russia, including in the form of our ADSs and unregistered global depositary shares representing common shares ( GDSs ), due to Russian securities regulations. We have received permission from the FFMS for up to 40% of our common shares to be circulated abroad through depositary receipt programs, which was the maximum volume allowed at that time by Russian law. Current regulations on the procedure for issuance of authorizations on placement and circulation of securities outside the Russian Federation provide that no more than 30% of a Russian company's shares of a particular class or type may be placed and/or circulated abroad. Until recently, this limit was set by the FFMS at 35% and it is unclear whether the FFMS's approval of an amount greater than 35% or 30% prior to the establishment of these lower limits will be respected, or whether the newly enacted 30% limit overrides prior FFMS permissions for higher amounts. Until this is clarified, we have instructed our depositary not to allow for the conversion of more than 35% of our common shares into ADSs and GDSs. Given that our ADSs and GDSs currently account for approximately 35% of our common shares, we cannot raise additional equity financing through placement of common shares in the form of depositary receipts. We have received FFMS permission for a total of 41,627,074 preferred shares to be circulated in the form of global depositary receipts, representing 30% of the total number of preferred shares currently authorized for issuance. Furthermore, it is not clear whether Deutsche Bank Trust Company Americas (the depositary ) may be forced to cancel and convert some of our ADSs and GDSs into a corresponding number of common shares. The Russian government or its agencies may also impose other restrictions on international financings by Russian issuers.

Any of the foregoing factors may limit the amount of capital available to meet our operating requirements. If we cannot obtain adequate funds to satisfy our capital requirements, we may need to limit our operations significantly, which could have a material adverse effect on our business, financial condition and results of operations.

We have merged and intend to continue to merge certain subsidiaries for operational reasons from time to time. Under Russian law, such mergers are considered a reorganization and the merged subsidiaries are required to notify their creditors of this reorganization. Russian law also provides that, for a period of 30 days after such notice, these creditors have a right to file a claim seeking acceleration of the reorganized subsidiaries' indebtedness and demand reimbursement for applicable losses. In the event that we undertake any such merger and all or part of certain of our subsidiaries' indebtedness is accelerated, we and such subsidiaries may not have the ability to raise the funds necessary for repayment and our business and financial condition could be materially adversely affected.

*Further volatility in the exchange rate of the ruble against the U.S. dollar may materially adversely affect our results of operations.*

Our reporting currency is the U.S. dollar. Our products are typically priced in rubles for Russian domestic sales (or in other local currencies for domestic sales outside of Russia, as the case may be) and in U.S. dollars (and, to a lesser

extent, euros) for export sales, whereas the majority of our direct costs are incurred in rubles and, to a lesser extent, in other local currencies where our operations are based. Depreciation in real terms of the ruble against the U.S. dollar results in a decrease in our costs relative to our revenues, while at the same time appreciating our U.S. dollar-denominated liabilities. Appreciation in real terms of the ruble against the U.S. dollar has the opposite effect. In 2008, the ruble depreciated in real terms against the U.S. dollar by 2% as compared with 2007, according

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to Rosstat, and by 1.2% as compared with 2007, according to the Ministry for Economic Development of the Russian Federation.

In the event of an increase in real terms of our dollar-denominated liabilities or our inability to decrease the relative proportion of dollar-denominated liabilities on our balance sheet in favor of ruble-denominated liabilities, further real depreciation of the ruble against the U.S. dollar may materially adversely affect our financial condition. Conversely, appreciation in real terms of the ruble against the U.S. dollar, which was the prevailing trend from 2002-2007, may materially adversely affect our results of operations if the prices we are able to charge for our products do not increase enough to compensate for the increase in real terms in our ruble-denominated expenditures. In order to mitigate such risks we maintain a correlation between our export revenues in foreign currencies and our liabilities in foreign currencies.

*Limitations on the conversion of rubles to foreign currencies in Russia could increase our costs when making payments in foreign currencies to suppliers and creditors and could cause us to default on our obligations to them.*

Many of our major capital expenditures are denominated and payable in various foreign currencies, including the U.S. dollar and euros. Russian legislation currently permits the conversion of ruble revenues into foreign currency without limitation. However, as the Russian authorities may impose limitations on the currency conversion market in the event of an economic or currency crisis, in such an event there may be a delay or other difficulty in converting rubles into foreign currency to make a payment or a delay in or restriction on the transfer of foreign currency. This, in turn, could limit our ability to meet our payment and debt obligations, which could result in the loss of suppliers, acceleration of debt obligations and cross-defaults and, consequently, have a material adverse effect on our business, financial condition and results of operations.

*We could be materially adversely affected if our lenders accelerate our debt due to our current and future failures to comply with our loan agreements.*

The terms of most of our loan agreements under which we or our subsidiaries are borrowers contain various representations, undertakings and provisions regarding events of default, including those related to current litigations and other proceedings, indebtedness, restrictions on payment of dividends, maintenance of certain financial ratios and compliance with applicable laws and regulations. Additionally, many of our loan agreements contain cross-default provisions whereby an event of default under one agreement may in and of itself result in a cross-default under other agreements. Furthermore, according to the terms of such agreements, certain of our actions aimed at developing our business and pursuing our strategic objectives, such as acquisitions, dispositions of assets, restructuring, investments into certain of our subsidiaries and others, require prior consent from the respective lenders.

In 2008 and early 2009, we have been in breach of certain covenants of certain of our loan agreements representing 78.9% of our indebtedness outstanding as of December 31, 2008. Certain of these breaches have been remedied and certain others, particularly relating to maintenance of financial ratios, are continuing. These agreements entitle our lenders to demand accelerated partial or full repayment of outstanding interest and principal. Certain of our loan agreements of which we are in breach contain cross-default provisions. In early 2009 we have received a request from WestLB AG ( WestLB ) addressed to Voskhod Chrome in March 2009 for an early repayment of the outstanding amount of \$84.8 million due to the continuing breach of change of control provision, which has not been waived by the lenders, and a number of other financial covenants. We have agreed with WestLB to repay the full amount outstanding on June 30, 2009, which we intend to do on that date. This request for early repayment received from WestLB has not so far resulted in cross-defaults under our other loans. Maintaining the integrity of our debt portfolio materially depends on our ability to negotiate waivers and extensions from our creditors. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources and Item 5. Operating and Financial Review and Prospects Description of Certain Indebtedness.

Our ability to continue to service, repay and refinance our indebtedness and come back into compliance with our financial and other loan covenants will depend on our ability to generate cash in the future and lenders, credit decisions. This, in turn, is subject to general economic, financial, competitive, legislative and other factors that are

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beyond our control. We cannot assure you that our breach of financial and other covenants in our loan agreements will not result in new and renewed demands from our lenders for acceleration of our loan repayment obligations of related litigation, including as a result of cross-defaults. If we fail to come back into compliance with our financial and other loan covenants contained in any of our loan agreements, including compliance with financial ratios or failure to obtain prior consent of lenders for certain actions, or fail to obtain extensions or waivers in respect of our current and future breaches of our loan agreements or amend our loan agreements, such failure could be deemed by the lenders to be an event of default which could result in, among other things, acceleration of repayment of principal and interest under the relevant loan agreement and any other loan agreement under which a default on such instrument would trigger a cross-default, reduced opportunities for future borrowing, debt service obligations in excess of our ability to pay, liability for damages or inability to further develop our business and pursue our strategic objectives, any of which could have a material adverse effect on our business, financial condition, results of operations and prospects and you could lose your entire investment in ADSs and shares if we are forced to seek relief under applicable bankruptcy or insolvency procedures.

*We have had in the past and may still have material weaknesses in our internal control over financial reporting, and we make no assurances that additional material weaknesses will not be identified in the future.*

Management identified six material weaknesses in our internal control over financial reporting as defined in the Exchange Act Rule 12b-2 and Rule 1-02 of Regulation S-X that affected our financial statements for the year ended December 31, 2008. The material weaknesses in our internal control over financial reporting identified for the year ended December 31, 2008 are described in Item 15. Controls and Procedures. Because of the effect of these material weaknesses, our auditors have opined that we have not maintained effective internal control over financial reporting as of December 31, 2008 under Section 404 of the Sarbanes-Oxley Act of 2002.

Notwithstanding the steps we have taken and continue to take that are designed to remedy each material weakness identified in Item 15. Controls and Procedures, we may not be successful in remedying these material weaknesses in the near or long term and we make no assurances that additional significant deficiencies or material weaknesses in our internal control over financial reporting will not be identified in the future. Our failure to implement and maintain effective internal control over financial reporting could result in errors in our financial statements that could result in a restatement of financial statements, cause us to fail to meet our reporting obligations and cause investors to lose confidence in our reported financial information, leading to a decline in the market price of our shares and ADSs.

*We depend on key accounting staff for the preparation of U.S. GAAP financial information. Given the competition for such personnel, we may be unable to retain our key accounting staff, which could disrupt our ability to timely and accurately report U.S. GAAP financial information.*

Our subsidiaries maintain their books and records in local currencies and prepare accounting reports in accordance with local accounting principles and practices. In particular, each of our Russian subsidiaries maintains its books in rubles and prepares separate unconsolidated financial statements in accordance with Russian accounting standards. For every reporting period, we translate, adjust and combine these Russian statutory financial statements to prepare consolidated financial statements prepared in accordance with U.S. GAAP. This is a time-consuming task requiring us to have accounting personnel experienced in internationally accepted accounting standards. We believe there is a shortage in Russia of experienced accounting personnel with knowledge of internationally accepted accounting standards. Moreover, there is an increasing demand for such personnel as more Russian companies are beginning to prepare financial statements on the basis of internationally accepted accounting standards. Such competition makes it difficult for us to hire and retain such personnel, and our key accounting staff may leave us. Under these circumstances, we may have difficulty in remedying the material weaknesses in our internal financial controls identified by our management and in the timely and accurate reporting of our financial information in accordance with U.S. GAAP. See We have had in the past and may still have material weaknesses in our internal control over

financial reporting, and we make no assurances that additional material weaknesses will not be identified in the future.

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***Risks Relating to Our Business and Industry***

*We operate in cyclical industries, and any local or global downturn, whether or not primarily affecting the mining and/or steel industries, may have an adverse effect on our results of operations and financial condition.*

Our mining business sells coal and iron ore. These commodities are traded in markets throughout the world and are influenced by various factors beyond our control, such as global economic cycles and economic growth rates. Prices of these products have varied significantly in the past and could vary significantly in the future. Prolonged declines in world market prices for these products would have a material adverse effect on our revenues.

The steel industry is highly cyclical in nature because the industries in which steel customers operate are cyclical and sensitive to changes in general economic conditions. The demand for steel products thus generally correlates to macroeconomic fluctuations in the economies in which steel producers sell products, as well as in the global economy. The prices of steel products are influenced by many factors, including demand, worldwide production capacity, capacity-utilization rates, raw material costs, exchange rates, trade barriers and improvements in steel-making processes. Steel prices have experienced, and in the future may experience, significant fluctuations as a result of these and other factors, many of which are beyond our control.

Our ferroalloys business sells nickel, ferrosilicon and ferrochrome. These ferroalloy products are primarily used in the manufacture of steel. Thus, market demand for our ferroalloy products is very closely linked with the market for steel and generally follows the cycles of the steel industry.

Power demand depends on its consumption by the real economy. In Russia, the steel and mining industries are major consumers of power and the recent declines in production by steel and mining companies has impacted demand for power. Therefore, the market demand for the power produced by our power business is affected by many of the same factors and cycles that affect our mining and metals businesses. Due to government price regulation and the current shortage of power generation capacity in Russia, reduced demand for power has not impacted power prices. However, as Russian regulated power prices are set in rubles, if power prices are not increased steadily they may decline on a real dollar basis when ruble devaluation and inflation are taken into account.

Prices for our products, including coal, iron ore, metals and power, as well as the prices of coal, iron ore, ferroalloys, power and natural gas and other commodities and materials we purchase from third parties for the production of our products, fluctuate substantially over relatively short periods of time and expose us to commodity price risk. We do not use options, derivatives or swaps to manage commodity price risk. We use our vertically integrated business model and intersegment sales, as well as short-term and long-term purchase and sales contracts with third-party suppliers and customers, to manage such risk. In addition, the length and pricing terms of our sales contracts on certain types of products are affected and regulated by orders issued by Russian antimonopoly authorities. We cannot ensure that our strategies and contracting practices will be successful in managing our pricing risk or that they will not result in liabilities because of future volatility in these markets. If our strategies to manage commodity price risk and the impact of business cycles and fluctuations in demand are not successful, it could have a material adverse impact on our business, results of operations, financial condition and prospects.

*The steel, mining and ferroalloy industries are highly competitive, and we may not be able to compete successfully.*

We face competition from Russian and international steel and ferroalloys manufacturers and mining companies. Recent consolidation in the steel sector globally has also led to the creation of several large steel producers, some of which have greater financial resources and more modern facilities compared to us. We also face price-based competition from steel and ferroalloys producers in emerging market countries, including, in particular, Ukraine and Kazakhstan. Increased competition could result in more competitive pricing and reduce our profitability.

Our competitiveness is based in part on our operations in Russia and other former Eastern Bloc countries having a lower cost of production than competitors in higher-cost locations. We have been facing a consistent upward trend in the past several years in production costs, particularly with respect to wages and transportation. See Recent and potential developments in the Russian rail transportation sector expose us to uncertainties regarding

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transportation costs of raw materials and steel products and Inflation could increase our costs and decrease operating margins. If these production costs continue to increase in the jurisdictions in which we operate, our competitive advantage will be diminished, which could have a material adverse effect on our results of operations and financial condition.

*Successful implementation of our strategy to expand our specialty long product sales and coal sales depends on our ability to increase our export sales of these products.*

While we expect continued growth of demand in the Russian market for specialty long products, our strategy to expand these sales substantially is dependent on our ability to increase our exports of these products to other countries, particularly the E.U. countries. We face a number of obstacles to this strategy, including trade barriers and sales and distribution challenges as well as restrictions imposed by antimonopoly legislation and regulatory orders. See Item 8. Financial Information Litigation Antimonopoly.

Likewise, our strategy to increase our sales of coal, particularly high-grade coking coal, is substantially dependent on our ability to increase our exports of these products from our coal assets in the Russian Far East to other countries, particularly Japan, China, South Korea and other Pacific Rim countries. In order to implement this strategy, we must complete the tasks of expanding the cargo-handling capacity of our Port Posiet OAO ( Port Posiet ) seaport on the Sea of Japan, building a specialized coal transshipment seaport at Vanino in Russia's Far East ( Port Vanino ) and making the capital improvements necessary for the development of our Elga coal deposit. See We will require a significant amount of cash to fund our capital improvements program. Our ability to increase coking coal export volumes is also limited by our ability to first satisfy domestic Russian coal demand, pursuant to a FAS directive issued to us in August 2008. See Regulation by the Federal Antimonopoly Service could lead to sanctions with respect to the subsidiaries we have acquired or established, our prices, our sales volumes or our business practices. If we fail to manage successfully the obstacles and tasks involved in the implementation of our export sales expansion strategy, it could materially adversely affect our prospects.

*If shares of our subsidiary holding companies are listed on a stock exchange, it could entail changes in such companies' management and corporate governance that might affect our integrated business model.*

While we intend to continue to operate as an integrated business, if and when a listing of shares takes place in respect of the subsidiary holding companies we are forming or intend to form to consolidate our mining and ferroalloy assets, changes to the management structure of such subsidiary holding companies and/or the assets consolidated within them may be made in preparation for such a listing. After a listing of a subsidiary holding company, the subsidiary's directors and management would operate the business of such subsidiary, in accordance with applicable law, for the benefit of all shareholders, including minority shareholders. In addition, companies listed on stock exchanges comply with certain corporate governance requirements and are encouraged to implement certain corporate governance recommendations, including the appointment of independent directors. These and other changes, if implemented in connection with the consolidation and potential listing of subsidiaries holding our mining and/or ferroalloy assets, may result in decision-making by the directors and management of such subsidiaries that may not be consistent with our current integrated business model. As our integrated business model is key to our strategy, changes in decision-making by our subsidiaries' directors and management in connection with a listing may materially adversely affect our business and prospects.

*Our business strategy envisions additional acquisitions and continued integration, and we may fail to identify suitable targets, acquire them on acceptable terms, identify all potential liabilities associated with them or successfully integrate them into our group.*

Our strategy relies on our status as an integrated mining, steel, ferroalloys and power group, which allows us to benefit from economies of scale, realize synergies, better satisfy the needs of our Russian and international customers, reduce our reliance on third party brokers by distributing and selling our products directly to end users, and compete effectively against other mining, steel, ferroalloys and power producers. We also intend to enhance the profitability of our business by applying our integration strategy to a larger asset base and, towards that end, on an ongoing basis we need to identify suitable targets that would fit into our operations, acquire them on terms

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acceptable to us and successfully integrate them into our group. We often compete with Russian and international companies for acquisitions, including subsoil licenses.

The acquisition and integration of new companies pose significant risks to our existing operations, including:

additional demands placed on our senior management, who are also responsible for managing our existing operations;

increased overall operating complexity of our business, requiring greater personnel and other resources; and

incurrence of debt to finance acquisitions and higher debt service costs related thereto, including, if necessary, upgrade costs of such assets.

In addition, integrating new acquisitions may require significant initial cash investments. Furthermore, even if we are successful in integrating our existing and new businesses, expected synergies and cost savings may not materialize, resulting in lower than expected profit margins.

We have acquired and established businesses in countries that represent new operating environments for us and which are located at a great distance from our headquarters in Russia. These businesses conduct operations in accordance with local customs and laws. For example, in connection with our recent acquisition of the BCG companies, a group of companies with coal-mining assets and operations in West Virginia, and our establishment of Mechel Bluestone Inc., a Delaware corporation that holds the BCG companies, we now have significant operations, assets and employees in the United States which are subject to U.S. federal and state laws and regulations. See Our existing arrangements with trade unions may not be renewable on terms favorable to us, and our operations could be materially adversely affected by a worsening of labor relations in the future, We have assumed liabilities with respect to postretirement benefits for our U.S. employees, which could be more burdensome if certain factors beyond our control are changed or corrected, Other Countries Where We Operate The BCG companies are subject to extensive U.S. laws, government regulations and other requirements relating to the protection of the environment, health and safety and other matters, which impose significant costs on us. U.S. regulatory agencies have the authority to temporarily or permanently close the BCG companies mines or modify their operations, which could materially adversely affect our business. Our operations may impact the environment or cause or contribute to contamination or exposure to hazardous substances, which could result in material liabilities to us, Other Countries Where We Operate Changes in U.S. regulations and the passage of new legislation in the United States could materially adversely affect the BCG companies operations, increase our costs or limit our ability to produce and sell coal in the United States, Other Countries Where We Operate We must obtain and maintain numerous U.S. governmental permits and approvals for our operations in the United States, which can be costly and time consuming, and our failure to obtain or renew necessary permits and approvals could negatively impact our business, Other Countries Where We Operate We may be subject to significant mine reclamation and closure obligations with respect to our U.S. coal mining operations, Other Countries Where We Operate Extensive environmental regulation in the United States, including the Clean Air Act and similar state and local laws, affect our U.S. customers and could reduce the demand for coal as a fuel source and cause our sales to decline and Other Countries Where We Operate Mining in the Northern and Central Appalachian region of the United States is more complex and involves more regulatory constraints than in other U.S. geographic areas. Thus, it may take some time to implement our operating standards and it is possible that for a certain period of time we may face some uncertainties with respect to the operational and financial needs of these businesses, which may hinder our integration efforts.

In some instances we conduct limited due diligence investigations in connection with our acquisitions and the contractual documentation does not contain representations and warranties and indemnities to protect against unidentified liabilities and other losses. Moreover, these acquired businesses may not have financial reports prepared

under internationally accepted accounting standards. Accordingly, these businesses may face risks that we have not yet identified and that are not described in this document and we may not realize the full benefit of our investment, which could have a material adverse effect on our business and prospects.

For example, in the case of the West Virginia-based BCG companies, which we acquired in May 2009, though we performed a pre-acquisition review of the companies' assets, liabilities, operations, legal matters and financial condition, the transaction was completed very recently and our review of the new acquisition is ongoing. Though we

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believe we have identified in this document the current material risks associated with the BCG companies in the context of our group, we may not have yet fully identified the extent of the historical, current and future costs related to the BCG companies' assets, liabilities, operations, legal matters and financial condition, including health, safety and environmental liability, problems with permits and regulatory compliance, labor issues and potential litigation. As noted above, implementing our operating standards at newly acquired companies takes time, and our assumptions regarding the liability and cost of operating U.S. assets and doing business in the United States are subject to change as we integrate the BCG companies into our group. If more liabilities and costs are associated with the BCG companies' acquisition than we have assumed, including liabilities and costs that affect the calculation of coal reserves owned or controlled by the BCG companies, we may not realize the investment benefits, operational synergies and marketing advantages we expect from the BCG acquisition, which could materially adversely affect our business, results of operations, financial condition and prospects.

*In the event the title to any privatized company we acquired is successfully challenged, we risk losing our ownership interest in that company or its assets.*

Almost all of our Russian assets consist of privatized companies, and our business strategy will likely involve the acquisition of additional privatized companies. The Russian statute of limitations for challenging privatization transactions is three years. However, because Russian privatization legislation is vague, internally inconsistent and in conflict with other legislation, including conflicts between federal and local privatization legislation, and the statute of limitations for challenging certain actions related to privatization may be argued to begin to run only upon the discovery of a violation, many privatizations are vulnerable to challenge. In the event that any title to, or our ownership stakes in, any of the privatized companies acquired by us is subject to challenge as having been improperly privatized and we are unable to defeat this claim, we risk losing our ownership interest in the company or its assets, which could materially adversely affect our business and results of operations.

In addition, under Russian law, transactions in shares may be invalidated on many grounds, including a sale of shares by a person without the right to dispose of such shares, breach of interested party and/or major transaction rules and/or the terms of transaction approvals issued by government authorities, or failure to register the share transfer in the securities register. As a result, defects in earlier transactions in shares of our subsidiaries (where such shares were acquired from third parties) may cause our title to such shares to be subject to challenge.

*The potential implementation by the Russian government of a law requiring companies to purchase or lease the land on which they operate may have a material adverse effect on our financial condition.*

Much of the land occupied by privatized Russian companies, including most of our subsidiaries, was not included in the privatizations of these companies and is still owned by federal, regional or municipal governments. The companies use the land pursuant to a special title of perpetual use whereby they have the right to use the land but do not have the right to alienate such land.

The Land Code of the Russian Federation, as amended, which was enacted on October 25, 2001 (the "Land Code"), requires privatized Russian companies to either purchase or lease the land on which they operate by January 1, 2010. In accordance with the current legislation the repurchase price of land plots held under special title of perpetual use is set in the amount of 2.5% of the cadastral value of such land plots. We estimate that the cost for us to purchase the land on which we operate is \$35.0 million. This estimate excludes certain land plots on which Southern Kuzbass Coal Company OAO ( "Southern Kuzbass Coal Company") operates, which have not been included in the state cadastral valuation. A bill has been introduced in the State Duma, Russia's Parliament, to extend the term of special title of perpetual use up until January 1, 2013. If this bill does not become law and if we are required to purchase the land plots on which we operate by January 1, 2010 as provided under the current Land Code it may have a material adverse effect on our financial condition.

*Increasing prices of electricity and natural gas could materially adversely affect our business.*

In 2008, our Russian operations purchased approximately 1.8 billion kilowatt-hours ( kWh ) of electricity, representing 55% of their needs. Domestic electricity prices are currently regulated by the Russian government, but the government is in the process of liberalizing the wholesale electricity market and moving from regulated pricing

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to a market-based system. This could lead to higher electricity prices. In addition, according to a 2008 long-term macroeconomic forecast made by the Ministry for Economic Development of the Russian Federation, electricity prices for industrial users are expected to reach 6.9 cents per kWh in 2009 and from 10 to 15 cents per kWh by 2020. In 2008, our average cost of electricity was 5.8 cents per kWh. Assuming a price of 6.9 cents per kWh in 2008, our Russian operations would have incurred approximately \$19.8 million in additional costs. Further price increases for electricity may also occur in the future as the industry is controlled to a greater extent by the private sector. If we are required to pay higher prices for electricity in the future, our costs will rise and our business and prospects could be materially adversely affected.

Our Russian operations also purchase significant amounts of natural gas, primarily for the production of electricity at our own co-generation facilities, from Gazprom OAO ( Gazprom ). Gazprom is a government-controlled company and the dominant producer and monopoly transporter of natural gas within Russia. Domestic natural gas prices are regulated by the Russian government. These prices have been rising over the last few years. The average price for industrial consumers was approximately \$65.3 per thousand cubic meters (\$1.9 per thousand cubic feet) in 2008, and increased by 25.0% compared with 2007. Further, Russian domestic natural gas prices are significantly below Western European levels, which presently helps to provide us with a cost advantage over our competitors, an advantage which is expected to diminish as Russian domestic gas prices approach Western European levels. The Ministry for Economic Development of the Russian Federation has forecasted natural gas prices in the range of \$223 to \$224 per thousand cubic meters (\$6.3 to \$6.4 per thousand cubic feet) in 2015. If we are required to pay higher prices for gas in the future, our costs will rise and our business, financial condition and prospects could be materially adversely affected.

*Recent and potential developments in the Russian rail transportation sector expose us to uncertainties regarding transportation costs of raw materials and steel products.*

Railway transportation is our principal means of transporting raw materials and steel products to our facilities and to customers in Russia and abroad. The Russian rail system is controlled by Russian Railways, an open joint-stock company wholly owned by the Russian government. Russian Railways is a state-sanctioned monopoly responsible for the management of all Russian railroads. The Russian government sets domestic rail freight prices and the terms of transportation. These rail freight prices are subject to annual adjustment based on, among other factors, inflation and the funding requirements of Russian Railways' capital investment program, which is in turn affected by the acute need to upgrade Russian Railways' rolling stock, track infrastructure and passenger- and cargo-handling facilities.

Our cargoes are currently transported in the railcars of either Russian Railways or third party owners engaged for transportation, as well as in our own railcars. The most significant railcar owner is Pervaya Gruzovaya Kompaniya OAO ( First Freight Company ), a wholly-owned subsidiary of Russian Railways from which we lease railcars, mainly to transport coal products and iron ore concentrate. At present, only two companies, Russian Railways and First Freight Company, possess a sufficiently extensive railcar fleet to provide for the traffic volumes we plan.

In December 2007, our subsidiary Mecheltrans OOO concluded a contract to arrange transportation and forwarding of cargoes with the railcar fleet owned by First Freight Company. Our freight volume transported by First Freight Company's railcars amounted to 11.0 million tonnes or RUR 7.1 billion in 2008.

In 2008, tariffs were indexed three times, which resulted in a 23% average tariff increase.

Since January 10, 2009, all tariffs have been increased by an additional 5%.

If rail freight prices continue to increase, or if there is a disruption in transportation of our materials and products due to a shortage of available working rolling stock, it could adversely affect our business, financial condition, results of

operations and prospects.

In connection with the downturn in economic activity due to the global financial crisis, recently the shortage of rail freight rolling stock has eased somewhat. However, as the economic situation improves, the rolling stock deficit is expected to worsen, which may negatively affect our business.

On May 6, 2008, an interdepartmental Russian government commission on structural reform of the rail transportation sector, headed by the Russian Ministry of Transportation, approved draft amendments to the Federal

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Law On Rail Transportation for further submission to the State Duma. On February 16, 2009, a committee of the Russian Union of Industrialists and Entrepreneurs considered certain provisions of the draft bill at the organization's convention. The text of the full draft has not been made public. Changes to Russian legislation regulating the rail transportation sector could result in further increases in our freight shipment costs, which in turn could have a material adverse effect on our business, results of operations, financial condition and prospects.

*We face numerous protective trade restrictions in the export of our steel products and ferroalloys, and we may face export duties in the future.*

We face numerous protective tariffs, duties and quotas which reduce our competitiveness in, and limit our access to, particular markets. Several key steel importing countries currently have import restrictions in place on steel products or intend to introduce them in the future. The E.U. has a quota system in place with respect to Russian steel imports, which affected our exports to ten countries in Central and Eastern Europe and the Baltic states (Estonia, Lithuania and Latvia) that joined the E.U. in 2004 as well as to Romania and Bulgaria, which joined the E.U. in 2007. Our sales into the E.U. constituted approximately 24% of our steel segment revenues and approximately 37% of our steel segment export revenues in 2008. The export of our steel into the E.U. is an important part of our growth strategy. If E.U. quotas are not increased in line with our sales growth objectives, our ability to expand our sales in the E.U. and pursue our growth strategy could be limited. In 2008, approximately 12% of our steel segment's export sales revenues were derived from sales of steel products that were subject to import restrictions. In addition, the E.U. has imposed antidumping duties on certain of our steel exports.

Our ferroalloys business is also subject to export restrictions. In February 2008, an antidumping duty in the amount of 17.8% was imposed on exports to the E.U. of ferrosilicon produced by our subsidiary Bratsk Ferroalloy Plant for a period of five years. We did not supply any ferrosilicon to the E.U. in 2008.

See Item 4. Information on the Company Steel Business Trade restrictions and Item 4. Information on the Company Ferroalloys Business Trade restrictions.

*We benefit from Russia's tariffs and duties on imported steel, which may be eliminated in the future.*

Russia has in place import tariffs with respect to certain imported steel products. These tariffs generally amount to 5-15% of value. Almost all of our sales of steel products in Russia were protected by these import tariffs in 2008. In January 2009, the Russian government increased the import duties on certain types of steel products (corrosion-resistant steel and some other steel products) from 5% to 15%. These tariffs and duties may be reduced or eliminated in the future, which could materially adversely affect our revenues and results of operations.

In August 2007, Russia and Ukraine signed an agreement imposing quotas on the export of Ukrainian steel bars to the Russian market. The agreement will be effective through December 31, 2010. The total quota of steel bars from Ukraine to Russia is equal to 1,205,000 tonnes during the effective term of the trade agreement and is divided into annual volumes. We believe that we benefit from this agreement because it prevents subsidized Ukrainian exports from reducing the prices we otherwise could obtain for these products in our domestic markets.

From March 20, 2007, Russia has imposed an antidumping duty on corrosion-resistant steel originating in the E.U. at the rate of \$840 per tonne. The duty, which we believe will benefit us, will be in force for a total of three years.

According to available public information, Russia has taken part in negotiations to join the World Trade Organization (the WTO). Russia's potential future accession to the WTO could negatively affect our business and prospects. In particular, Russia's entry into the WTO may require gradual reduction or elimination of import tariffs and duties on steel products, causing increased competition in the Russian steel market from foreign producers and exporters. See

also Increasing prices of electricity and natural gas could materially adversely affect our business.

*Estimates of our reserves are subject to uncertainties.*

The estimates of our reserves contained in this document are subject to uncertainties. These estimates are based on interpretations of geological data obtained from sampling techniques and projected rates of production in

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the future. Actual production results may differ significantly from reserve estimates. In addition, it may take many years from the initial phase of drilling before production is possible. During that time, the economic feasibility of exploiting a discovery may change as a result of changes in the market price of the relevant commodity.

In addition, the calculation of reserves of the Elga coal deposit, which we acquired in October 2007 along with our acquisition of Yakutugol, is subject to certain risks due to the license obligations and capital costs involved in developing required infrastructure and commencing production and the nature of the undeveloped Elga coal deposit. See Item 4. Information on the Company Mining Business Mineral reserves (coal, iron ore and limestone) Coal.

*We are subject to mining risks.*

Our business operations, like those of other mining companies, are subject to all of the hazards and risks normally associated with the exploration, development and production of natural resources, any of which could result in production shortfalls or damage to persons or property.

In particular, hazards associated with our open pit mining operations include, but are not limited to:

flooding of the open pit;

collapses of the open pit wall;

accidents associated with the operation of large open pit mining and rock transportation equipment;

accidents associated with the preparation and ignition of large-scale open pit blasting operations;

deterioration of production quality due to weather; and

hazards associated with the disposal of mineralized waste water, such as groundwater and waterway contamination.

Hazards associated with our underground mining operations include but are not limited to:

underground fires and explosions, including those caused by flammable gas;

cave-ins or ground falls;

discharges of gases and toxic chemicals;

flooding;

sinkhole formation and ground subsidence; and

other accidents and conditions resulting from drilling, blasting and removing and processing material from an underground mine, including due to human error.

We are at risk of experiencing any and all of these hazards. The occurrence of such hazards could delay production, increase production costs, result in injury to persons or death, and damage to property, as well as liability for us.

Furthermore, the risk of occurrence of these hazards is exacerbated by the significant level of wear of the equipment of our mining enterprises. We are conducting a program of phased replacement and refurbishment of obsolete equipment in order to meet safety requirements at our most dangerous facilities. See Item 8. Financial Information Litigation Environmental and safety.

On May 30, 2008, there was a shaft cave-in at the Lenin underground mine, an asset of our subsidiary Southern Kuzbass Coal Company in Kemerovo region, Russia. Five of our workers were killed and mining operations were suspended for 17 calendar days, resuming on June 16, 2008. The causes of the accident were investigated by the Kemerovo regional office of the Russian Federal Service for Environmental, Technological and Nuclear Supervision ( Rostekhnadzor ). Following its investigation, Rostekhnadzor issued a report. Rostekhnadzor found that the primary cause of the accident was workers gross breach of safety rules.

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On July 29, 2008, a methane flash occurred at the Lenin mine. All 41 miners who were in the area of the explosion were evacuated to the surface; however, 17 persons were injured. Mining operations were suspended for 67 calendar days, resuming on October 4, 2008. The Kemerovo regional office of Rostekhnadzor conducted an investigation and issued a report, finding that the flash was caused by ignition of a hazardous concentration of methane in the atmosphere in a mined-out section of the mine that arose through extraction from methane-containing mine faces.

In 2008, we took steps to improve safety at the Lenin mine. We commissioned safety inspections, improved safety procedures and monitoring and provided our engineering and technical personnel with additional training and instruction on mining safety. After the July 2008 methane flash, we also revised our mining operations plan and production target for the remaining part of 2008. See Item 8. Financial Information Litigation Environmental and safety.

*More stringent environmental laws and regulations or more stringent enforcement of existing environmental laws and regulations in the jurisdictions where we operate may have a significant negative effect on our operating results.*

Our operations and properties are subject to environmental, worker protection and industrial safety and other laws and regulations in the jurisdictions in which we operate. For instance, our operations generate large amounts of pollutants and waste, some of which are hazardous, such as benzapiren, sulfur oxide, sulfuric acid, nitrogen ammonium, sulfates, nitrites and phenicols. Some of our operations result in the creation of hazardous sludges, including sludges containing base elements such as chromium, copper, nickel, mercury and zinc. The creation, storage and disposal of such hazardous waste is subject to environmental regulations, including some requiring the clean-up of contamination and reclamation, such as requirements for cleaning up highly hazardous waste oil and iron slag. In addition, pollution risks and related clean-up costs are often impossible to assess unless environmental audits have been performed and the extent of liability under environmental laws is clearly determinable.

Generally, there is a greater awareness in Russia of damage caused to the environment by industry than existed during the Soviet era. At the same time, environmental legislation in Russia is generally weaker and less stringently enforced than in the E.U. or the United States. However, recent Russian government initiatives indicate that Russia will introduce new water, air and soil quality standards and increase its monitoring and fines for noncompliance with environmental rules. In addition, we are currently assessing whether our Romanian and Bulgarian operations will face higher environmental compliance costs due to the integration of these countries into the E.U. See note 26(c) to our consolidated financial statements in Item 18. Financial Statements.

Based on the current regulatory environment in Russia and elsewhere where we conduct our operations, as of December 31, 2008, we have not created any reserves for environmental liabilities and compliance costs, other than an accrual in the amount of \$71.6 million for asset retirement obligations, consistent with U.S. GAAP requirements. Any change in this regulatory environment could result in actual costs and liabilities for which we have not provided.

Also, in the course, or as a result, of an environmental investigation by Russian governmental authorities, courts can issue decisions requiring part or all of the production at a facility that has violated environmental standards to halt for a 90-day period. We have been cited in Russia for various violations of environmental regulations in the recent past, including during the 2008 financial year, and we have paid certain fines levied by regulatory authorities in connection with these infractions. Though our production facilities have not been ordered to suspend operations due to environmental violations during the respective periods since we acquired or established them, there are no assurances that environmental protection authorities will not seek such suspensions in the future. In the event that production at any of our facilities is partially or wholly suspended due to this type of sanction, our business could suffer and our operating results could be negatively affected.

The assets and operations of our newly acquired BCG companies based in West Virginia are subject to U.S. environmental and other regulatory risks. See [Other Countries Where We Operate](#). The BCG companies are subject to extensive U.S. laws, government regulations and other requirements relating to the protection of the environment, health and safety and other matters, which impose significant costs on us. U.S. regulatory agencies have the authority to temporarily or permanently close the BCG companies' mines or modify their operations,

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which could materially adversely affect our business. Our operations may impact the environment or cause or contribute to contamination or exposure to hazardous substances, which could result in material liabilities to us, Other Countries Where We Operate Changes in U.S. regulations and the passage of new legislation in the United States could materially adversely affect the BCG companies' operations, increase our costs or limit our ability to produce and sell coal in the United States, Other Countries Where We Operate We must obtain and maintain numerous U.S. governmental permits and approvals for our operations in the United States, which can be costly and time consuming, and our failure to obtain or renew necessary permits and approvals could negatively impact our business, Other Countries Where We Operate We may be subject to significant mine reclamation and closure obligations with respect to our U.S. coal mining operations, Other Countries Where We Operate Extensive environmental regulation in the United States, including the Clean Air Act and similar state and local laws, affect our U.S. customers and could reduce the demand for coal as a fuel source and cause our sales to decline and Other Countries Where We Operate Mining in the Northern and Central Appalachian region of the United States is more complex and involves more regulatory constraints than in other U.S. geographic areas.

In addition, we are generally not indemnified against environmental liabilities or any required land reclamation expenses of our acquired businesses that arise from activities that occurred prior to our acquisition of such businesses. See Our business strategy envisions additional acquisitions and continued integration, and we may fail to identify suitable targets, acquire them on acceptable terms, identify all potential liabilities associated with them or successfully integrate them into our group.

*Our business could be adversely affected if we fail to obtain or renew necessary licenses and permits or fail to comply with the terms of our licenses and permits.*

Our business depends on the continuing validity of our licenses and the issuance of new licenses and our compliance with the terms thereof, including subsoil licenses for our mining operations. Regulatory authorities exercise considerable discretion in the timing of license issuance, renewal of licenses and monitoring licensees' compliance with license terms. In particular, subsoil licenses and related agreements typically contain certain environmental, safety and production commitments. See Item 4. Information on the Company Regulatory Matters Russian Regulation Subsoil licensing Maintenance and termination of licenses. If regulatory authorities determine that we have violated the terms of our licenses, it could lead to suspension or termination of our licenses, and to administrative, civil and criminal liability. In addition, requirements imposed by relevant authorities may be costly to implement and result in delays in production. See Item 4. Information on the Company Mining Business Mineral reserves (coal, iron ore and limestone). Accordingly, these factors may seriously affect our ability to operate our business and realize our reserves.

The assets and operations of our newly acquired BCG companies based in West Virginia are subject to risks relating to permits required under U.S. federal and state laws. See Other Countries Where We Operate We must obtain and maintain numerous U.S. governmental permits and approvals for our operations in the United States, which can be costly and time consuming, and our failure to obtain or renew necessary permits and approvals could negatively impact our business.

*Our controlling shareholder has the ability to take actions that may conflict with the interests of the holders of our shares and ADSs.*

Our Chief Executive Officer, Igor Zyuzin, directly and indirectly owns approximately 66.76% of our common shares and may also acquire additional shares from time to time in compliance with current Company's rules. Except in certain cases as provided by the Federal Law On Joint-Stock Companies, dated December 26, 1995, as amended (the Joint-Stock Companies Law), resolutions at a shareholders' meeting are adopted by a simple majority in a meeting at which shareholders holding more than half of the voting shares are present or represented. Accordingly, Mr. Zyuzin

has the power to control the outcome of most matters to be decided by a majority vote at a shareholders meeting and can control the appointment of the majority of directors and the removal of all of the elected directors. In addition, our controlling shareholder is likely to be able to take actions which require a three-quarters supermajority vote of shares represented at such a shareholders meeting, such as amendments to our charter, reorganization, significant sales of assets and other major transactions in case if other shareholders do not participate in the meeting. Thus, our controlling shareholder can take actions that may conflict with the interests of other holders of our shares and ADSs.

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*Our competitive position and future prospects depend on our senior managers and other key personnel.*

Our ability to maintain our competitive position and to implement our business strategy is dependent to a large degree on the services of our senior management team and other key personnel, particularly Mr. Zyuzin, our Chief Executive Officer and controlling shareholder. See Our controlling shareholder has the ability to take actions that may conflict with the interests of the holders of our shares and ADSs and Item 6. Directors, Senior Management and Employees Directors and Executive Officers. Mr. Zyuzin has provided and continues to provide strategic direction and leadership to us.

Moreover, competition in Russia, and in the other countries where we operate, for personnel with relevant expertise is intense due to the small number of qualified individuals and, as a result, we attempt to structure our compensation packages in a manner consistent with the evolving standards of the Russian labor market. The loss or decline in the services of members of our senior management team or an inability to attract, retain and motivate qualified key personnel could have a material adverse effect on our business, financial condition and results of operations.

*Regulation by the Federal Antimonopoly Service could lead to sanctions with respect to the subsidiaries we have acquired or established, our prices, our sales volumes or our business practices.*

Our business has grown substantially through the acquisition and founding of companies, many of which required the prior approval or subsequent notification of the Russian Federal Antimonopoly Service (the FAS) or its predecessor agencies. Relevant legislation restricts the acquisition or founding of companies by groups of companies or individuals acting in concert without such approval or notification. This legislation is vague in certain parts and subject to varying interpretations. If the FAS were to conclude that an acquisition of an existing company or the creation of a new company was done in contravention of applicable legislation and that competition has been limited as a result, it could seek redress, including invalidating the transactions that led to the limitation of competition, obliging the acquirer to perform activities to restore competition, and seeking the dissolution of the company created as a result of reorganization. Any of these actions could materially adversely affect our business and our results of operations.

As of April 22, 2009, nine of our companies were included by the FAS in its register of entities with a market share exceeding 35% in the relevant market or with a dominant position on a certain market, including:

*Beloretsk Metallurgical Plant OAO* as controlling 100% of the market for local telephony services in the city of Beloretsk;

*Chelyabinsk Metallurgical Plant OAO ( Chelyabinsk Metallurgical Plant )* as controlling more than 65% of the market for forgings made of stainless steel ingots in the Russian market;

*Southern Urals Nickel Plant OAO ( Southern Urals Nickel Plant )* as controlling more than 65% of the market for nickel in sulfate and hydroxide in the Russian Federation;

*Izhstal OAO ( Izhstal )* as controlling more than 65% of the market for graded high-speed steel and its substitute and the market for small shaped graded high-speed steel in the Russian Federation;

*Vyartsilya Metal Products Plant ZAO ( Vyartsilya Metal Products Plant )* as controlling more than 65% of the market of railroad transportation of cargo for third parties and companies on the track section from Vyartsilya village to Vyartsilya station;

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*Kuzbass Power Sales Company OAO ( Kuzbass Power Sales Company )* as controlling more than 50% of the electricity trading market in the Kemerovo region;

*Mechel-Energo OOO ( Mechel-Energo )* as controlling more than 50% of the market for the trading of electricity in the cities of Mezhdurechensk, Myski and Novokuznetsk;

*Yakutugol OAO*, including its subsidiaries *Dzhebariki-Khaya Mine OAO* and *Kangalassk Open Pit Mine OAO* as controlling more than 65% of the coal market of the Sakha Republic (an administrative region of Russia in eastern Siberia, also known as Yakutia) and as holding a dominant market position as the sole

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supplier of Far East Generating Company OAO ( Far East Generating Company ), a power plant designed to consume only the type of coal produced by Yakutugol and its subsidiaries; and

*Moscow Coke and Gas Plant OAO* as controlling 100% of the market for cargo transportation services on the company's rail siding in the Lenin District of Moscow region from the Obmennaya station to the Zavodskaya station.

When our companies are included in the register of entities with a market share exceeding 35% in the relevant market or with a dominant position on a certain market, this does not by itself result in restriction of the activities of such entities. However, these entities may be subject to additional FAS oversight by reason of their having been deemed to have a dominant market position.

In 2008, in furtherance of the FAS's mandate to exercise state control over economic concentration, the FAS considered applications made by our companies with the aim of obtaining permissions required under Russian law and issued a number of directives to a number of our companies placing certain restrictions on our business practices.

On April 14, 2008, the FAS issued a directive ordering Yakutugol, Southern Kuzbass Coal Company and Mechel-Invest OOO ( Mechel-Invest ), as a group of companies holding a dominant position on the Russian coking coal market, to fulfill the following requirements:

to support certain production volumes and product lines;

to provide, to the extent possible, equal supply terms to all customers without discrimination against companies not forming part of the Mechel-Invest group of companies;

not to restrict other companies from supplying coking coal to the same geographical area of operations; and

to notify the FAS prior to any increase in domestic prices of coking coal, steam coal and coking coal concentrate, if such increase amounts to more than 10% of the relevant price used 180 days before the date such increase is planned to take place, with submission to the FAS of the financial and economic reasoning for the planned increase of prices.

The above directive is not in effect currently as Mechel-Invest does not hold Yakutugol's shares as of June 30, 2008, and was liquidated by a way of the merger to Mechel Trading House on December 31, 2008.

A new directive with substantially identical requirements was issued to Mechel, Southern Kuzbass Coal Company and Korshunov Mining Plant OAO ( Korshunov Mining Plant ) on May 13, 2008, as described below.

Additionally, on March 6, 2008, we received from the FAS two directives relating to the same subsidiaries as the May 13, 2008 directive, with one of them also being addressed to Elgaugol. These directives lost effect. However, on October 10, 2008, the FAS issued new directives to Mechel Mining Management ordering Mechel Mining Management, Yakutugol and Southern Kuzbass Coal Company to follow the FAS's requirements in place of the original addressees. These directives contain requirements similar to the ones described in the previous paragraph, except for the requirement for prior notification of contemplated price increases. Under these two directives, the companies are required to provide a justification of increases in the price of coking coal concentrate if the change in price is 10% more than the weighted average price over the previous six months.

Furthermore, in connection with the establishment of Mechel Mining, the subsidiary into which certain mining assets are being consolidated, we received a directive from the FAS dated May 13, 2008, which contains requirements as to

the activities of Mechel, Southern Kuzbass Coal Company and Korshunov Mining Plant, which have been deemed by FAS to be a group of companies holding a dominant position on the Russian coking coal market. The requirements repeat those described above pursuant to the directive issued to Yakutugol, Southern Kuzbass Coal Company and Mechel-Invest on April 14, 2008. Additionally, on June 23, 2008 the FAS issued two more directives, which were addressed to our subsidiary holding company Mechel Mining and relating to its subsidiaries Yakutugol and Southern Kuzbass Coal Company. The requirements under these two directives substantially repeat those described above.

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In addition, in connection with our transfer of management of Beloretsk Metallurgical Plant, Izhstal, Chelyabinsk Metallurgical Plant and Urals Stampings Plant to Mechel Management, in 2008 FAS issued four directives addressed to Mechel Management. Furthermore, in connection with our transfer of management of Southern Urals Nickel Plant and Bratsk Ferroalloy Plant to Mechel Ferroalloys Management and the consolidation of our ferroalloy assets under our subsidiary Oriel Resources, in October 2008 FAS issued two directives addressed to Mechel Ferroalloys Management and one directive addressed to Oriel Resources, and in November 2008 FAS issued one additional directive addressed to Mechel. The requirements under all eight of these directives are substantially similar to those described above, except that they relate to our production and sales of ferrosilicon, nickel products, stampings and certain other steel products.

In the event of breach of the terms of business conduct set forth by the FAS by our companies, the FAS may seek to impose liability for violation of antimonopoly legislation and of administrative legislation, which would materially adversely affect our business and results of operations. Such liability may take the form of an administrative fine of up to 15% of the proceeds of sale of all goods, works and services on the market where such violation, was committed, but not more than 2% of gross proceeds of sale of all goods, works and services. Russian legislation also provides for criminal liability for violations of antimonopoly legislation resulting in damage over one million rubles. Furthermore, for systematic violations a court may order, pursuant to a suit filed by the FAS, a compulsory split-up or spin-off of the violating company, and no affiliation can be preserved between the new entities established as result of such a mandatory reorganization. The imposition of any such liability on us or our subsidiaries could materially adversely affect our business, results of operations, financial condition or prospects.

Negative publicity associated with any antimonopoly, administrative, criminal or other investigation or prosecution carried out with respect to our business practices, regardless of the outcome, could damage our reputation and result in a significant drop in the price of our shares and ADSs and could materially adversely affect our business and prospects.

*In the event that the minority shareholders of our subsidiaries were to successfully challenge past interested party transactions or do not approve interested party transactions in the future, we could be limited in our operational flexibility.*

We own less than 100% of the equity interests in some of our subsidiaries. In addition, certain of our wholly owned subsidiaries have previously had other shareholders. We and our subsidiaries in the past have carried out, and continue to carry out, transactions among our companies and affiliates, as well as transactions with other parties which may be considered to be interested party transactions under Russian law, requiring intra-group approval by disinterested directors, disinterested independent directors or disinterested shareholders depending on the nature of the transaction and the parties involved. See Item 10. Additional Information Interested Party Transactions. The provisions of Russian law defining which transactions must be approved as interested party transactions are subject to different interpretations, and these transactions may not always have been properly approved, including by former shareholders. We cannot make any assurances that our and our subsidiaries applications of these concepts will not be subject to challenge by former and current shareholders. Any such challenges, if successful, could result in the invalidation of transactions, which could have a material adverse effect on our business, financial condition, results of operations or prospects.

In addition, Russian law requires a three-quarters majority vote of the holders of voting stock present at a shareholders meeting to approve certain transactions and other matters, including, for example, charter amendments, reorganization, major transactions involving assets in excess of 50% of the assets of the company, acquisition by the company of outstanding shares and certain share issuances. In some cases, minority shareholders may not approve interested party transactions requiring their approval or other matters requiring approval of minority shareholders or supermajority approval. In the event that these minority shareholders were to challenge successfully past interested

party transactions, or do not approve interested party transactions or other matters in the future, we could be limited in our operational flexibility and our business, financial condition, results of operations or prospects could be materially adversely affected.

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*In the event certain minority shareholder lawsuits are resolved against us, our financial condition and results of operations could be materially adversely affected.*

Russian law does not protect us against, and does not allow us to include in our charter, protections against unfriendly and other similar actions by minority shareholders. For example, minority shareholders holding as little as a single share in a company have standing under Russian law to bring claims against the company, challenge decisions of governing bodies. These features of Russian corporate law are often abused by minority shareholders, who can bring claims in local courts seeking injunctions and other relief for which, as a practical matter, we may not receive notice. Any such actions by minority shareholders, if resolved against us, could have a material adverse effect on our business, results of operations and financial condition.

*Our existing arrangements with trade unions may not be renewable on terms favorable to us, and our operations could be materially adversely affected by a worsening of labor relations in the future.*

As of December 31, 2008, approximately 75% of our employees were represented by trade unions. Although we have not experienced any business interruption at any of our companies as a result of labor disputes from the dates of their respective acquisition by us and we consider our relations with our employees to be good, under Russian law unions have the legal right to strike and other Russian companies with large union representation have been recently affected by interruptions due to strikes, lockouts or delays in renegotiations of collective bargaining agreements. Our businesses could also be affected by similar events if our relations with our labor force and trade unions worsen in the future. Although currently at all our Russian businesses our collective bargaining agreements have been extended for a period of at least one year from the fourth quarter of 2008 to the first quarter of 2009, if employees are dissatisfied with their terms, our business and results of operations could be materially adversely affected.

Our risks relating to trade union relations may be increased by our May 2009 acquisition of the BCG companies. Approximately half of the BCG companies' workforce is represented by the United Mine Workers of America (UMWA) labor union. Though we believe the BCG companies have a good relationship with the UMWA, there are no assurances that our acquisition of the BCG companies will not be detrimental to that relationship. Our U.S. employees have the right at any time under the U.S. National Labor Relations Act to form or affiliate with a union and the current presidential administration in the United States has indicated that it will support legislation that may make it easier for employees to unionize. Any further unionization of employees could adversely affect the stability of our production and reduce our profitability. Additionally, due to the increased risk of strikes and other work-related stoppages that may be associated with union operations in the coal industry, our competitors who operate without union labor may have a competitive advantage in areas where they compete with our unionized operations.

*We have assumed liabilities with respect to postretirement benefits for our U.S. employees, which could be more burdensome if certain factors beyond our control are changed or corrected.*

With the acquisition of the BCG companies, we have assumed long-term liability with respect to pension obligations and postretirement welfare benefit plans. The BCG companies contribute to multiemployer defined benefit pension plans sponsored by the UMWA. In the event of our partial or complete withdrawal from any multiemployer plan which is underfunded, we would be liable for a proportionate share of such plan's unfunded vested benefits. In the event that any other contributing employer withdraws from any plan which is underfunded, and such employer (or any member in its controlled group) cannot satisfy its obligations under the plan at the time of withdrawal, then we, along with the other remaining contributing employers, would be liable for our proportionate share of such plan's unfunded vested benefits. Assessment of withdrawal liability could adversely affect our cash flow and reduce our profitability, and could materially adversely affect our financial condition.

Our postretirement medical obligations have been estimated based on actuarial assumptions, including actuarial estimates, assumed discount rates, estimates of life expectancy, and changes in healthcare costs. If our assumptions relating to these benefits change in the future or are incorrect, we may be required to record additional expenses, which would reduce our profitability. In addition, future regulatory and accounting changes

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relating to these benefits could result in increased obligations or additional costs, which could also have a material adverse impact on our cash flows, results of operations or financial condition.

*We do not carry the types of insurance coverage customary in more economically developed countries for a business of our size and nature, and a significant event could result in substantial property loss and inability to rebuild in a timely manner or at all.*

The insurance industry is still developing in Russia, and many forms of insurance protection common in more economically developed countries are not available in Russia on comparable terms, including coverage for business interruption. At present, most of our Russian production facilities are not insured, and we have no coverage for business interruption or for third-party liability, other than customary insurance coverage against the risks associated with our international trading operations and sales as well as the business in which we operate, other than insurance required under Russian law, collective agreements, loan agreements or other undertakings. Some of our international production facilities are not covered by comprehensive insurance typical for such operations in Western countries. Furthermore, we cannot confirm that the insurance we have in place is adequate for the potential losses and the liability we may suffer.

Since most of our production facilities lack insurance covering their property, if a significant event were to affect one of our facilities, we could experience substantial financial and property losses, as well as significant disruptions in our production activity, for which we would not be compensated by business interruption insurance.

Since we do not maintain separate funds or otherwise set aside reserves for these types of events, in case of any such loss or third-party claim for damages we may be unable to seek any recovery for lost or damaged property or compensate losses due to disruption of production activity. Any such uninsured loss or event may have a material adverse effect on our business, results of operations and financial condition.

*If transactions, corporate decisions or other actions of members of our group and their predecessors-in-interest were to be challenged on the basis of noncompliance with applicable legal requirements, the remedies in the event of any successful challenge could include the invalidation of such transactions, corporate decisions or other actions or the imposition of other liabilities on such group members.*

Businesses of our group, or their predecessors-in-interest at different times, have taken a variety of actions relating to share issuances, share disposals and acquisitions, mandatory buy-out offers, valuation of property, interested party transactions, major transactions, decisions to transfer licenses, meetings of governing bodies, other corporate matters and antimonopoly issues that, if successfully challenged on the basis of noncompliance with applicable legal requirements by competent state authorities, counterparties in such transactions or shareholders of the relevant members of our group or their predecessors-in-interest, could result in the invalidation of such actions, transactions and our corporate decisions, restrictions on voting rights or the imposition of other liabilities. Because applicable provisions of Russian law are subject to many different interpretations, we may not be able to defend successfully any challenge brought against such actions, decisions or transactions, and the invalidation of any of them or imposition of any such liability may, individually or in the aggregate, have a material adverse effect on our business, financial condition and results of operations.

### ***Risks Relating to Our Shares and the Trading Market***

*Because the depositary may be considered the beneficial holder of the shares underlying the ADSs, these shares may be arrested or seized in legal proceedings in Russia against the depositary.*

Because a court interpreting Russian law may not recognize ADS holders as beneficial owners of the underlying shares, it is possible that holders of ADSs could lose all their rights to those shares if the assets of the depositary in Russia are seized or arrested. In that case, holders of ADSs would lose their entire investment.

A court interpreting Russian law may treat the depositary as the beneficial owner of the shares underlying the ADSs. This is different from the way other jurisdictions treat ADSs. In the United States, although shares may be held in the depositary's name or to its order, making it a legal owner of the shares, the ADS holders are the beneficial, or real, owners. In U.S. courts, an action against the depositary would not result in the beneficial

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owners losing their shares. Russian law does not make the same distinction between legal and beneficial ownership, and it may only recognize the rights of the depositary in whose name the shares are held, not the rights of ADS holders, to the underlying shares. Thus, in proceedings brought against a depositary, whether or not related to shares underlying ADSs, Russian courts may treat those underlying shares as the assets of the depositary, open to seizure or arrest.

*Voting rights with respect to the shares represented by our ADSs are limited by the terms of the deposit agreements for the ADSs and relevant requirements of Russian law.*

ADS holders have no direct voting rights with respect to the shares represented by the ADSs. They exercise voting rights with respect to the shares represented by ADSs only in accordance with the provisions of the relevant deposit agreement relating to the ADSs and relevant requirements of Russian law. Therefore, there are practical limitations upon the ability of ADS holders to exercise their voting rights due to the additional procedural steps involved in communicating with them. For example, the Joint-Stock Companies Law and our charter require us to notify shareholders no less than 30 days prior to the date of any meeting and at least 70 days prior to the date of an extraordinary meeting to elect our Board of Directors upon publication of the notice in the Russian official newspaper *Rossiyskaya Gazeta*. Our common shareholders will receive notice directly from us and will be able to exercise their voting rights by either attending the meeting in person or voting by power of attorney.

ADS holders, by comparison, will not receive notice directly from us. Rather, in accordance with the deposit agreement, we will provide the notice to the depositary. The depositary has in turn undertaken, as soon as practicable thereafter, to mail to ADS holders notice of such meeting, copies of voting materials (if and as received by the depositary from us) and a statement as to the manner in which instructions may be given by ADS holders. To exercise their voting rights, ADS holders must then instruct the depositary how to vote their shares. Because of this extra procedural step involving the depositary, the process for exercising voting rights may take longer for ADS holders than for holders of shares. ADSs for which the respective depositary does not receive timely voting instructions will not be voted at any meeting.

In addition, although securities regulations expressly permit the depositary to split the votes with respect to the shares underlying the ADSs, as the case may be, in accordance with instructions from ADS holders, there is little court or regulatory guidance on the application of such regulations, and the depositary may choose to refrain from voting at all unless it receives instructions from all ADS holders to vote the shares in the same manner. Holders of ADSs may thus have significant difficulty in exercising voting rights with respect to the shares underlying the ADSs. There can be no assurance that holders and beneficial owners of ADSs will (1) receive notice of shareholder meetings to enable the timely return of voting instructions to the depositary, (2) receive notice to enable the timely cancellation of ADSs in respect of shareholder actions or (3) be given the benefit of dissenting or minority shareholders' rights in respect of an event or action in which the holder or beneficial owner has voted against, abstained from voting or not given voting instructions.

*The price of our shares and ADSs may be highly volatile.*

The trading prices of our shares and ADSs may be subject to wide fluctuations in response to many factors, including:

fluctuations in our operating results and those of other Russian and international mining, steel, ferroalloys and power companies, for the first quarter of 2009, as was seen after reporting of our operating results;

fluctuations in national and industry growth rates;

actual or anticipated announcements of technical innovations or new products or services by us or our competitors;

changes in governmental legislation or regulation;

general economic conditions within our business sector or in Russia or other countries where we have operations; or

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extreme price and volume fluctuations on the Russian or other emerging market stock exchanges and stock exchanges in developed markets.

*ADS holders may be unable to repatriate their earnings.*

Dividends that we may pay in the future on the shares represented by the ADSs are calculated in Russian rubles and may be declared and paid to the depositary in rubles. Such dividends will be converted into U.S. dollars by the depositary and distributed to holders of ADSs, net of the depositary's fees and expenses. The ability to convert rubles into U.S. dollars is subject to the availability of U.S. dollars in the currency markets. Although there is a developing market for the conversion of rubles into U.S. dollars, including the interbank currency exchange and over-the-counter and currency futures markets, the further development of this market is not guaranteed.

*ADS holders may not be able to benefit from the United States-Russia income tax treaty.*

Under Russian law, dividends paid to a non-resident holder of the shares generally will be subject to Russian withholding tax at a rate of 15%.

Russian tax rules applicable to the holders of the ADSs are characterized by significant uncertainties. The Ministry of Finance of the Russian Federation has expressed its opinion in private rulings that holders of depositary receipts should be treated as the beneficial owners of the dividends paid on underlying shares for the purposes of double tax treaty provisions applicable to taxation of dividend income from the underlying shares, provided that the tax treaty residence of the holders of the depositary receipts is duly confirmed. However, the Russian tax authorities have not provided official, generally applicable guidance addressing how an ADS holder should demonstrate its beneficial ownership in underlying shares. As Russian tax legislation does not specify the form of the documents confirming the status of the beneficiary shareholder in the foreign jurisdiction (e.g., U.S. permanent resident status), the Russian tax authorities have stated that the documents confirming the permanent residence of a foreign company can be documents in any format provided they are officially consularized or apostilled.

Until the Russian tax authorities clarify whether it is permitted under Russian law to withhold Russian withholding tax in respect of dividends a company pays to the depositary at a lower rate than the domestic rate applicable to such payments (currently 15%), we intend to withhold Russian withholding tax at the domestic rate applicable to such dividends, regardless of whether the depositary (the legal owner of the shares) or an ADS holder would be entitled to reduced rates of Russian withholding tax under the relevant income tax treaty if it were the beneficial owner of the dividends for purposes of that treaty. Although non-resident ADS holders may apply for a refund of a portion of the amount so withheld by us under the relevant income tax treaty, no assurance can be made that the Russian tax authorities will grant any refunds. See Item 10. Additional Information Taxation Russian Income and Withholding Tax Considerations for additional information.

*Capital gains from the sale of ADSs may be subject to Russian income tax.*

Under Russian tax legislation, gains realized by non-resident legal entities or organizations from the disposition of Russian shares and securities, as well as financial instruments derived from such shares, such as the ADSs, may be subject to Russian profits tax or withholding income tax if immovable property located in Russia constitutes more than 50% of our assets. However, no procedural mechanism currently exists to withhold and remit this tax with respect to sales made to persons other than Russian companies and foreign companies with a registered permanent establishment in Russia. Gains arising from the disposition on foreign stock exchanges of the foregoing types of securities listed on these exchanges are not subject to taxation in Russia.

Gains arising from the disposition of the foregoing types of securities and derivatives outside of Russia by U.S. holders who are individuals not resident in Russia for tax purposes will not be considered Russian source income and will not be taxable in Russia. Gains arising from disposition of the foregoing types of securities and derivatives in Russia by U.S. holders who are individuals not resident in Russia for tax purposes may be subject to tax either at the source in Russia or based on an annual tax return, which they may be required to submit with the Russian tax authorities.

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*Holders of our ADSs may have limited recourse against us and our directors and executive officers because most of our operations are conducted outside the United States and most of our directors and all of our executive officers reside outside the United States.*

Our presence outside the United States may limit our ADS holders' legal recourse against us. Mechel is incorporated under the laws of the Russian Federation. Most of our directors and all of our executive officers reside outside the United States, principally in Russia. A substantial portion of our assets and the assets of most of our directors and executive officers are located outside the United States. As a result, holders of our ADSs may be limited in their ability to effect service of process within the United States upon us or our directors and executive officers or to enforce in a U.S. court a judgment obtained against us or our directors and executive officers in jurisdictions outside the United States, including actions under the civil liability provisions of U.S. securities laws. In addition, it may be difficult for holders of ADSs to enforce, in original actions brought in courts in jurisdictions outside the United States, liabilities predicated upon U.S. securities laws.

There is no treaty between the United States and the Russian Federation providing for reciprocal recognition and enforcement of foreign court judgments in civil and commercial matters. These limitations may deprive investors of effective legal recourse for claims related to investments in the ADSs. The deposit agreement provides for actions brought by any party thereto against us to be settled by arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association, provided that any action under the U.S. federal securities laws or the rules or regulations promulgated thereunder may, but need not, be submitted to arbitration. The Russian Federation is a party to the United Nations (New York) Convention on the Recognition and Enforcement of Foreign Arbitral Awards, but it may be difficult to enforce arbitral awards in the Russian Federation due to a number of factors, including the inexperience of Russian courts in international commercial transactions, official and unofficial political resistance to enforcement of awards against Russian companies in favor of foreign investors and Russian courts' inability to enforce such orders.

### ***Risks Relating to the Russian Federation and Other Countries Where We Operate***

*We have used certain information in this document that has been sourced from third parties.*

We have sourced certain information contained in this document from independent third parties, including private companies, Russian government agencies and other publicly available sources. We believe these sources of information are reliable and that the information fairly and reasonably characterizes the industry in Russia. However, although we take responsibility for compiling and extracting the data, we have not independently verified this information. In addition, the official data published by Russian federal, regional and local governments may be substantially less complete or researched than those of Western countries. Official statistics may also be produced on different bases than those used in Western countries.

*Emerging markets such as Russia are subject to greater risks than more developed markets, and financial turmoil in any emerging market could disrupt our business, as well as cause the price of our shares and ADSs to suffer.*

Investors in emerging markets such as the Russian Federation should be aware that these markets are subject to greater risk than more developed markets, including in some cases significant legal, economic and political risks. Investors should also note that emerging economies such as the economy of the Russian Federation are subject to rapid change and that the information set out herein may become outdated relatively quickly. Accordingly, investors should exercise particular care in evaluating the risks involved and must decide for themselves whether, in light of those risks, their investment is appropriate. Generally, investment in emerging markets is only suitable for sophisticated investors who fully appreciate the significance of the risks involved and investors are urged to consult with their own legal and financial advisers before making an investment in the shares.

Many financial indices in Russia and other emerging markets, as well as developed markets, have declined significantly since the summer of 2008, and continue to be depressed as of the date of this document. Continued volatility in the United States, Russian and other securities markets stemming from the global financial crisis or other factors may continue to adversely affect the price of our shares and ADSs.

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***Economic risks***

*Economic instability in Russia could adversely affect our business and the value of our shares and ADSs.*

Since the dissolution of the Soviet Union in the early 1990s, the Russian economy has experienced at various times:

significant declines in gross domestic product;

hyperinflation;

an unstable currency;

high government debt relative to gross domestic product;

a weak banking system providing limited liquidity to domestic enterprises;

high levels of loss-making enterprises that continued to operate due to the lack of effective bankruptcy proceedings;

significant use of barter transactions and illiquid promissory notes to settle commercial transactions;

widespread tax evasion;

growth of a black and gray market economy;

pervasive capital flight;

high levels of corruption and the penetration of organized crime into the economy;

significant increases in unemployment and underemployment; and

the impoverishment of a large portion of the population.

Although Russia has benefited from the increase in global commodity prices, providing an increase in disposable income and an increase in consumer spending, the Russian economy has been subject to abrupt downturns in the past. In particular, on August 17, 1998, in the face of a rapidly deteriorating economic situation, the Russian government defaulted on its ruble-denominated securities, the CBR stopped its support of the ruble and a temporary moratorium was imposed on certain foreign currency payments. These actions resulted in an immediate and severe devaluation of the ruble and a sharp increase in the rate of inflation; a substantial decline in the prices of Russian debt and equity securities; and an inability of Russian issuers to raise funds in the international capital markets. These problems were aggravated by a major banking crisis in the Russian banking sector after the events of August 17, 1998, as evidenced by the termination of the banking licenses of a number of major Russian banks. This further impaired the ability of the banking sector to act as a consistent source of liquidity to Russian companies and resulted in the losses of bank deposits in some cases.

Recently, the Russian economy has experienced the negative influence of the global financial and economic crisis, which has led to a substantial decrease in the gross domestic product's growth rate, ruble depreciation and domestic demand decline. The Russian government has accumulated a significant stabilization fund and the CBR has considerable hard currency reserves, which some observers believe will soften the impact of the economic crisis on

the Russian economy. However, since the depth and duration of the global economic crisis, and the crisis's impact on Russia, are not yet clear, it is possible that the Russian economy could be impacted more severely than expected. Further economic instability in Russia could have a material adverse effect on our business, financial condition and results of operations.

*The Russian banking system is still developing, and another banking crisis could place severe liquidity constraints on our business.*

The Russian banking sector has steadily developed, as demonstrated by the growing presence of prominent international banks in Russia, as well as the consolidation of the Russian banking system and the increased presence of state-owned banks. However, many Russian banks currently do not meet international banking standards, and the transparency of the Russian banking sector in some respects still lags far behind internationally accepted norms.

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The CBR has increased its supervision of banks and has suspended a number of bank licenses for violation of its banking regulations. Furthermore, in Russia, bank deposits made by corporate entities generally are not insured.

Prior to the onset of the current world financial and economic crisis, there had been a rapid increase in lending by Russian banks, which many believed was accompanied by a deterioration in the credit quality of the borrowers. In addition, a previously robust domestic corporate debt market led to Russian banks increasingly holding large amounts of Russian corporate ruble bonds in their portfolios, leading to further deterioration in the risk profile of Russian bank assets. In addition, since Russian banks generally have lower capital adequacy requirements, the banking sector could be more susceptible than the Western banking system to the current market downturn and economic slowdown, including due to Russian corporate defaults that may occur.

In 2008, events in the Russian banking industry unfolded in line with the developing world banking crisis, which was triggered by a mid-September 2008 liquidity crunch, and at times has included all the classic banking crisis traits of deposit runs, a credit crunch and ongoing currency pressure. The current financial crisis is affecting all Russian banking institutions. The initial liquidity concerns that emerged in mid-September have since evolved into a full-blown credit crunch, as the situation with banking sector capitalization both in terms of deposits and wholesale funding has deteriorated.

Ongoing sector pressure is likely to result in a dramatic slowdown in lending growth, deteriorating asset quality and significant changes to the current structure. In the near future, the stability of the banking sector in Russia will depend on steps taken towards recovery from the world financial crisis and the scale of the Russian government's support.

There is currently a limited number of sufficiently creditworthy Russian banks. We hold the bulk of our excess ruble and foreign currency cash in Russian banks, including Russian subsidiaries of foreign banks. There are few, if any, safe ruble-denominated instruments in which we may invest our excess ruble cash. The current financial crisis, or the bankruptcy or insolvency of the banks from which we receive or with which we hold our funds, could result in the loss of our deposits or affect our ability to complete banking transactions in Russia, which could have a material adverse effect on our business, financial condition and results of operations.

*The infrastructure in Russia needs significant improvement and investment, which could disrupt normal business activity.*

The infrastructure in Russia largely dates back to the Soviet era and has not been adequately funded and maintained over the past decade. Particularly affected are the rail and road networks, power generation and transmission systems, communication systems and building stock. The deterioration of the infrastructure in Russia harms the national economy, disrupts the transportation of goods and supplies, adds costs to doing business and can interrupt business operations. These factors could have a material adverse effect on our business and results of operations.

*The Russian economy and the value of our shares and ADSs could be materially adversely affected by fluctuations in the global economy.*

Global credit markets and the global capital markets have recently experienced liquidity disruptions. See Risks Relating to Our Financial Condition and Financial Reporting We will require a significant amount of cash to fund our capital improvements program and The Russian banking system is still developing, and another banking crisis could place severe liquidity constraints on our business. Turmoil in the international credit markets, the recession in the economies and the collapse or near-collapse of several large financial institutions have resulted in increased volatility in the securities markets in many countries, including Russia. As has happened in the past, financial problems or an increase in the perceived risks associated with investing in emerging economies could dampen foreign investment in Russia and Russian businesses could face severe liquidity constraints, further materially adversely affecting the

Russian economy. Additionally, because Russia produces and exports large amounts of oil, the Russian economy is especially vulnerable to the price of oil on the world market and a decline in the price of oil could slow or disrupt the Russian economy or undermine the value of the ruble against foreign currencies. Russia is also one of the world's largest producers and exporters of metal products and its economy is vulnerable to fluctuations in world commodity prices and the imposition of tariffs and/or antidumping measures by

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any of its principal export markets. See **Risks Relating to Our Business and Industry** We operate in cyclical industries, and any local or global downturn, whether or not primarily affecting the mining and/or steel industries, may have an adverse effect on our results of operations and financial condition.

As many of the factors that affect the Russian and global economies affect our business and the business of many of our domestic and international customers, we could be materially adversely affected by a prolonged downturn affecting the Russian or global economy. In addition to reduced demand for our products, we may experience increases in accounts receivable and bad debt among our customers, some of whom may face liquidity problems and potential bankruptcy. Our suppliers may significantly raise their prices, eliminate or reduce trade financing or reduce their output. A decline in product demand, a decrease in collectability of accounts receivable or substantial changes in the terms of our suppliers' pricing policies or financing terms, or the potential bankruptcy of our customers or contract counterparties may have a material adverse effect on our business, financial condition, results of operations and prospects.

In addition, a deterioration in macroeconomic conditions could require us to reassess the value of goodwill on certain of our assets, recorded as the difference between the fair value of the assets of business acquired and its purchase price. This goodwill is subject to impairment tests on an ongoing basis. The weakening macroeconomic conditions in the countries in which we operate and/or a significant difference between the performance of an acquired company and the business case assumed at the time of acquisition could require us to write down the value of the goodwill or portion of such value, which could have a material adverse effect on our financial condition and results of operation. See note 3(n) to our consolidated financial statements in **Item 18. Financial Statements**.

### ***Political and social risks***

*Political and governmental instability could materially adversely affect our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*

Since 1991, Russia has sought to transform itself from a one-party state with a centrally-planned economy to a democracy with a market economy. As a result of the sweeping nature of the reforms, and the failure of some of them, the Russian political system remains vulnerable to popular dissatisfaction, including dissatisfaction with the results of privatizations in the 1990s, as well as to demands for autonomy from particular regional and ethnic groups.

Current and future changes in the government, conflicts between federal government and regional or local authorities, major policy shifts or lack of consensus between various branches of the government and powerful economic groups could disrupt or reverse economic and regulatory reforms. Any disruption or reversal of reform policies could lead to political or governmental instability or the occurrence of conflicts among powerful economic groups, resulting in an adverse impact on Russia's economy and investment climate, which could have a material adverse effect on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.

*Corruption and negative publicity could disrupt our ability to conduct our business.*

The local press and international press have reported high levels of corruption in Russia, including the bribery of officials for the purpose of initiating investigations by government agencies. Press reports have also described instances in which government officials engaged in selective investigations and prosecutions to further the commercial interests of certain government officials or certain companies or individuals. Additionally, there are reports of the Russian media publishing disparaging articles in return for payment. If officials make unlawful demands to us or if we are accused of involvement in official corruption, it could result in negative publicity, disrupt our ability to conduct our business effectively and thus materially adversely affect our business, financial condition and results of operations and the value of our shares and ADSs.



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*Shortage of qualified personnel could materially adversely affect our business, financial condition, results of operations and prospects.*

Currently the labor market does not suffer from an acute shortage of qualified labor. But in the future we might face such a challenge. It could be caused by the decline in the working age population due to a relatively low birth rate at the end of the 1980s through the early 1990s. In 2008, Rosstat estimated Russia's population at 142 million, a decline of almost seven million from 1992. Although the birth rate recently reached its highest rate in 15 years, the population continues to decline due to a relatively low birth rate, an aging population and low life expectancy. According to different estimates Russia's working age population will decline by 18-19 million people by 2025. If the present trend continues without a migration inflow to Russia, the decreasing working population will become a barrier to economic growth around 2015, according to the Economic Forecasting Institute of the Russian Academy of Sciences.

A shortage of skilled Russian workers combined with restrictive immigration policies could materially adversely affect our business, financial condition, results of operations and prospects.

### ***Legal risks and uncertainties***

*Deficiencies in the legal framework relating to subsoil licensing subject our licenses to the risk of governmental challenges and, if our licenses are suspended or terminated, we may be unable to realize our reserves, which could materially adversely affect our business and results of operations.*

Most of the existing subsoil licenses in Russia date from the Soviet era. During the period between the dissolution of the Soviet Union in August 1991 and the enactment of the first post-Soviet subsoil licensing law in the summer of 1992, the status of subsoil licenses and Soviet-era mining operations was unclear, as was the status of the regulatory authority governing such operations. The Russian government enacted the Procedure for Subsoil Use Licensing on July 15, 1992, which came into effect on August 20, 1992 (the Licensing Regulation). As was common with legislation of this time, the Licensing Regulation was passed without adequate consideration of transition provisions and contained numerous gaps. In an effort to address the problems in the Licensing Regulation, the Ministry of Natural Resources (the MNR) issued ministerial acts and instructions that attempted to clarify and, in some cases, modify the Licensing Regulation. Many of these acts contradicted the law and were beyond the scope of the MNR's authority, but subsoil licensees had no option but to deal with the MNR in relation to subsoil issues and comply with its ministerial acts and instructions. Thus, it is possible that licenses applied for and/or issued in reliance on the MNR's acts and instructions could be challenged by the prosecutor general's office as being invalid. In particular, deficiencies of this nature subject subsoil licensees to selective and arbitrary governmental claims.

Legislation on subsoil rights still remains internally inconsistent and vague, and the regulator's acts and instructions are often arguably inconsistent with legislation. Subsoil licensees thus continue to face the situation where both failing to comply with the regulator's acts and instructions and choosing to comply with them places them at the risk of being subject to arbitrary governmental claims, whether by the regulator or the prosecutor general's office. Our competitors may also seek to deny our rights to develop certain natural resource deposits by challenging our compliance with tender rules and procedures or compliance with license terms.

An existing provision of law that a license may be suspended or terminated if the licensee does not comply with the significant or material terms of a license is an example of such a deficiency in the legislation. However, the MNR (including its successor agency since May 13, 2008, the Ministry of Natural Resources and Ecology) has not issued any interpretive guidance on the meaning of these terms. Similarly, under Russia's civil law system, court decisions on the meaning of these terms do not have any precedential value for future cases and, in any event, court decisions in this regard have been inconsistent. These deficiencies result in the regulatory authorities, prosecutors and courts having significant discretion over enforcement and interpretation of the law, which may be used to challenge our

subsoil rights selectively and arbitrarily.

Moreover, during the tumultuous period of the transformation of the Russian planned economy into a free market economy in the 1990s, documentation relating to subsoil licenses was not properly maintained in accordance with administrative requirements and, in many cases, was lost or destroyed. Thus, in many cases,

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although it may be clearly evident that a particular enterprise has mined a licensed subsoil area for decades, the historical documentation relating to their subsoil licenses may not be complete. If, through governmental or other challenges, our licenses are suspended or terminated we would be unable to realize our reserves, which could materially adversely affect our business and results of operations.

*Weaknesses relating to the Russian legal system and legislation create an uncertain investment climate.*

Russia is still developing the legal framework required to support a market economy. The following weaknesses relating to the Russian legal system create an uncertain investment climate and result in risks with respect to our legal and business decisions:

inconsistencies between and among the Constitution, federal law, presidential decrees and governmental, ministerial and local orders, decisions, resolutions and other acts;

conflicting local, regional and federal rules and regulations;

the lack of fully developed corporate and securities laws;

substantial gaps in the regulatory structure due to the delay or absence of implementing legislation;

the relative inexperience of judges in interpreting legislation;

the lack of full independence of the judicial system from commercial, political and nationalistic influences;

difficulty in enforcing court orders;

a high degree of discretion or arbitrariness on the part of governmental authorities; and

still-developing bankruptcy procedures that are subject to abuse.

All of these weaknesses could affect our ability to enforce our rights under our licenses and under our contracts, or to defend ourselves against claims by others. We make no assurances that regulators, judicial authorities or third parties will not challenge our compliance with applicable laws, decrees and regulations.

*Failure to comply with existing laws and regulations could result in substantial additional compliance costs or various sanctions which could materially adversely affect our business, financial condition, results of operations and prospects.*

Our operations and properties are subject to regulation by various government entities and agencies in connection with obtaining and renewing various licenses, permits, approvals and authorizations, as well as with ongoing compliance with existing laws, regulations and standards. Regulatory authorities exercise considerable discretion in matters of enforcement and interpretation of applicable laws, regulations and standards, the issuance and renewal of licenses, permits, approvals and authorizations and in monitoring licensees' compliance with the terms thereof. Russian authorities have the right to, and frequently do, conduct periodic inspections of our operations and properties throughout the year.

Our failure to comply with existing laws and regulations or to obtain all approvals, authorizations and permits required for our operations or findings of governmental inspections, may result in the imposition of fines or penalties or more severe sanctions including the suspension, amendment or termination of our licenses, permits, approvals and

authorizations or in requirements that we cease certain of our business activities, or in criminal and administrative penalties applicable to our officers. Any such decisions, requirements or sanctions could increase our costs and materially adversely affect our business, financial condition, results of operations and prospects.

*One or more of our subsidiaries could be forced into liquidation on the basis of formal noncompliance with certain requirements of Russian law, which could materially adversely affect our business, financial condition, results of operations and prospects.*

Certain provisions of Russian law may allow a court to order liquidation of a Russian legal entity on the basis of its formal noncompliance with certain requirements during formation, reorganization or during its operation. There have been cases in the past in which formal deficiencies in the establishment process of a Russian legal entity

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or noncompliance with provisions of Russian law have been used by Russian courts as a basis for liquidation of a legal entity. For example, under Russian corporate law, negative net assets calculated on the basis of Russian accounting standards as of the end of the second or any subsequent year of a company's operation can serve as a basis for a court to order the liquidation of the company upon a claim by governmental authorities. Many Russian companies have negative net assets due to very low historical asset values reflected on their balance sheets prepared in accordance with Russian accounting standards; however, their solvency, *i.e.*, their ability to pay debts as they come due, is not otherwise adversely affected by such negative net assets. Currently, we have two subsidiaries with negative net assets: Kaslinsky Architectural Art Casting Plant OOO and Tikhvin Ferroalloy Plant.

If involuntary liquidation were to occur, then we may be forced to reorganize the operations we currently conduct through the affected subsidiaries. Any such liquidation could lead to additional costs, which could materially adversely affect our business, financial condition, results of operations and prospects.

*Selective government action could have a material adverse effect on the investment climate in Russia and on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*

Governmental authorities in Russia have a high degree of discretion. Press reports have cited instances of Russian companies and their major shareholders being subjected to government pressure through prosecutions of violations of regulations and legislation which are either politically motivated or triggered by competing business groups.

In mid-2008, Mechel came under public criticism by the Russian government. Repeated statements were made accusing Mechel of using tax avoidance schemes and other improprieties. Ultimately the allegations regarding tax avoidance were not confirmed by the tax authorities, but the antimonopoly investigation resulted in imposition of a fine and a number of FAS directives regarding our business practices. See [Risks Relating to Our Business and Industry](#) Regulation by the Federal Antimonopoly Service could lead to sanctions with respect to the subsidiaries we have acquired or established, our prices, our sales volumes or our business practices and [Item 8. Financial Information](#) Litigation Antimonopoly.

Selective government action, if directed at us or our major shareholders, could have a material adverse effect on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.

*Due to still-developing law and practice related to minority shareholder protection in Russia, the ability of holders of our shares and ADSs to bring, or recover in, an action against us may be limited.*

In general, minority shareholder protection under Russian law derives from supermajority shareholder approval requirements for certain corporate action, as well as from the ability of a shareholder to demand that the company purchase the shares held by that shareholder if that shareholder voted against or did not participate in voting on certain types of actions. Companies are also required by Russian law to obtain the approval of disinterested shareholders for certain transactions with interested parties. See [Item 10. Additional Information](#) Description of Capital Stock Rights attaching to common shares. Disclosure and reporting requirements have also been enacted in Russia. Concepts similar to the fiduciary duties of directors and officers to their companies and shareholders are also expected to be further developed in Russian legislation; for example, recent amendments to the Russian Code of Administrative Offenses impose administrative liability on members of a company's board of directors or management board for violations committed in the maintenance of shareholder registers and the convening of general shareholders' meetings. While these protections are similar to the types of protections available to minority shareholders in U.S. corporations, in practice, the enforcement of these and other protections has been poor.

The supermajority shareholder approval requirement is met by a vote of 75% of all voting shares that are present at a shareholders' meeting. Thus, controlling shareholders owning less than 75% of the outstanding shares of a company

may hold 75% or more of the voting power if enough minority shareholders are not present at the meeting. In situations where controlling shareholders effectively have 75% or more of the voting power at a shareholders meeting, they are in a position to approve amendments to our charter, reorganization, significant sales of assets and other major transactions, which could be prejudicial to the interests of minority shareholders. See

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Risks Relating to Our Business and Industry Our controlling shareholder has the ability to take actions that may conflict with the interests of the holders of our shares and ADSs.

*Shareholder liability under Russian legislation could cause us to become liable for the obligations of our subsidiaries.*

The Civil Code of the Russian Federation, as amended (the Civil Code ), and the Joint-Stock Companies Law generally provide that shareholders in a Russian joint-stock company are not liable for the obligations of the joint-stock company and bear only the risk of loss of their investment. This may not be the case, however, when one person is capable of determining decisions made by another person or entity. The person or entity capable of determining such decisions is deemed an effective parent. The person whose decisions are capable of being so determined is deemed an effective subsidiary. Under the Joint-Stock Companies Law, an effective parent bears joint and several responsibility for transactions concluded by the effective subsidiary in carrying out these decisions if:

    this decision-making capability is provided for in the charter of the effective subsidiary or in a contract between the companies; and

    the effective parent gives obligatory directions to the effective subsidiary based on the above-mentioned decision-making capability.

In addition, an effective parent is secondarily liable for an effective subsidiary's debts if an effective subsidiary becomes insolvent or bankrupt resulting from the action or inaction of an effective parent. This is the case no matter how the effective parent's ability to determine decisions of the effective subsidiary arises. For example, this liability could arise through ownership of voting securities or by contract. In these instances, other shareholders of the effective subsidiary may claim compensation for the effective subsidiary's losses from the effective parent which caused the effective subsidiary to take action or fail to take action knowing that such action or failure to take action would result in losses. Accordingly, we could be liable in some cases for the debts of our subsidiaries. This liability could have a material adverse effect on our business, results of operations and financial condition.

*Shareholder rights provisions under Russian law could result in significant additional obligations on us.*

Russian law provides that shareholders that vote against or abstain from voting on certain matters have the right to request that the company redeem their shares at market value in accordance with Russian law. The decisions that trigger this right include:

    decisions with respect to a reorganization;

    the approval by shareholders of a major transaction, which, in general terms, is a transaction involving property worth more than 50% of the gross book value of our assets calculated according to Russian accounting standards, regardless of whether the transaction is actually consummated, except for transactions undertaken in the ordinary course of business; and

    the amendment of our charter in a manner that limits shareholder rights.

Our (or, as the case may be, our subsidiaries') obligation to purchase shares in these circumstances, which is limited to 10% of our or each of our subsidiary's net assets, as applicable, calculated in accordance with Russian accounting standards at the time the matter at issue is voted upon, could have a material adverse effect on our business, financial condition, results of operations and prospects due to the need to expend cash on such obligatory share purchases.

*The lack of a central and rigorously regulated share registration system in Russia may result in improper record ownership of our shares and ADSs.*

Ownership of Russian joint-stock company shares (or, if the shares are held through a nominee or custodian, then the holding of such nominee or custodian) is determined by entries in a share register and is evidenced by extracts from that register. Currently, there is no central registration system in Russia. Share registers are maintained by the companies themselves or, if a company has more than 50 shareholders, by licensed registrars located

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throughout Russia. Regulations have been issued regarding the licensing conditions for such registrars, as well as the procedures to be followed by both companies maintaining their own registers and licensed registrars when performing the functions of registrar. In practice, however, these regulations have not been strictly enforced, and registrars generally have relatively low levels of capitalization and inadequate insurance coverage. Moreover, registrars are not necessarily subject to effective governmental supervision. Due to the lack of a central and rigorously regulated share registration system in Russia, transactions in respect of a company's shares could be improperly or inaccurately recorded, and share registration could be lost through fraud, negligence or oversight by registrars incapable of compensating shareholders for their misconduct. This creates risks of loss not normally associated with investments in other securities markets. Furthermore, the depository, under the terms of the agreements governing the deposit and record of our ADSs, will not be liable for the unavailability of shares or for the failure to make any distribution of cash or property with respect thereto due to the unavailability of the shares. See Item 10. Additional Information Description of Capital Stock Registration and transfer of shares.

*Characteristics of and changes in the Russian tax system could materially adversely affect our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*

Generally, Russian companies are subject to numerous taxes. These taxes include, among others:

profits tax;

value-added tax ( VAT );

unified social tax;

mineral extraction tax; and

property and land taxes.

Laws related to these taxes have been in force for a short period relative to tax laws in more developed market economies and few precedents with regard to the interpretation of these laws have been established. Global tax reforms commenced in 1999 with the introduction of Part One of the Tax Code of the Russian Federation, as amended (the Russian Tax Code ), which sets general taxation guidelines. Since then, Russia has been in the process of replacing legislation regulating the application of major taxes such as corporate profits tax, VAT and property tax with new chapters of the Russian Tax Code.

In practice, the Russian tax authorities generally interpret the tax laws in ways that rarely favor taxpayers, who often have to resort to court proceedings to defend their position against the tax authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretations of the legislation and assessments. Differing interpretations of tax regulations exist both among and within government ministries and organizations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement. Tax declarations, together with related documentation such as customs declarations, are subject to review and investigation by a number of authorities, each of which may impose severe fines, penalties and interest charges. Generally, in an audit, taxpayers are subject to inspection with respect to the three calendar years which immediately preceded the year in which the audit is carried out. Previous audits do not completely exclude subsequent claims relating to the audited period because Russian tax law authorizes upper-level tax inspectorates to reaudit taxpayers which were audited by subordinate tax inspectorates. In addition, on July 14, 2005, the Russian Constitutional Court issued a decision that allows the statute of limitations for tax liabilities to be extended beyond the three-year term set forth in the tax laws if a court determines that a taxpayer has obstructed or hindered a tax audit. Because none of the relevant terms is defined, tax authorities may have broad discretion to argue that a taxpayer has

obstructed or hindered an audit and ultimately seek back taxes and penalties beyond the three year term. In some instances, new tax regulations have been given retroactive effect.

Moreover, financial results of Russian companies cannot be consolidated for tax purposes. Therefore, each of our Russian subsidiaries pays its own Russian taxes and may not offset its profit or loss against the loss or profit of any of our other subsidiaries. In addition, intercompany dividends are subject to a withholding tax of 0% (if as of the date of deciding to pay dividends, the company receiving dividends for a period of not less than 365 days has continuously possessed not less than 50% of the charter capital of the company paying dividends (or depositary

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receipts of the company giving the right to obtain not less than 50% of its dividends), if the cost of acquisition of shares or depositary receipts of the company paying dividends exceeded RUR 500 million) or 9%, if being distributed by Russian companies to Russian companies and/or individual Russian residents, and 15%, if being distributed by foreign companies to Russian companies and natural persons (tax residents of the Russian Federation) or by Russian companies to foreign companies and natural persons who are not Russian tax residents. Dividends from foreign companies to Russian companies are subject to a tax of 9%. Taxes paid in foreign countries by Russian companies may be offset against payment of these taxes in the Russian Federation up to the maximum amount of the Russian tax liability. In order to apply the offset, the company is required to confirm the payment of taxes in the foreign country. The confirmations must be authorized by the tax authority of the foreign country if taxes were paid by the company itself, and the confirmation must be authorized by the tax agent if taxes were withheld by the tax agent under foreign tax law or international tax agreement.

The foregoing conditions create tax risks in Russia that are more significant than typically found in countries with more developed tax systems, imposing additional burdens and costs on our operations, including management resources. In addition to our tax burden, these risks and uncertainties complicate our tax planning and related business decisions, potentially exposing us to significant fines and penalties and enforcement measures despite our best efforts at compliance. See also [Risks Relating to the Russian Federation and Other Countries Where We Operate](#) [Legal risks and uncertainties](#) [Selective government action could have a material adverse effect on the investment climate in Russia and on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.](#)

*Vaguely drafted Russian transfer pricing rules and lack of reliable pricing information may potentially affect our results of operations.*

Russian transfer pricing rules effective since 1999 give Russian tax authorities the right to control prices for transactions between related entities and certain other types of transactions between unrelated parties, such as foreign trade transactions or transactions with significant price fluctuations if the transaction price deviates by more than 20% from the market price. Special transfer pricing rules apply to operations with securities and derivative instruments. The Russian transfer pricing rules are vaguely drafted, and are subject to interpretation by Russian tax authorities and courts. Due to the uncertainties in interpretation of transfer pricing legislation, the tax authorities may challenge our prices and make adjustments which could affect our tax position. As of the end of 2007, as a result of various tax audits of our companies we received assessments from the tax authorities for transfer-pricing related taxes, interest and penalties totaling \$20.2 million relating to the years 2004-2005. In 2008, various tax audits of our companies did not result in claims from the tax authorities for use of transfer pricing; however, under Russian law review of past tax periods relating to the years 2006-2008 by tax authorities is lawful and in this connection claims from the tax authorities are not excluded. We have so far successfully challenged these assessments in court; however, the court decisions that have been issued are subject to appeal by the tax authorities with the Supreme Arbitration Court of the Russian Federation. If similar such assessments are upheld in the future, our financial condition and results of operations could be materially adversely affected. In addition, we could face significant losses associated with the assessed amount of underpaid prior tax and related interest and penalties. See also [Characteristics of and changes in the Russian tax system could materially adversely affect our business, financial condition, results of operations and prospects and the value of our shares and ADSs](#) and [Item 8. Financial Information](#) [Litigation](#) [Tax.](#)

In addition, a number of draft amendments to the transfer pricing law have recently been introduced which, if implemented, would considerably toughen the existing law. The proposed changes, among other things, may shift the burden of proving market prices from the tax authorities to the taxpayer, cancel the existing permitted deviation threshold and introduce specific documentation requirements for proving market prices.

*Russian currency control regulations could hinder our ability to conduct our business.*

In the past, Russian currency regulations imposed various restrictions on operations involving conversion of foreign currencies in an attempt to support the ruble. Effective from January 1, 2007, most of these restrictions have been removed. In 2007, Russian law changed to allow Russian residents to open accounts and effect operations through foreign bank accounts. However, in case of a crisis, the government and the CBR may impose requirements

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on cash inflows and outflows into and out of Russia or on the use of foreign currency in Russia in the future. For example, Russian companies currently must repatriate proceeds from export sales, subject to certain exceptions. Moreover, the foreign currency market in Russia is still developing and we may experience difficulty in converting rubles into other currencies. Any delay or difficulty in converting rubles into a foreign currency to make a payment or any practical difficulty in the transfer of foreign currency could limit our ability to meet our payment and debt obligations, which could result in the acceleration of debt obligations and cross defaults, or prevent us from carrying on necessary business transactions.

*Russian capitalization rules could affect our ability to deduct interest on certain borrowings.*

Russian capitalization rules limit the amount of interest that can be deducted by a Russian company on debts payable to non-resident shareholders. Until January 1, 2006, these rules applied only to loans issued to a Russian company by a foreign shareholder owning directly or indirectly more than 20% of the charter capital of the Russian company. However, thin capitalization rules that came into effect on January 1, 2006 extend the rules' application to loans issued to a Russian company by another Russian company that is affiliated with the foreign shareholder as well as to loans secured by such foreign shareholder or its affiliated Russian company. Under these rules, a positive difference between the accrued interest and maximum interest calculated in accordance with the thin capitalization rules is considered to be dividends and, thus, is not included in the taxable expenses. Application of the Russian thin capitalization rules could thus affect our ability to deduct interest on certain borrowings that we would otherwise be able to deduct.

*Expansion of limitations on foreign investment in strategic sectors could affect our ability to attract and/or retain foreign investments.*

On April 29, 2008, the Federal Law "On the Procedure for Foreign Investment in Companies With Strategic Impact on the National Defense and Security of the Russian Federation" (the "Strategic Industries Law") was adopted. See Item 4. Information on the Company Regulatory Matters Russian Regulation The Strategic Industries Law.

Since our subsidiary Southern Urals Nickel Plant carries out exploration and production on land with nickel and cobalt ore deposits included in the official list of subsoil plots of federal importance published on March 5, 2009 in the Russian official gazette *Rossiyskaya Gazeta* (the "Strategic Subsoil List"), it qualifies as a company with strategic importance for the national defense and security of the Russian Federation (a "Strategic Company") subject to special regulation. Our subsidiary Southern Urals Nickel Plant is also a Strategic Company, as the Buruktal (Orenburg region) and the Sakhara (Chelyabinsk region) nickel and cobalt ore deposits, for which Southern Urals Nickel Plant holds the subsoil licenses, are also included in the Strategic Subsoil List. Our subsidiaries Port Posiet, Port Kambarka OAO (Port Kambarka) and Port Mechel Temryuk (Port Temryuk) are included in the register of natural monopolies, and therefore are also Strategic Companies.

According to the Strategic Industries Law, the activity of a business entity which is deemed to occupy a dominant position in the production and sale of metals and alloys with special features which are used in production of weapons and military equipment is also deemed to be strategic activity. Our subsidiary Ural Stampings Plant has been found by FAS to hold a dominant position on the market of carbonic, alloyed and heat-resistant alloyed stampings. Such products are of a type generally used in the production of weapons and military equipment. Therefore, Ural Stampings Plant may also qualify as Strategic Company. Furthermore, entities producing and distributing industrial explosives and entities that operate equipment containing radioactive materials are also deemed to be Strategic Companies. Thus, our subsidiaries Yakutugol and Vzryvprom also qualify as Strategic Companies, as they both hold licenses to produce industrial explosives and Yakutugol, in addition, holds a license to operate equipment containing radioactive materials.

Therefore, any sale to a foreign investor or group of entities of a stake in Port Posiet, Port Kambarka, Port Temryuk, Southern Urals Nickel Plant, Yakutugol, Vzryvprom and, possibly, Urals Stampings Plant, which sale, according to the Strategic Industries Law, is deemed to convey control, as described in Item 4. Information on the Company Regulatory Matters Russian Regulation The Strategic Industries Law, will be subject to prior approval from state authorities. Likewise, a sale to a foreign investor or group of entities of a stake in Mechel which

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according to the Strategic Industries Law provides control over Port Posiet, Port Kambarka, Port Temryuk, Southern Urals Nickel Plant, Yakutugol, Vzryvprom and, potentially, Urals Stampings Plant, will also be subject to prior approval from state authorities.

Additionally, in case a foreign investor or group of entities which is a holder of securities of Port Posiet, Port Kambarka, Port Temryuk, Southern Urals Nickel Plant, Yakutugol, Vzryvprom and, potentially, Urals Stampings Plant, becomes a holder of voting shares in amount which is considered to give them direct or indirect control over these companies in accordance with the Strategic Industries Law due to a change in allocation of voting shares pursuant to the procedures provided by Russian law (*e.g.*, as a result of a buy-back by the relevant company of its shares, conversion of preferred shares into common shares, holders of preferred shares becoming entitled to vote at a general shareholders meeting in the events provided under Russian law), such shareholders will have to apply for state approval of their control within three months after they received such control.

In this connection, there is a risk that the necessity to receive prior or subsequent state approvals and the chance of not being granted such approvals might affect our ability to attract foreign investments, to create joint ventures with foreign partners with respect to our companies that qualify as Strategic Companies or effect restructuring of our group which might, in turn, adversely affect our business, financial condition, results of operations and prospects.

### ***Other Countries Where We Operate***

*We face risks similar to those in Russia in other countries of the former Soviet Union and former Soviet-bloc countries in Eastern and Central Europe.*

We currently have four steel mills in Romania, a hardware plant in Lithuania, a blocking minority stake in a power plant in Bulgaria and two mining projects in Kazakhstan. We may acquire additional operations in countries of the former Soviet Union, former Soviet-bloc countries in Eastern and Central Europe or elsewhere. As with Russia, the other countries where we have operations are emerging markets subject to greater political, economic, social and legal risks than more developed markets. In many respects, the risks inherent in transacting business in these countries are similar to those in Russia, especially those risks set out above in Economic risks, Political and social risks and risks and uncertainties.

*The BCG companies are subject to extensive U.S. laws, government regulations and other requirements relating to the protection of the environment, health and safety and other matters, which impose significant costs on us. U.S. regulatory agencies have the authority to temporarily or permanently close the BCG companies mines or modify their operations, which could materially adversely affect our business. Our operations may impact the environment or cause or contribute to contamination or exposure to hazardous substances, which could result in material liabilities to us.*

Like other mining businesses in the United States, our BCG companies are subject to a wide range of rules and regulations, including those governing water discharges, air emissions, the management, treatment, storage, disposal and transportation of hazardous materials and waste, protection of plants, wildlife and other natural resources, worker health and safety, reclamation and restoration of properties after mining activities cease, surface subsidence from underground mining, blasting operations, noise, the effects of mining on surface water and groundwater quality and availability, and reporting and recordkeeping. Violations of these requirements can result in fines, penalties, required facility upgrades or operational changes, suspension or revocation of permits and, in severe cases, temporary or permanent facility shut-down. We incur substantial costs to comply with U.S. governmental regulations that apply to our operations in the United States.

We could become subject to investigation or cleanup obligations, or related third-party personal injury or property damage claims, in connection with on-site or off-site contamination issues or other noncompliance with U.S. regulatory requirements. In particular, under the U.S. Comprehensive Environmental Response, Compensation and Liability Act (CERCLA, commonly known as Superfund) and analogous state laws, current and former property owners and operators, as well as hazardous waste generators, arrangers and transporters, can be held liable for investigation and cleanup costs at properties where there has been a release or threatened release

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of hazardous substances. Such laws can also require so-called potentially responsible parties to fund the restoration of damaged natural resources or agree to restrictions on future uses of impacted properties.

Liability under such laws can be strict, joint, several and retroactive. Accordingly, we could theoretically incur liability (whether as a result of government enforcement or private personal injury or property damage claims) for known or unknown liabilities at (or caused by migrations from or hazardous waste shipped from) any of our current or former facilities or properties, including those owned or operated by our predecessors or third parties.

*Changes in U.S. regulations and the passage of new legislation in the United States could materially adversely affect the BCG companies' operations, increase our costs or limit our ability to produce and sell coal in the United States.*

New legislation, regulations and rules adopted or implemented in the future (or changes in interpretations of existing laws and regulations) may materially adversely affect our operations. Some U.S. commentators expect that the current U.S. administration could implement policies or sponsor legislation that will make the production and/or consumption of coal in the United States more expensive and create additional regulatory burdens, and it remains unclear whether this will affect the business and prospects of the BCG companies. In particular, future regulation of greenhouse gases in the United States could occur pursuant to future treaty obligations, statutory or regulatory changes under the U.S. Clean Air Act, federal or state adoption of a greenhouse gas regulatory scheme, or otherwise. The U.S. Congress has recently considered, and there are pending, various proposals to reduce greenhouse gas emissions, and the U.S. Environmental Protection Agency (the EPA) recently issued several proposed determinations and rulemakings relating to greenhouse gas emissions from various sources. In the absence of federal legislation, many states and regions have undertaken greenhouse gas initiatives.

These and other potential U.S. federal, state and regional climate change rules will likely require additional controls on coal-fueled power plants, industrial boilers and manufacturing operations, and may even cause some users of coal to switch from coal to a lower carbon fuel. There can be no assurance at this time that a carbon dioxide cap-and-trade program, a carbon tax or other regulatory regime, if implemented, will not affect the future market for coal in the regions where we operate and reduce the demand for coal.

Furthermore, surface and underground mining are subject to increasing regulation, including pursuant to the federal MINER Act, blast survey and monitoring restrictions, and requirements by the U.S. Army Corps of Engineers and U.S. Department of Interior's Office of Surface Mining, which may require us to incur additional costs.

*We must obtain and maintain numerous U.S. governmental permits and approvals for our operations in the United States, which can be costly and time consuming, and our failure to obtain or renew necessary permits and approvals could negatively impact our business.*

Numerous governmental permits and approvals are required for our U.S. operations. Many of our permits are subject to renewal from time to time, and renewed permits may contain more restrictive conditions than existing permits. In addition, violations of our permits may occur from time to time, permits we need may not be issued or, if issued, may not be issued in a timely fashion.

In recent years, the permitting required under the U.S. Clean Water Act to address filling streams and valleys in connection with mining operations has been the subject of extensive litigation, including in West Virginia, where our BCG companies' operations are based. It is unclear at this time how these issues will ultimately be resolved, but for this as well as other issues that may arise involving necessary permits, such requirements could prove costly and time consuming, and could delay, interrupt or discontinue our operations.

*We may be subject to significant mine reclamation and closure obligations with respect to our U.S. coal mining operations.*

The U.S. Surface Mining Control and Reclamation Act ( SMCRA ) and counterpart state rules establish operational, reclamation and closure standards for all aspects of surface mining in the United States, as well as many aspects of underground mining. Our estimated reclamation and mine closure obligations could change significantly

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if actual amounts (which are dependent on a number of variables, including estimated future retirement costs, estimated proven reserves and assumptions involving profit margins, inflation rates and interest rates) differ significantly from our assumptions, which could have a material adverse affect on our results of operations and financial condition.

*Extensive environmental regulation in the United States, including the Clean Air Act and similar state and local laws, affect our U.S. customers and could reduce the demand for coal as a fuel source and cause our sales to decline.*

The U.S. Clean Air Act and similar state and local laws extensively regulate the amount of sulfur dioxide, particulate matter, nitrogen oxides, mercury and other compounds that are emitted into the air from power plants and other sources. Stricter regulations of such emissions could increase the cost of using coal in the United States, reducing demand and make it a less attractive fuel alternative for future planning.

For example, in order to meet the Clean Air Act limits on sulfur dioxide emissions from power plants, coal users may need to install scrubbers, use sulfur dioxide emission allowances (some of which they may purchase), blend high sulfur coal with low sulfur coal or switch to other fuels. Some of the EPA's initiatives to reduce sulfur dioxide, nitrous oxide and mercury emissions have been the subject of litigation in recent years, and the EPA continues to address issues raised in court opinions. In addition, several electric utilities have been sued by the government for alleged violations of the Clean Air Act, which could adversely impact the demand for coal.

To the extent compliance with these laws and regulations and any new or proposed requirements affect our customers in the United States, an important market for the BCG companies, this could adversely affect our operations and results.

*Mining in the Northern and Central Appalachian region of the United States is more complex and involves more regulatory constraints than in other U.S. geographic areas.*

The geological characteristics of Northern and Central Appalachian coal reserves, such as depth of overburden and coal seam thickness, make them complex and costly to mine. As such mines become depleted, replacement reserves may not be available when required or, if available, may not be capable of being mined at costs comparable to those characteristic of the depleting mines. In addition, as compared to mines in other areas such as in the western United States, permitting, licensing and other environmental and regulatory requirements are more costly and time consuming to satisfy. These factors could materially adversely affect the mining operations and cost structures of, and customers ability to use coal produced by, operators in Northern and Central Appalachia, including our BCG companies.

## **Item 4. Information on the Company**

### **Overview**

We are a vertically integrated mining, steel, ferroalloys and power group with revenues of \$10.0 billion in 2008.

Our mining business consists of coal and iron ore mines in Russia. Our subsidiary Southern Kuzbass Coal Company and its subsidiaries operate coal mines located in the Kuznetsky Basin, near the city of Mezhdurechensk in southwestern Siberia. We have four open pit mines – Krasnogorsk, Tomusinsk, Olzherassk and Sibirginsk – and three underground mines – Lenin, Sibirginsk and New-Olzherassk. In the Sakha Republic in eastern Siberia, our subsidiary Yakutugol operates the Nerungrinsk and Kangalassk open pit mines and the Dzhebariki-Khaya underground mine, and also holds the license rights to mine the undeveloped Elga coal deposit, which we plan to mine using the open pit method after the completion of the construction of a private rail branch line of approximately 315 kilometers in length, which will connect the Elga coal deposit to the Baikal-Amur Mainline.

We also provide coal washing services, both to our coal-mining subsidiaries and to third parties; according to the Central Dispatching Department, at the end of 2008 we controlled 20% of Russia's overall coal-washing capacity.

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Our subsidiary Korshunov Mining Plant operates three open pit iron ore mines – Korshunovsk, Rudnogorsk and Tatianinsk. These mines are located near Zheleznogorsk-Ilimsky, a town in Irkutsk region in central Siberia.

Our steel business comprises the production and sale of semi-finished steel products, carbon and specialty long products, carbon and stainless flat products and value-added downstream metal products including hardware, stampings and forgings. It also produces significant amounts of coke, both for internal use and for sales to third parties. We have the flexibility to supply our own steel mills with our mining products or to sell such mining products to third parties, depending on price differentials between local suppliers and foreign and domestic customers.

Our steel and steel-related production facilities in Russia include two integrated steel mills, a coke plant, a hardware plant, a forging and stamping mill and a scrap processing facility in the southern Ural Mountains, a hardware plant in northwestern Russia near the border with Finland and a coke and coal gas plant near Moscow. Outside of Russia, our steel facilities are in the E.U., including a hardware plant in Lithuania and four steel mills in Romania.

We started the formation of the ferroalloys business by acquiring Southern Urals Nickel Plant in 2001. We acquired Bratsk Ferroalloys Plant in 2007. In April 2008, we completed the acquisition of 99.3% of Oriel Resources plc ( Oriel Resources ) from its shareholders in a public offer conducted under the U.K. Takeover Code. The assets acquired with Oriel Resources included Tikhvin Ferroalloy Plant ZAO ( Tikhvin Ferroalloy Plant ), a ferrochrome smelter located near St. Petersburg, as well as the Voskhod chrome and Shevchenko nickel projects in Kazakhstan. With Oriel's acquisition in 2008, we continued developing our ferroalloy division within the group. The activities at our new division are aimed at increasing the efficiency of our steel business, driven by the use of our own raw materials (ferroalloys) for specialty and stainless steel production, as well as our competitiveness in general.

In October 2008, we completed the consolidation of our ferroalloy assets based on Oriel Resources Ltd. (UK). Oriel Resources owns a 100% interest in Tikhvin Ferroalloy Plant (Leningrad region, Russia), a 100% interest in Bratsk Ferroalloys Plant (Irkutsk region, Russia), an 84.06% interest in Southern Urals Nickel Plant (Orenburg region, Russia), as well as the Voskhod chrome and the Shevchenko nickel deposits in Kazakhstan. Southern Urals Nickel Plant operates two open pit nickel mines – Sakhara and Buruktal – and a nickel production plant in the city of Orsk in Orenburg region, in the southern part of Russia's Ural mountain range.

In April 2007, we acquired a controlling interest in Southern Kuzbass Power Plant, located in the city of Kaltan, in the Kemerovo region. In June 2007, we acquired a controlling interest in Kuzbass Power Sales Company, the largest power distribution company in the Kemerovo region. In December 2007, we purchased a 49% stake in Toplofikatsia Rousse JSC ( Toplofikatsia Rousse ), a power plant located in Rousse, Bulgaria. We envision that our power business will enable us to market another higher value-added product made from our steam coal, such as electricity and heat energy, and increase the electric power self-sufficiency of the mining and steel segments of our business.

Our group includes a number of logistical and marketing assets that help us to deliver and market our mining products, raw steel, manufactured steel goods and ferroalloy products. We have freight seaports in Russia on the Pacific Ocean and on the Black Sea and a freight river port on a tributary of the Volga River in central Russia. We have a freight railcar pool, and we have begun building a private rail branch line to access one of our coal deposits in eastern Siberia. We have a network of overseas branches and agents to market our products internationally, and we have a Russian domestic customer service subsidiary with more than 50 regional offices.

Mechel OAO is an open joint-stock company incorporated under the laws of the Russian Federation. From the date of our incorporation on March 19, 2003 until August 19, 2005, our corporate name was Mechel Steel Group OAO. We conduct our business through a number of subsidiaries. We are registered with the Federal Tax Service of the Russian Federation under state registration number 1037703012896. Our principal executive offices are located at Krasnoarmeyskaya Street, 1, Moscow 125993, Russian Federation. Our telephone number is +7 495 221 8888. Our

Internet addresses are [www.mechel.com](http://www.mechel.com) and [www.mechel.ru](http://www.mechel.ru). Information posted on our website is not a part of this document. We have appointed CT Corporation Systems, 111 Eighth Avenue, New York, New York 10011 as our authorized agent upon which process may be served for any suit or proceeding arising out of or relating to our shares and ADSs or the ADS deposit agreement.

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### **Competitive Strengths**

Our main competitive strengths are the following:

#### ***Leading mining and metals group by production volume with strong positions in key businesses***

*By volume we are the largest coking coal producer in Russia and one of the largest worldwide.*

According to the Central Dispatching Department, in 2008, we were the largest producer of coking coal in Russia by volume (we have lost our volume based leading position in Russian coking coal production, according to the Central Dispatching Department's report for the first quarter of 2009). Based on publicly available information, we believe we were one of the largest coking coal producer in the world based on 2008 production volume. According to the RosInformUgol, we also control 26% of Russia's coking coal washing capacity by volume.

Our acquisition of the remaining 75% less one share of Yakutugol in 2007, which made us the owners of 100% of Yakutugol's shares, has given us a 22% market share in the coking coal market in Russia by production volume in 2008 according to data from the Central Dispatching Department. According to RasMin OOO ( RasMin ), a private information and research company focusing on the coal-mining industry, in 2008 Yakutugol's export sales of coking coal were the largest by volume of any Russian company. Yakutugol has major customers in Japan, South Korea and Taiwan.

Our acquisition of the BCG companies in May 2009 adds value by diversifying our coking coal portfolio and strengthening our position in the world market. The BCG companies' hard coking coal of low, medium and high volatility is well known and highly regarded by customers in North America, Europe and Asia for its excellent quality.

Together with our existing coal varieties from Southern Kuzbass Coal Company and Yakutugol, now we can supply customers all over the world with a full range of coals to make high-quality coke.

*By volume we are Russia's second largest producer of specialty steel products and Russia's second largest producer of long steel products.*

According to a comparison by Metall-Expert, in 2008 by production volume we were Russia's second largest producer of long steel products (excluding square billets) after Evraz Group, and first in the production of wire rod. Our long steel products business has particularly benefited from increased infrastructure and construction activity in Russia. Our share of Russia's total production volume of reinforcement bars (rebar) in 2008 was approximately 22% according to Metall-Expert. According to Metall-Expert and Chermet, a Russian ferrous metals industry association ( Chermet ), we are Russia's second largest producer of specialty steel by production volume, accounting for 25% of Russia's total specialty steel output in 2008. Our product range in specialty steel is broader and more comprehensive than other Russian producers, giving us an added advantage in the domestic Russian market.

#### ***High degree of vertical integration***

*Our steel segment is able to source almost all its raw materials from our group companies, which provides a hedge against supply interruptions and market volatility.*

We believe that our internal supplies of coking coal, iron ore and ferroalloys provide us significant advantages over other steel producers, such as higher stability of operations, better quality control of end products, reduced production costs, improved flexibility and planning latitude in the production of our steel and value-added steel products and the ability to respond quickly to market demands and cycles. We believe that the level of our self-sufficiency in raw

materials sets our steel business apart in certain respects: based on publicly available information, we believe we are the world's only steel manufacturer with its own nickel supply, and our acquisition of Oriel Resources in April 2008 has given us the capability to mine our own chrome, which we believe makes us the world's only steel producer with its own chrome supply, based on publicly available information.

In 2008, we internally sourced 60% of the coking coal, 70% of the iron ore concentrate, 80% of the nickel and 100% of the ferrosilicon requirements of our steel segment. We constantly adjust the level of inputs that we source from our group companies on the basis of external economic factors such as market prices and transportation costs,

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as well as internal changes in demand for certain grades or types of materials. We are capable of satisfying approximately 45% of our group's electricity needs from our own generation facilities; in 2008, we satisfied approximately 45% of our electricity needs internally.

We view our ability to source our inputs internally not only as a hedge against potential supply interruptions, but as a hedge against market volatility. From an operational perspective, because our mining, ferroalloys and power assets produce the same type of inputs that our manufacturing facilities use, we are less dependent on third-party vendors and less susceptible to supply bottlenecks. From a financial perspective, this also means that if the market prices of our steel segment's inputs rise, putting pressure on steel segment margins, the margins of our mining, ferroalloys and power segments will tend to increase. The inverse is also true: while decreases in commodities prices tend to reduce revenues in the mining and ferroalloys industry, they also create an opportunity for increased margins in our steel business.

*Our logistics capability allows us to avoid infrastructure bottlenecks, to market our products to a broader range of customers and to reduce our reliance on trade intermediaries.*

We are committed to maximum efficiency in delivering goods to consumers and have been actively developing our own logistics network. Using our own transportation capacity enables us to save costs. We are less exposed to market fluctuations in transportation prices and are able to establish flexible delivery schedules that are convenient for our clients. Our logistics capacities are currently comprised of one river and two sea ports as well as a transport operations company, Mecheltrans, which manages the rail transportation of our products and carries out the overall coordination of our sea and rail transportation logistics for our products.

Mecheltrans is designed to maximize our profitability. The rail operator not only transports Mechel's products but also provides transportation services to third parties, thereby maximizing efficiencies across our transportation network.

We own two seaports and a river port and we have our own rail rolling stock. Port Posiet in Russia's Far East, on the Sea of Japan, allows us easy access to Pacific Rim coal customers and provides a delivery terminal for the coal mined by our subsidiary Yakutugol in eastern Siberia. We are in the process of upgrading Port Posiet, which upon completion will enable us to expand the cargo-handling capacity of the port to 7.0–9.0 million tonnes per year and to accommodate Panamax ships, which will increase its attractiveness and utility as an export port for large volumes of coal. Port Kambarka, on the Kama River in the Udmurt Republic (a Russian administrative region also known as Udmurtia) is connected to the Volga River basin and the Caspian Sea, and is connected by canal to the Don River and the Baltic Sea. In 2007, we increased our strength in cargo shipment logistics with the acquisition of Port Temryuk on the Sea of Azov, an inlet of the Black Sea basin, which is primarily used for coal transshipment and provides us access to the fast-growing economies of the Black Sea basin and beyond. We are focused on construction of a specialized coal transshipment seaport at Vanino in Russia's Far East with a capacity of 25.0 million tonnes per year. As of December 31, 2008, our subsidiary Mecheltrans OOO (Mecheltrans) owned and leased more than 3,800 rail freight cars that we use to ship our products. On June 23, 2008, pursuant to the terms of our license to mine the Elga coal deposit we began construction on a private rail branch line, which we will own and control subject to applicable regulation. This rail branch line will connect the Elga coal deposit to Ulak Station on the Baikal-Amur Mainline, which in turn connects to the Transsiberian Railway, serving European Russia west of the Ural Mountains and eastward to the Pacific Ocean. We anticipate that the Elga branch line not only will provide an avenue for delivery of coal produced at the Elga coal deposit, but will eventually serve as the primary transportation corridor for coal mined in nearby license areas.

### ***One of the lowest-cost coking coal producers worldwide***

*Our coking coal mining and transportation costs are among the lowest of our major Russian competitors.*

We view strict cost management and increases in productivity as fundamental aspects of our day-to-day operations, and continually reassess and improve the efficiency of our mining and metals operations. Approximately 86% of our coking coal production is mined from open pit mines, which we believe based on publicly available information is a greater percentage than any of our major domestic competitors. Open pit mining

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is generally considered safer, cheaper and faster than the underground method of coal mining. Most of our mines and processing facilities have long and established operating histories.

By acquiring Yakutugol in the fourth quarter of 2007, we have secured a high-quality, high-volume coking coal producer with an existing Pacific Rim customer base as well as an opportunity for synergies with our Port Posiet seaport on the Pacific Ocean, which allows us transshipment of various goods in bulk, including coal. Thanks to its convenient geographical position on the Sea of Japan, near the Chinese border south of Vladivostok, and its connection with the Trans-Siberian Railway and highways and other transportation lines connecting the borders of three countries, Port Posiet allows us to optimize the transportation of Mechel's products to the Asia-Pacific region, allowing for year-round utilization of vessels with displacements up to 26,000 tonnes.

*Our coking coal mining costs are lower than those of many of our international competitors.*

Our base of operations in Russia and our high degree of vertical integration allow us to take advantage of a number of cost advantages vis-à-vis many of our international competitors. Having the ability to internally source our materials also gives us better market insight when we negotiate with our outside suppliers and improves our ability to manage our raw material costs. These advantages include lower labor costs, access to power and gas supplies that are inexpensive from an international perspective and our cost savings from producing approximately 86% of our coking coal in open pit rather than underground mines. We internally satisfy nearly a third of our electricity needs from our own co-generation facilities, and purchase the remainder at relatively low, regulated prices. We also purchase natural gas from Gazprom at relatively low, regulated prices for our power generation and other production needs. Based on publicly available information, we believe that Russia has lower labor costs, including fewer pension obligations, as compared to the United States, Western Europe, Japan and South Korea. We believe that our Russian base of operations provides us with cost advantages over many of our international competitors not only in terms of labor and energy costs, but tax and regulatory compliance as well.

We believe that we have a significant competitive advantage over our competitors in our ability to increase our production capacity relatively cost effectively because our substantial existing infrastructure can accommodate new facilities and production lines through brownfield development. Moreover, due to our integration, experience and location in Russia, which has some of the largest deposits of coal and iron in the world, we are better positioned than many of our international competitors to secure raw materials for any increases in steel production.

### ***Strategically positioned to supply key growth markets***

*Our mining and logistical assets are well-positioned to expand exports to fast-growing Asian markets.*

We believe that the geographical locations of our assets, particularly the eastern Siberian coal mines of Yakutugol and its undeveloped Elga coal deposit, are strategically located to expand exports of our products to key Asian markets. With Port Posiet on the Sea of Japan and its annual cargo throughput capacity of 2.5 million tonnes, located within 2,500 kilometers of our eastern Siberian coal assets, we are positioned to expand our exports to key growth markets; this is particularly relevant in respect of coking coal, which we are well-positioned to deliver for steel mills in fast-growing economies in South Asia and East Asia. Our Port Vanino coal transshipment terminal, scheduled to open in 2012, will further reinforce our Far East logistical capabilities. We have a sales and distribution network with offices in four countries and agents in five additional countries. This network facilitated sales constituting 37% and 36% of our total sales in 2008 and 2007, respectively, reducing our reliance on the Russian market in the event that it were to experience a downturn, such as the current one. We view our international marketing capabilities and the proximity of our mining and logistical assets to key fast-growing economies as a key competitive advantage which allows us to diversify our sales, provides us with additional growth opportunities and acts as a hedge in the event of a decrease in demand from customers in Russia.

Our West Virginia coal-mining operations carried out through the BCG companies are situated in West Virginia, just 400 miles from the deep-water port in Norfolk, Virginia, which accepts Capesize vessels. Together with other opportunities to ship from deep ports at Baltimore and New Orleans, we see promising export potential for the BCG companies.

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Historically the BCG companies' key markets have been in North America, but in the last two years, they have expanded their sales to Asia and Europe. We are planning to expand the geography of the BCG companies' sales by using our distribution network.

*Our steel mills are well-positioned to supply Russian infrastructure projects.*

Russia is our most important market and we have significant domestic market shares in all our key specialty steel and rolled long product lines. We believe we have established a strong reputation and brand image for Mechel within Russia, just as we have with our international customers. The location of a number of our core steel segment assets in the southern Urals positions us advantageously, from a geographical and logistical perspective, to serve the areas in Russia west of the Urals where Russia's construction industry is most active. The construction industry has been a key source of our growth and we have captured a large portion of the market; according to Metall-Expert, our share of Russia's total production volume of construction rebar in 2008 was approximately 22%.

### ***Track record of acquisitions***

Along with the expansion of the Russian economy and the increased efficiency of our operations and improved quality of our products, our ability to select acquisition targets and incorporate them into our group has been a key driver of our growth. The potential for synergies within our existing assets and the potential for reducing costs and improving efficiency are key criteria we apply when acquiring companies and assets. Through acquisitions, the nature of the business of our group has changed, expanding our steel product portfolio towards higher-value-added specialty steel products and our upstream product portfolio towards highly-sought grades of coal. Parallel to the expansion in our mining and metals businesses, our expanding logistics capabilities, including our own port facilities and rolling stock, have allowed us to reduce the potential for transportation bottlenecks and maintain and improve our reliability as a supplier to a wider range of customers.

Building upon our success in turning around the coal operations of Southern Kuzbass Coal Company in the late 1990s and following our acquisition and revitalization of Chelyabinsk Metallurgical Plant, in the last few years we have acquired other metal finishing and hardware manufacturing operations, as well as mining, power and ferroalloys operations. As we have acquired and integrated companies that are closer to the end-customers and produce higher-value-added products, the nature of our group has transformed steadily from primarily a raw materials processor to a vertically integrated, logistically coherent mining, steel, ferroalloys and power group that offers customers products from virtually every stage of the industrial process.

With each of our acquisitions, we implement improved operational and management practices. We also analyze each acquisition to determine the minimum capital expenditures necessary to achieve our target increases in productivity and efficiency, both on a per-asset and group-wide basis. We also devote the management, technological and logistical resources necessary to integrate new acquisitions into all aspects of our business, including the supply of raw materials and steel, industrial production and sales and distribution. We have a track record of using existing workforces and maintaining strong relations with the local communities where we operate following our acquisitions.

Our successful track record of identifying, acquiring and integrating target companies that complement our group is due in part to our clearly defined investment criteria, prudent approval procedures and our time-tested ability to identify synergies in target assets that can be quickly implemented while at the same time moving forward with our longer-term strategic goals. Our acquisition program evaluates potential targets to determine whether they conform to our long-term strategy to shift our product mix up the value chain, expand our mining asset base, expand into new markets and strengthen our position in existing markets and reduce costs through improved management and intra-group synergies.

A recent example of our track record of identifying opportunities for efficiency and intra-group synergies relates to Mechel Campia Turzii, which requires steel billets as raw material for its plant. In order to achieve cost savings, we decided to use cast billets supplied by a plant owned by our new Romanian subsidiary Ductil Steel, acquired in April 2008, to replace the billets formerly delivered to Mechel Campia Turzii from our Chelyabinsk Metallurgical Plant, thereby avoiding transportation costs and import duties. In 2008 Mechel Campia Turzii generally operated at a profit. However, in the fourth quarter of 2008 and in the first quarter of 2009 Mechel

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Campia Turzii operated at a loss due to the impact of financial crisis, resulting in sharp decline in demand what in its turn caused cutting in prices. The negative results were also triggered by a large amount of raw materials earlier bought at high (pre-crisis) prices.

Another example of our ability to integrate our subsidiaries while identifying and eliminating inefficiencies is our acquisition of Yakutugol. Yakutugol operated at a loss in the first three quarters of 2007, during which we owned a non-controlling 25% plus one share interest in the company. In October 2007, we acquired the remaining 75% less one share interest in Yakutugol, and in the fourth quarter of 2007, Yakutugol began operating with a profit primarily due to our implementation of effective management techniques. In 2008, Yakutugol also operated with a profit. However, in the first quarter of 2009 Yakutugol operated at a loss. The main reason is sharp decline in demand and prices at coking coal caused by financial crisis.

Our most recent deal is the acquisition of 100% of the shares and interests in the BCG companies, which is Mechel's first experience acquiring and integrating a company outside Eurasia. The strategic reasons for this acquisition include establishing our coal business on a worldwide level, diversifying our customer base and sales geography and improving the quality of our coking coal products. We intend to integrate the BCG companies into our broad marketing network in the near future.

### ***Track record of strong financial performance***

We have experienced year-on-year EBITDA growth of 23% and 55% in the financial years ended December 31, 2008 and 2007, respectively. We have also experienced year-on-year revenue growth of 49%, 52% and 15% in the financial years ended December 31, 2008, 2007 and 2006, respectively. We have been able to finance most of our capital improvements program with cash flow from operations. We have enjoyed access to financing from leading international banks, including during a period of high volatility in the international credit markets. In late 2007, we secured a \$2 billion loan to finance our purchase of Yakutugol and Elgaugol and related assets. In March 2008, we secured a \$1.5 billion loan to finance the acquisition of Oriel Resources. See Item 5. Operating and Financial Review and Prospects Description of Certain Indebtedness.

We understand that even in the current difficult economic situation on world markets, it is important to maintain our capital improvements program in order to keep up the quality of existing assets and preserve our capacity to ramp up production in response to market conditions. See Capital Improvements Program.

However, due to the world financial crisis developing in the fourth quarter of 2008, as of December 31, 2008, we were in breach of a number of financial and non-financial covenants (as discussed in detail in note 15 to our consolidated financial statements in Item 18. Financial Statements ) and as a result, the lenders can request accelerated repayment of a substantial portion of our long-term debt. As of December 31, 2008, we had \$5.1 billion of loans repayable during 2009 including \$1.6 billion of long-term debt that was classified as short-term liabilities as of that date because of the covenant violations. We do not have the resources to enable us to repay the total of these loans if repayment were called.

We have commenced discussions with our bankers about additional facilities to be provided on a long-term basis. We are also seeking to refinance and/or restructure the terms and conditions of our existing debt to extend maturities beyond 2009 and provide greater working capital flexibility. We are currently in negotiations with our creditor banks, but it is likely that the terms and agreement on the conditions of these borrowing arrangements will not be completed until the second half of 2009.

We have concluded that the uncertainty about the refinancing and restructuring of our outstanding debt described above represent a material uncertainty that casts significant doubt upon our ability to continue as a going concern.

Based on our plans as noted herein, we believe that we have, or will secure, adequate capital resources and liquidity to continue in operational existence for the foreseeable future and have presented our consolidated financial statements on a going concern basis of accounting.

Following the onset of the world financial crisis, our net income of \$1,637.4 million achieved in the nine months ended September 30, 2008 was partially offset by the net loss of \$496.9 million we incurred in the fourth quarter of 2008.

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### **Strong and focused management team**

Our current management team has significant experience in all aspects of our businesses and has successfully transformed us from a small coal trading operation to a large, integrated coal, steel, ferroalloys and power producer. Mr. Zyuzin, our controlling shareholder, is our Chief Executive Officer. Mr. Zyuzin has over 22 years of experience in the coal mining industry and has a doctorate in coal mining technical sciences. Chief Executive Officer of Oriel Resources Ltd., Alexey Ivanushkin, has significant experience from his previous positions at Glencore International and as chief executive officer at Chelyabinsk Metallurgical Plant. Our Senior Vice President, Vladimir Polin, has almost 25 years of production-floor, marketing and management experience in the metals business. Many of our directors and officers began their careers in technical positions in mines and manufacturing facilities and moved up to senior management positions over the course of their careers.

### **Business Strategy**

Our long-term goal is to expand our mining business, through organic growth as well as through acquisitions; to improve our steel segment margins through plant modernization, cost cutting and product portfolio optimization; to maintain our strong position as a producer of carbon and specialty long steel products in Russia; and to capitalize on the synergies deriving from our status as an integrated mining, steel, ferroalloys and power group. We also intend to leverage our core businesses, where appropriate, with acquisitions of value-added downstream businesses.

Due to the world economic crisis, it has become more difficult to increase our profits and expand business by way of new acquisitions. Nevertheless, we continue to work on the development of the Elga coal deposit, which we expect to allow us to significantly increase our coal production. We are focused on cost cutting and optimizing our product portfolio, increasing labor productivity and other anti-recessionary measures.

Our group is a leader by production volume of specialty steel in Russia. The manufacturing of specialty steel requires the use of various types of ferroalloys. The assets acquired with Oriel Resources in April 2008 gave us our own chrome and nickel deposits in Kazakhstan. The existence of these assets within our group provide operational synergies and increase our competitiveness.

Expansion of our power segment, comprising one sales and two generating assets, enables us to supply electricity within our group, as well as gain a profit from supplies of end products to third parties. Producing electricity and heat energy from the steam coal produced by our mining segment is part of our overall strategy to move our end products up the value chain and sell higher value-added products to customers.

Our acquisition of the BCG companies is expected to strengthen the position of our mining segment on the international coking coal market, making it one of the world's leading producers with additional pricing leverage. We are assessing the possibility of increasing the BCG companies' annual production up to 7 million tonnes of high-quality hard coking coal concentrate from 2.5 million tonnes. We intend to include the BCG companies in the general development strategy of our group.

The key elements of our strategy include the following:

#### ***Enhancing our position as a leading mining, metals and ferroalloys group***

*We plan to develop our existing reserves base.*

We intend to build on our substantial mining experience by developing our existing coal and iron ore reserves, particularly in order to sell more high-quality coking coal and iron ore concentrate to third parties. We plan to increase

our coal production from 26 million tonnes in 2008 to 37 million tonnes in 2012, and maintain our iron ore concentrate production at the level of at least 5.0 million tonnes, with a possible increase in iron ore production by 10-15% by 2012 due to upgrades to the Korshunov Mining Plant. See Capital Improvements Program. We intend to expand the production of Voskhod chrome ore deposit to 1.3 million tonnes and to start the exploration of nickel ores at the Shevchenko deposit in Kazakhstan, as well as to fully commission the Tikhvin Ferroalloy Plant in Russia, which produces carbon ferrochrome. We plan to further develop our ferroalloy production at Bratsk Ferroalloy Plant through the acquisition in 2008 of a license to mine quartzite, a raw material for ferrosilicon production, for the Uvatskoye deposit in the Irkutsk region.

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We intend to develop our acquired coking and steam coal reserves owned by Yakutugol. Yakutugol, which has three producing mines as well as two licenses for the undeveloped Elga coal deposit and the Piatimetrovy and Promezhutochny Seam parcel, holds mining rights to reserves that we believe will solidify our position as a leading world producer of coking coal for years to come. We intend to seek additional mining licenses through acquisitions and/or participation in auctions and tenders in view of our strategic plans and market dynamics. In particular, we believe that obtaining additional mining rights near the Elga coal deposit would allow us to realize more fully the potential benefit of the private rail branch line we are constructing to deliver Elga's future coal production to market.

*We intend to increase our group's output of high-value-added steel products and continue to optimize our product mix.*

We plan to continue our approach of selectively investing in technology and capital improvements, including expanding the use of continuous casters (concasters) in our steel manufacturing facilities, optimizing our product catalog and cutting production costs. We have already built a solid presence in the construction steel business, including the second largest market share in rebar, according to Metall-Expert based on Russian production volumes in 2008. We are also a market leader in wire rod production and have a strong presence in the construction steel market. We are also one of Russia's primary producers of specialty steel, having the second largest market share, according to Chermet and Metall-Expert based on Russian production volumes in 2008.

*We intend to continue to seek out acquisition and expansion opportunities and realize the maximum potential from our completed acquisitions.*

Our strategy involves finding acquisition and expansion opportunities that we believe will reinforce or complement our existing business lines. We actively monitor global mining and metals markets for new opportunities. In 2007, we completed a series of acquisitions that added a power segment to our group. In keeping with our long-term strategy of vertical integration, our strategy envisions realizing the maximum benefit from our own power generating facilities. We also intend to increase our presence and capability in ferroalloys, with the aim of positioning ourselves to be a leader in what we believe will be a high-margin business going forward. Our 2007 acquisition of Bratsk Ferroalloy Plant and our 2008 acquisition of Oriol Resources, which includes the Tikhvin Ferroalloy Plant in Russia and the Voskhod chrome ore and Shevchenko nickel deposits in Kazakhstan, have allowed us to form a ferroalloys segment within our group. With these acquisitions we became self-sufficient not only in nickel, but chrome as well, which we believe gives us a rare competitive advantage among world steel producers.

An example of expansion in steel, a business line where we are already a well-established leader by production volume in Romania as well as Russia, is our April 2008 purchase of Ductil Steel, a company with two steel plants in Romania. Before this acquisition, we had already owned two steel plants in Romania: Mechel Targoviste and Mechel Campia Turzii. Following our acquisition of Ductil Steel, in order to enhance the performance and efficiencies of our Romanian subsidiaries, we established the Mechel East Europe Metallurgical Division effective from October 22, 2008.

An example of expansion in coal is our May 2009 acquisition of 100% of the shares and interests of the BCG companies, which is a West Virginia-based coal business engaged in the mining, processing and sale of premium quality hard coking coal.

After stabilization on financial and commodities markets we hope to continue to seek out opportunities to expand our group through acquisitions, including by obtaining new subsoil licenses in Russia and abroad. In doing so, we seek to maintain and expand our presence in regions with low costs and high economic growth potential. We intend to continue to selectively acquire value-added downstream businesses such as hardware, stampings and forgings producers to help us reach our customer base, including in new markets. This downstream integration:

is a logical extension of our specialty and low-carbon long product lines, representing a higher-margin, next value-added step for products that we already manufacture;

is in a market less cyclical than the upstream market, reducing our exposure to market downturns and commodity price fluctuations; and

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moves us closer to our final customers, enabling us to better understand customer needs, influence buyer behavior and respond quickly to change.

***Maintaining a high degree of vertical integration***

*We intend to maintain the flexibility to source our inputs internally as circumstances require.*

Our recent expansion of our ferroalloy mining, processing and manufacturing capacity, with the acquisition of Bratsk Ferroalloy Plant (which produces ferrosilicon used in all steel manufacturing) and the Oriel Resources assets (which we expect to more than double our capacity to mine and process ferroalloys used to make steel), is consistent with our strategy to maintain the potential to source our materials as our product focus shifts to higher-value-added steel products. We have expanded our power generation and distribution business into a separate financial reporting segment; we see expansion of our electric power capabilities not only as a diversification measure and a way to market another value-added product made from our coal, but also as a way to have more control over our energy efficiency and hedge against increases in the price of the electricity our facilities use. However, even as we expand and develop our internal sourcing capability we intend to adhere to our longstanding approach of purchasing inputs from third-party suppliers and selling products, including raw materials, to domestic and international customers in a way that we believe creates the most advantageous profit opportunities for our group. The BCG companies' acquisition enlarges our coking coal portfolio, adding high quality hard coking coal with low ash content to the grades of coal we produce. This allows us better flexibility not only to serve our coking coal consumers, but also to use these grades internally in our coke production, if needed because of market conditions.

*We plan to expand our logistical capabilities.*

We intend to selectively expand our logistics capabilities, currently centered on our railway freight and forwarding company, and enhanced by our acquisitions of Port Posiet, Port Kambarka and Port Temryuk and the construction of Port Vanino, strategic acquisitions designed to help us optimize our transportation expenses. We have engaged project engineers in preparation for the construction of a rail branch line to the Elga coal deposit in eastern Siberia and the design and construction of the Port Vanino Complex.

*We will leverage synergies among our core businesses.*

In addition to synergies derived from our status as an integrated group, we believe that additional cost savings and opportunities will arise as we benefit from economies of scale and continue to integrate recent acquisitions, in particular by implementing improvements in working practices and operational methods. We regularly evaluate the manner in which our subsidiaries source their raw material needs and transfer products within the group in order to operate in the most efficient way, and we expect to identify and take advantage of further synergies among our core businesses.

***Continuing to enhance our low-cost position in coal and improve steel segment margins***

*We aim to improve our steel segment margins through plant modernization, cost-cutting and product portfolio optimization.*

We intend to further increase our efficiency and reduce our manufacturing costs by:

preserving cost advantages in our labor, raw materials and energy inputs;

achieving additional savings by fully integrating recent acquisitions into our operations;

producing higher value-added products, such as electricity and heat energy;

cultivating additional markets for steam coal; and

providing our mining and steel segments with their own energy resources.

Our ongoing plant modernization program is aimed at maintaining capacity at the present level, increasing efficiency and reducing the environmental impact of our operations. In line with this strategy, in 2007 and 2008 we completed a \$17.0 million modernization of the concaster and a \$13.2 million reconstruction of mill No. 380 at Mechel Targoviste. During that period we also commissioned a \$12.3 million shaft furnace at Southern Urals Nickel

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Plant, finished a \$29.0 million overhaul of a rebar rolling mill at Chelyabinsk Metallurgical Plant, made a \$33.7 million extension of a sintering unit at Chelyabinsk Metallurgical Plant and completed a \$22.0 million air separation complex at Chelyabinsk Metallurgical Plant and constructed a \$10.8 million ring rolling mill at Urals Stampings Plant. In continuation of this strategy in 2009 and beyond, we aim to realize projects to construct the universal rail and structural steel mill at Chelyabinsk Metallurgical Plant and modernize the electric arc furnace at Izhstal. See **Capital Improvements Program**.

We intend to maintain our position as a low-cost producer of coal, despite an ongoing worldwide economic and financial crisis which has negatively impacted the economic development of Russia and other countries. We are analyzing our production costs, considering ways to achieve maximum synergies from the integration of the BCG companies in order to reduce mining production costs and costs of sales.

We plan to increase our efficiency and reduce production costs by:

optimizing production plans;

additional saving by increasing labor efficiency and loading mining equipment; and

retaining current advantages related to labor, raw materials and power costs.

*We will strive to maintain strong export sales.*

We intend to maintain strong relationships with our significant international customers. Although we are focused on growing our market position within our domestic markets (of which Russia is by far the largest), export sales, which constituted 38% of our total sales revenues in 2008, allow us to diversify our sales and reduce our reliance on the domestic market in the event that it were to experience a downturn. In our key export markets our steam coal customers include cement companies such as Sumitomo Osaka Cement Co., Ltd. and Taiheiyo Cement Corporation in Japan, Holcim Ltd. in Europe, and Oytash Ic Ve Dis Ticaret A.Ş., Akansa Cimento Sanayi Ve Ticaret A.Ş. and Lafarge Aslan Cimento A.Ş. in Turkey; as well as power generating companies such as OVA Elektrik A.Ş. in Turkey, Korea South East Power Co., Ltd. in South Korea, and RWE AG, DONG Energy A/S and Varna Power Plant in Europe. Our coking coal customers include ArcelorMittal, Kazzinc and Kazchrome JSC in Kazakhstan, various metal manufacturing facilities in Ukraine, JFE Steel Corporation, Nisshin Steel Co. Ltd, Kobe Steel, Mitsui Mining and Sumitomo Metal Industries, Ltd. in Japan, the Pohang Iron and Steel Company (POSCO) in South Korea, Saurashtra Fuel Ltd. in India, and Capital Iron and Steel Plant in China. Another E.U. customer is the Solvay Sodi chemical plant in Bulgaria. In our key export markets our product pricing policy is generally based on the current market price, our price forecasts and actual supply-and-demand dynamics.

### ***Continuing expansion in high-growth markets***

*We plan to increase coking coal sales to high-growth international markets.*

We intend to continue to capitalize on our ability to serve fast-growing Asian and other international markets. In particular we view Japan, China, South Korea and India as countries to which our international growth strategy will be applied.

### ***Developing our domestic and export steel sales capabilities***

Our continued focus on the domestic Russian market is a key element of our strategy. We are particularly well-positioned to supply construction and infrastructure projects in Russia from our Chelyabinsk Metallurgical Plant

located in the southern Urals. Not only do our products and prices tend to appeal to Russian customers, but the geographical reach of our production and logistics facilities and sales network give us a presence in the Russian heartland that facilitates sales to customers in Russia's remote regions. For example, our domestic trading subsidiary Mechel-Service has over 50 offices in various cities in Russia.

Following the strategy of broadening our presence in regions of interest, Mechel-Service has established a branch in Kazakhstan and Romania, and acquired 100% stake in German steel trading and service company HBL Holding in September 2008. HBL Holding's activities comprise trading of steel, stainless steel and aluminum

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products, and non-ferrous metals, warehousing and processing. HBL Holding has eight regional sites to serve the local clients. All sites are located in Germany in North Rhine-Westphalia, Bremen and Saxony-Anhalt.

Our extensive operations in Romania, consisting of four steel mills, serve as an attractive platform to expand our steel product sales to the important export markets of the E.U.

Implementation of these strategies is subject to a number of risks. See **Item 3. Key Information** **Risk Factors** for a description of these risks.

### ***Restructuring of mining and ferroalloy assets***

In April 2008, we established Mechel Mining OAO ( **Mechel Mining** ), a wholly-owned subsidiary in which we consolidated the coal and iron ore assets of our mining segment (Southern Kuzbass Coal Company, Korshunov Mining Plant and Yakutugol).

In 2008, we consolidated our ferroalloy assets under our wholly-owned subsidiary Oriol Resources, on the basis of which we established a ferroalloys reporting segment that includes the nickel mining and production business of Southern Urals Nickel Plant, ferrosilicon producer Bratsk Ferroalloy Plant, along with the assets acquired with Oriol Resources ferrochrome producer Tikhvin Ferroalloy Plant and the Voskhod chrome and Shevchenko nickel projects in Kazakhstan. In the course of the consolidation we formed Mechel Ferroalloys Management OOO ( **Mechel Ferroalloys Management** ), a management company that acts as the executive body of each of the companies in our ferroalloys segment.

In connection with this restructuring we have been implementing management, reporting and control systems for each such subsidiary holding company, allowing for the preparation of consolidated financial statements for each of them. We believe that such separation and consolidation will enable these businesses to obtain the financing necessary for their development and will enable us to optimize their value within our group, including through more focused operational management teams. Such financings may include the issuance and/or sale of both bonds and shares, including the sale of equity securities in connection with a listing on an international stock exchange.

We intend to retain a controlling voting interest in each of these subsidiary holding companies as we continue to build upon our business model of vertical integration among our assets. See **Risk Factors** **Risks Relating to Our Business and Industry** If shares of our subsidiary holding companies are listed on a stock exchange, it could entail changes in such companies' management and corporate governance that might affect our integrated business model.

## **Our History and Development**

### ***General***

We trace our beginnings to a small coal trading operation in Mezhdurechensk in the southwestern part of Siberia in the early 1990s. See **Item 5. Operating and Financial Review and Prospects** **The Reorganization**. Since that time, through strategic acquisitions in Russia and abroad, Mechel has developed into a large, integrated mining, steel, ferroalloys and power group, comprising coal, iron ore, nickel, chrome ore and limestone assets and coke, steel and ferroalloy production, with operations and assets in Russia, Romania, Bulgaria, Lithuania, Kazakhstan and the United States. With each of our acquisitions, we implement improved operational and management practices, and we are generally able to realize significant increases in production efficiency and volume with only modest, targeted capital expenditures. We also devote the management, technological and logistical resources necessary to integrate new acquisitions into all aspects of our business, including the supply of raw materials and steel, production methodologies and sales and distribution.

## **Mining Business**

### *Mining process*

*Coal.* Coal is mined using open pit or underground mining methods. Following a drilling and blasting stage, a combination of shovels and draglines is used for moving coal and waste at our surface mines. Production at the underground mines is predominantly from longwall mining, a form of underground coal mining where a long wall of coal in a seam is mined in a single slice. After mining, depending upon the amount of impurities in the coal, the

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coal is processed in a wash plant, where it is crushed and impurities are removed by gravity methods. Coking coal concentrate is then transported to steel plants for conversion to coke for use in pig iron smelting. Steam coal is shipped to power utilities which use it in furnaces for steam generation to produce electricity. Our primary coal products are coking and steam coal concentrate and raw, size-sorted steam coal. Among the key advantages of our mining business is the high quality of our coking coal, the low level of volatile matter in our steam coal and our modern coal washing facilities, primarily built during the 1970s and 1980s, including facilities built as recently as 2001-2002.

*Iron ore.* All three of our iron ore mines are conventional open pit operations. Following a drilling and blasting stage, ore is hauled by rail hopper cars to the concentrator plant. At the concentrator plant, the ore is crushed and ground to a fine particle size, then separated into an iron ore concentrate slurry and a waste stream using wet magnetic separators. The iron ore is upgraded to a concentrate that contains about 62.9% elemental iron. Tailings are pumped to a tailings dam facility located adjacent to the concentrating plant. The concentrate is sent to disk vacuum filters which remove the water from the concentrate to reduce the moisture level, enabling shipment to customers by rail during warmer months, but in colder periods the concentrate must be dried further to prevent freezing in the rail cars. Korshunov Mining Plant operates its own drying facility with a dry concentrate production capacity of up to 16,000 tonnes per day.

*Limestone.* Our limestone mining operation uses conventional mining technology. Ore is drilled and blasted, then loaded with electric shovels into haul trucks. Relatively minor amounts of waste are hauled to external dumps. The ore is hauled to stockpiles located adjacent to the crushing and screening plant. Ore is crushed, screened and segregated by size fraction. The crushed limestone is separated into three product categories for sale: 0-20 millimeters, 20-40 millimeters and 40-80 millimeters.

### ***Description of key products***

*Coking coal and coking coal concentrates.* Coking coal is washed, low-phosphorous bituminous coal designated for further processing into coke in coking furnaces, which in turn is used in the blast furnace in the production of pig iron, a precursor of steel in integrated steel mills. Coking coals have high plasticity, meaning that they are amenable to being softened, liquefied and resolidified into hard and porous lumps when heated in the absence of air. From our Southern Kuzbass Coal Company and Yakutugol we offer coking coal of marks OS (meager and caking), KS (coking and caking), KS (blend), KO (coking and meager) and K9 (coking). We process coking coal into coking coal concentrate to reduce ash content and increase volatility and plasticity. We offer coking coal concentrate of marks OS (meager and caking), KO (coking and meager), KS (coking and caking) and K9 (coking). The BCG companies, our West Virginia operations, produce low, medium and high volatility metallurgical hard coking coal. Metallurgical coals can be mixed in different proportions to provide blends with the best characteristics for any specific customer. Blending takes place directly in port when loading to a vessel, without any additional washing at processing plants. This approach saves money and provides a competitive advantage over competitors with higher processing costs.

*Steam coal and steam coal concentrates.* Steam coal has properties that make it suitable for use in thermal applications, including electric power generation. From our Southern Kuzbass Coal Company we offer steam coal and steam coal concentrate of marks T (lean) and A (anthracite) various grain-size class, GZhO (gas, fat and meager), TR (lean and run-of-mine). We also offer steam coal from Yakutugol of marks 3SS (weakly to non-caking), K6 (coking and oxidized), D (long-flame) and B2 (brown category 2). The BCG companies, our West Virginia operations, produce medium and high volatility bituminous steam coal.

*Other coal products.* From our Southern Kuzbass Coal Company we also offer our customers middlings and anthracite concentrates of various grades.

*Iron ore concentrate.* From our Korshunov Mining Plant we offer iron ore concentrate with a standard iron weight fraction of 62%.

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The following table sets forth third-party sales of mining products (by volume) and as a percentage of total sales (including intra-group sales) for the periods indicated.

Product	2008	2007	2006	2008	2007	2006
	(In thousands of tonnes <sup>(1)</sup> )			(% of total sales, including intra-group)		
Coking coal concentrate <sup>(2)</sup>	8,360	6,018	6,603	77%	62%	73%
Steam coal <sup>(2)</sup>	8,543	7,230	6,728	90%	96%	100%
Iron ore concentrate	2,713	2,358	2,885	58%	51%	56%

(1) Includes resales of mining products purchased from third parties.

(2) Includes only post-acquisition volumes of Yakutugol.

The following table sets forth revenues by product, as further divided between domestic sales and exports (including as a percentage of total mining segment revenues) for the periods indicated:

Revenues	2008		2007		2006	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
(In millions of U.S. dollars, except for percentages)						
Coking coal concentrate	1,861.1	55.8%	622.9	45.4%	518.3	49.6%
Domestic Sales (%)	49.7%		83.7%		74.0%	
Export (%)	50.3%		16.3%		26.0%	
Steam Coal	925.0	27.8%	436.3	31.8%	311.1	29.7%
Domestic Sales (%)	11.4%		12.5%		21.0%	
Export (%)	88.6%		87.5%		79.0%	
Iron ore concentrate	339.4	10.2%	213.6	15.6%	168.2	16.1%
Domestic Sales (%)	23.5%		67.7%		98.0%	
Export (%)	76.5%		32.3%		2.0%	
Other <sup>(1)</sup>	207.9	6.2%	99.7	7.2%	48.1	4.6%
Total	3,333.4	100%	1,372.5	100%	1,045.7	100%
Domestic Sales (%)	39.4%		59.8%		63.1%	
Export (%)	60.6%		40.2%		36.9%	

(1) Includes revenues from transportation, distribution, construction and other miscellaneous services provided to local customers.

**Marketing and distribution**

Our mining products are marketed domestically primarily through Mechel Trading House and Mechel-Service and internationally through Mechel Trading's branch in Liechtenstein. The following table sets forth by percentage of sales the regions in which our mining segment products were sold for the periods indicated:

<b>Region<sup>(1)</sup></b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
Russia	39.5%	59.5%	63.1%
Other CIS	9.1%	13.3%	12.8%
Europe	14.2%	10.8%	14.0%
Asia	32.1%	12.9%	5.6%
Middle East	2.5%	3.5%	4.5%
Other regions	2.6%		
Total	100%	100%	100%

(1) The regional breakdown of sales is based on the geographic location of our customers, and not on the location of the end users of our products, as our distributor customers resell and, in some cases, further export our products.

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In 2008, the five largest customers of our mining products were EvrazResurs Trading House OOO and West Siberian Metallurgical Plant OAO ( ZapSib ) (coking coal concentrate, iron ore concentrate), Magnitogorsk Metallurgical Plant OAO (coking coal concentrate), Novolipetsk Metallurgical Plant OAO (coking coal concentrate), Rutek Trading AG (coking coal concentrate, steam coal), Sumitomo Corporation (coking coal concentrate, steam coal), which together accounted for 36% of our mining segment sales.

<b>Customer</b>	<b>% of Total Mining Segment Sales</b>	<b>Product</b>	<b>% of Total Products Sales</b>
EvrazResurs Trading House OOO and West Siberian Metallurgical Plant OAO ( ZapSib )	9.7%	Coking coal concentrate	13.3%
Magnitogorsk Metallurgical Plant OAO	9.7%	Iron ore concentrate	22.4%
Novolipetsk Metallurgical Plant OAO	6.4%	Coking coal concentrate	17.4%
Rutek Trading AG	5.7%	Coking coal concentrate	11.4%
		Steam coal	8.5%
Sumitomo Corporation	4.0%	Steam coal	3.3%
		Coking coal concentrate	1.0%
		Steam coal	12.5%

*Domestic sales*

We generally do not involve intermediaries in the domestic distribution of our mining products. Our domestic coking and steam coal and iron ore customers are generally located in large industrial areas and have had long-standing relationships with us.

We ship our coking coal concentrate from our coal washing facilities, located near our coal mines and pits, by railway directly to our customers, including steel producers. Our largest domestic customer for our coking coal concentrate was MMK, accounting for 17% of our total coking coal concentrate sales and 10% of our total mining segment sales in 2008. On March 19, 2009, MMK sued a trading subsidiary of ours seeking to invalidate MMK's long-term coking coal supply contract with us. On June 11, 2009, the court denied the claim, but this decision may be appealed. See Item 8. Financial Information. Litigation – Commercial litigation.

Far Eastern Generating Company OAO, is our largest domestic customer of steam coal, accounting for 2.0% of our total steam coal sales and 0.5% of our total mining segment sales in 2008. We ship our steam coal from our warehouses by railway directly to our customers, which are predominantly electric power stations. Our supply contracts for steam coal are generally concluded with customers on a long-term basis. Some of our steam coal is consumed within the group; for example, sales of steam coal and middlings (lower-quality coal) from our Southern Kuzbass Coal Company to our Southern Kuzbass Power Plant were \$20.7 million in 2008.

Iron ore concentrate is shipped via railway directly from our Korshunov Mining Plant to customers. Our largest domestic customer, ZapSib, accounted for 22% of our total iron ore concentrate sales and 2% of our total mining segment sales in 2008. We set our prices on a monthly basis. EvrazHolding's ironworks, together with ZapSib, is also among our largest domestic coking coal customers. EvrazHolding purchases our coking coal through its subsidiary company EvrazResurs Trading House OOO. This company accounted for 13% of our coking coal concentrate sales and 7% of our total mining segment sales in 2008.

Since 2001, Mechel Trading House has operated its wholly owned subsidiary, Mecheltrans, a railway freight and forwarding company. Mecheltrans owns its own rail rolling stock, consisting of 216 open cars and 213 pellet cars, leases 1,377 open cars and has 2,280 open cars under equipment lease finance terms. The company transported domestically approximately 37.9 million tonnes of our cargo in 2008, approximately 55% of which was comprised of coal and iron ore.

Pursuant to a directive from the FAS dated August 14, 2008, we entered into long-term coking coal supply contracts with some of our major domestic customers. These new contracts provide for the supply of coking coal concentrate under a fixed price based on the price of premium hard coking coal under one-year contracts under FOB terms from Australian ports, excluding the costs of transshipment and rail transportation with the application of a

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coefficient representing the quality of the coal concentrate. Previously, the delivery terms for most of our major domestic customers provided for sale at spot market prices.

The long-term contracts were entered into with MMK, EvrazResurs, Severstal, KOKS, Metalltrade for terms of four and five years for a total annual volume of delivery from four to five million tonnes of coking coal. However, MMK, one of our major domestic customers with which we have entered into a five-year contract for delivery of a total of 12 million tonnes of coking coal, has filed a lawsuit in a Russian court seeking rescission of its contract. See Item 8. Financial Information Litigation Commercial litigation.

### *Export sales*

We export coking coal, steam coal concentrate, low bituminous and anthracite steam coal, and iron ore concentrate.

In the year ended December 31, 2008, the largest foreign customer of our mining segment was Rutek Trading AG, accounting for 6% of our total mining segment sales. Rutek Trading's purchases from Mechel consisted of coking coal concentrate (84%) and steam coal (16%).

We are Russia's largest exporter of coking coal concentrate, according to RasMin. Our exports of coking coal concentrate primarily go to Japan, Ukraine, South Korea and India. In 2008, Rutek Trading AG was our largest foreign customer of coking coal concentrate, accounting for 9% of our total coking coal concentrate sales and 5% of our total mining segment sales by revenue. Shipments are made by rail.

Our exports of steam coal are primarily to Japan, Bulgaria, Belgium, Turkey and Spain, which together accounted for 55% of our total steam coal sales and 15% of our total mining segment sales by revenue in 2008. Our largest foreign customers of steam coal were Sumitomo Corporation and Toplofikatsia Rousse. Steam coal is shipped to customers from our warehouses by railway and, in some cases, further by ship from Russian and Ukrainian ports.

Our Port Posiet processed 2.8 million tonnes of cargo, mostly coal, in 2008. We ship primarily our steam coal and coking coal concentrate to Japan from Port Posiet. The port's current capacity is approximately 3.0 million tonnes of annual cargo-handling throughput and 200,000-220,000 tonnes of warehousing capacity depending on coal type. The port's proximity to roads and rail links to key product destinations and transshipment points in China and Russia make it a cost-effective link in the logistical chain for bringing our Far East coal production to market.

In 2008, we increasingly used long-term contracts for export sales of coking and steam coal as compared to the 2007 financial year. Coal not shipped under long-term contracts was sold on a spot market.

We also sold iron ore concentrate to customers in China during 2008, which accounted for 77% of our total iron ore concentrate sales and 8% of our total mining segment sales in 2008. We ship iron ore concentrate to China by rail and by sea.

### ***Market share and competition***

#### *Coal*

As a result of upstream acquisitions primarily by steel producers, based on publicly available information, we estimate that the number of Russian coal producers has decreased from about 250 in the mid-1990s to less than 60 in 2008. Based on our industry contacts and publicly available information, we believe that over the last few years, Russian coal mining companies have generally enjoyed a relatively stable customer base.

According to data from the Central Dispatching Department, in 2008 we were the largest coking coal producer in Russia, with a 22% share of total production by volume, and we had a 8% market share with respect to overall Russian coal production by volume. We also controlled 26% of the coking coal washing facilities in Russia by capacity at the end of 2008, according to RosInformUgol. The following table lists the main Russian coking coal

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producers in 2008, the industrial groups to which they belong, their coking coal production volumes and their share of total Russian production volume.

<b>Group</b>	<b>Company</b>	<b>Coking Coal Production (Thousands of Tonnes)</b>	<b>% of Coking Coal Production by Volume</b>
Mechel OAO	Southern Kuzbass Coal Company OAO	7,094	10.3%
	Yakutugol Holding Company OAO	8,053	11.7%
	Mechel total	15,147	22.1%
Raspadskaya OAO Severstal OAO	Raspadskaya ZAO	9,329	13.6%
	Vorkutaugol OAO	6,167	9.0%
	Vorgashorskaya Mine OAO	549	0.8%
	Yunyaginskoye OOO	203	0.3%
	Severstal total	6,919	10.1%
Sibuglemet Holding	Polusukhinskaya Mine OAO	3,010	4.4%
	Mezhdurechye OAO <sup>(1)</sup>	3,250	4.7%
	Antonovskaya Mine ZAO	1,454	2.1%
	Bolshevik Mine OAO	932	1.4%
	Sibuglemet total	8,646	12.6%
Evraz Group S.A. Kuzbassrazrezugol Coal Company OAO SUEK OAO Other	Yuzhkuzbassugol Coal Company ZAO	8,387	12.2%
	Kuzbassrazrezugol Coal Company OAO	4,619	6.7%
	SUEK OAO (Kemerovo region)	2,740	4.0%
	Other	12,875	18.8%
Total		68,662	100%

Source: Central Dispatching Department.

(1) We own 16.1% of Mezhdurechye OAO.

A sharp decrease in demand for coking coal from our domestic customers led to a decrease in our coking coal production in the first quarter of 2009. As a result, we have lost our volume based leading position in Russian coking coal production, according to the Central Dispatching Department's report for the first quarter of 2009. We have produced 1.0 million tonnes of coking coal in the first quarter of 2009, which is 8.4% of total Russian coking coal production, according to the Central Dispatching Department.



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According to data from the Central Dispatching Department, in 2008, we were the third largest steam coal producer in Russia in terms of volume, with a 5.7% share of total production. The following table lists the main Russian steam coal producers in 2008, the groups to which they belong, their steam coal production volumes and their share of total Russian steam coal production volume.

<b>Group</b>	<b>Company</b>	<b>Steam Coal Production (Thousands of Tonnes)</b>	<b>% of Steam Coal Production by Volume</b>
SUEK OAO	SUEK Kemerovo region	27,552	10.6%
	SUEK Krasnoyarsk region	36,990	14.2%
	SUEK Khakasian Republic	8,382	3.2%
	SUEK Irkutsk region	5,766	2.2%
	SUEK Zabaikalsky region	4,526	1.7%
	SUEK Primorsky region	4,457	1.7%
	Urgalugol OAO	2,278	0.7%
	<b>SUEK total</b>	<b>87,673</b>	<b>33.7%</b>
Kuzbassrazrezugol Coal Company OAO	Kuzbassrazrezugol Coal Company OAO	44,667	17.2%
	Mechel OAO	11,403	4.4%
	Yakutugol Holding Company OAO	3,463	1.3%
		<b>Mechel total</b>	<b>14,866</b>
SDS-Ugol Holding Company OAO	Barzasskoye Partnership OOO	159	0.1%
	Chernigovets ZAO	4,680	1.8%
		<b>SDS-Ugol total</b>	<b>4,839</b>
Evraz Group S.A. LUTEK OAO Zarechnaya Mine OAO Priargunskoye Industrial Mining and Chemical Amalgamation OAO Other	Yuzhkuzbassugol Coal Company ZAO	4,645	1.8%
	LUTEK OAO	5,322	2.0%
	Zarechnaya Mine OAO	4,441	1.7%
	Priargunskoye Industrial Mining and Chemical Amalgamation OAO	4,011	1.5%
		<b>Other</b>	<b>89,723</b>
<b>Total</b>		<b>260,186</b>	<b>100%</b>

Source: Central Dispatching Department.

In the domestic coal market, we compete primarily on the basis of price, as well as on the basis of the quality of coal, which in turn depends upon the quality of our production assets and the quality of our mineral reserves. Competition in the steam coal market is also affected by the fact that most steam power stations were built near specific steam coal sources and had their equipment customized to utilize the particular type of coal produced at the relevant local source. Outside of Russia, competition in the steam coal market is largely driven by coal quality, including volatile matter and calorie content.

*Iron ore*

The Russian iron ore market is generally characterized by high demand and limited sources of supply, with product quality as the main factor driving prices. According to Rudprom, the market is dominated by relatively few producers, with the top three mining groups representing over 72% of total production of iron ore concentrate.

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The following table lists the main Russian iron ore concentrate producers in 2008, the groups to which they belong, their iron ore concentrate production volumes and their share of total Russian production volume.

<b>Group</b>	<b>Company</b>	<b>Iron Ore Concentrate Production (Thousands of Tonnes)</b>	<b>% of Total Production</b>
Metalloinvest OOO	Lebedinsky GOK	19,732	21.0%
	Mikhailovsky GOK	15,718	16.7%
	Metalloinvest total	35,450	37.7%
Evraz Group S.A.	Kachkanarsky GOK	8,635	9.2%
	Vysokogorsky GOK	1,663	1.8%
	EvrazRuda	7,358	7.8%
	Evraz Group total	17,656	18.8%
Severstal-Resurs OAO	Kostomukshinsky GOK	9,855	10.5%
	Olenegorsky GOK	4,675	5.0%
	Severstal-Resurs total	14,530	15.5%
NLMK OAO	Stoylensky GOK	11,484	12.2%
Yevrokhim OAO	Kovdorsky GOK	5,423	5.8%
Mechel OAO	Korshunov Mining Plant	4,700	5.0%
Industrial Metallurgical Holding OOO	KMARuda	2,104	2.2%
Ural Mining-Metallurgical Company OAO	Bogoslovskoye RU	1,058	1.1%
Other		1,621	1.7%
Total		94,026	100%

Source: Metal-Expert.

In addition, Sokolovsko-Sarbaykoye Mining Amalgamation, which is located in Kazakhstan and produced 15.49 million tonnes of iron ore concentrate and 6.95 million tonnes of pellets in 2008 (according to Rudprom), has been a major supplier to MMK since April 2006.

***Coal production***

Our active coal mines are primarily located in the Kuznetsky basin, a major Russian coal-producing region, and in the Sakha Republic in eastern Siberia. The earliest production at our Kuznetsky basin mines was in 1953, and 1979 in our Sakha Republic mines.

Our recent license acquisitions include:

in 2004 we acquired through auction a subsoil license for the Sibirginsk mine area of the Sibirginsk and Tomsk coal deposits, near our Sibirginsk Open Pit Mine;

in 2005 we acquired through auction two subsoil licenses for the Rapsadsk open pit mine area of the Rapsadsk coal deposit and the Berezovsk-2 area of the Berezovsk and Olzherassk coal deposits;

in 2005 we acquired through auction two subsoil licenses for the Erunakovsk-1 and Erunakovsk-3 coal mines near Kemerovo; and

in 2005 we acquired the right to explore for and develop coking coal under three subsoil licenses for the Sorokinsk, Razvedochny and Olzherassk coalfields in Kemerovo.

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In October 2007, we acquired 75% less one share of Yakutugol, a coal producer located in eastern Siberia, in the Sakha Republic, increasing our stake to 100%. Yakutugol in turn owns the Kangalassk and Nerungrinsk open pit mines, the Dzhebariki-Khaya underground mine and a coal license for the Seam Piatimetrovy and Promezhutochny area. Yakutugol extracts predominantly coking coal, as well as steam coal. The Nerungrinsk mine produces high-quality coking and steam coal. The Kangalassk mine produces steam coal that is sold as fuel for power plants in the Sakha Republic. The Dzhebariki-Khaya mine produces steam coal, most of which is sold to the state housing and municipal services administration. Yakutugol's output in 2008 was 11.6 million tonnes of coal consisting of 8.1 million tonnes of coking coal and 3.5 million tonnes of steam coal, and it sells most of its output to the Asian Pacific region, primarily Japan, South Korea and Taiwan, primarily pursuant to long-term contracts. We had previously acquired a blocking stake in Yakutugol of 25% plus one share in 2005.

Together with our acquisition of Yakutugol, we also acquired 68.86% of the shares of Elgaugol, which at the time of the acquisition held the license to the undeveloped Elga coal deposit in the Sakha Republic. As part of the auction conditions, we are required to meet certain operational milestones: (1) completing the legal permits for development of the Elga coal deposit by June 2009; (2) commencing construction of the mining plant by November 2009; (3) completing construction of the mining plant (including water supply) and commencing coal production by October 2010; (4) reaching an estimated annual coal production of 9.0 million tonnes by July 2013; and (5) reaching an estimated annual coal production of 18 million tonnes by July 2018. In addition, we undertook the obligation to build a rail branch line of approximately 315 kilometers in length, from the Ulak station on the Baikal-Amur Mainline up to the Elga coal deposit. See Item 5. Operating and Financial Review and Prospects Contractual Obligations and Commercial Commitments. We will operate this rail branch line as a private railway. After our acquisition of Elgaugol, the Elga mining license was transferred to Yakutugol effective upon the end of the first quarter of 2008. The Elga license area is part of a larger coal-bearing geological feature which up to now has been isolated from transportation links. The viability of the Elga project is dependent upon the construction of the rail branch line, as there are presently no transportation links by which to bring coal to market from the Elga license area.

On March 25, 2008, our subsidiary Yakutugol entered into a turn-key contract with Transstroy ZAO Engineering Corporation ( Transstroy ). Under this contract Transstroy undertakes to perform engineering survey works, handle the permitting process and design and build a rail branch line to the Elga coal deposit from the Baikal-Amur Mainline. Yakutugol's obligation is to ensure timely payment, including advances, and build a temporary access road.

The total approximate value of the contract amounts to 33.4 billion rubles. This amount breaks down as follows:

- a fixed price of 2.5 billion rubles for research and design, technical drafting, testing, expert examination, title registration and permitting services;
- a fixed price of 2.2 billion rubles for construction of a temporary access road along the planned rail branch line;
- a fixed price of 1.6 billion rubles for completion of construction of the unfinished initial 60-kilometer section of railway spur track; and
- an estimated price of 27.1 billion rubles, subject to adjustment, for construction of the rail branch line from the 60th to 315th kilometer.

According to the construction schedule, March 26, 2008 was defined as the date of commencement of works. Pursuant to the contract, phase I of the project will be complete by August 1, 2010 and the final phase II will be complete by December 30, 2011.



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The table below sets forth certain information regarding the subsoil licenses used by our coal mines.

<b>Mine<sup>(1)</sup></b>	<b>License Area</b>	<b>License-Holding Subsidiary</b>	<b>License Expiry Date</b>	<b>Status<sup>(2)</sup></b>	<b>Area (sq. km)</b>	<b>Year Production Commenced</b>
Krasnogorsk Open Pit	Tomsk, Sibirginsk	Southern Kuzbass Coal Company OAO	Dec 2013	In production	22.4	1954
Krasnogorsk Open Pit	Sorokinsk, Tomsk, Sibirginsk	Southern Kuzbass Coal Company OAO	Nov 2025	In production	2.8	2007
Lenin Underground	Olzherassk	Southern Kuzbass Coal Company OAO	Nov 2013	In production	10.0	1953
Lenin Underground (Usinsk Underground)	Olzherassk	Southern Kuzbass Coal Company OAO	Dec 2014	In development <sup>(3)</sup>	3.6	1965
Olzherassk Open Pit	Raspadsk, Berezovsk, Olzherassk	Southern Kuzbass Coal Company OAO	Jan 2014	In production	9.3	1980
Olzherassk Open Pit	Raspadsk	Southern Kuzbass Coal Company OAO	Dec 2024	In production	3.5	2007
Olzherassk Open Pit <sup>(4)</sup>	Berezovsk-2, Berezovsk, Olzherassk	Southern Kuzbass Coal Company OAO	Dec 2024	In production	4.8	2007
New-Olzherassk Underground (formerly Invest-Coal)	Raspadsk	Southern Kuzbass Coal Company OAO	Dec 2021	In production	1.2	2006
New-Olzherassk Underground <sup>(4)</sup>	Razvedochny, Raspadsk	Southern Kuzbass Coal Company OAO	Nov 2025	In development	14.6	n/a
Sibirginsk Underground	Sibirginsk, Tomsk	Southern Kuzbass Coal Company OAO	Dec 2024	In production	5.9	2002
Sibirginsk Open Pit	Sibirginsk, Kureinsk, Uregolsk	Southern Kuzbass Coal Company OAO	Jan 2014	In production	15.3	1973
Tomusinsk Open Pit	Tomsk	Tomusinsk Open Pit Mine OAO	Dec 2012	In production	6.7	1959
Erunakovsk-1 Underground	Erunakovsk-1, Erunakovsk	Southern Kuzbass Coal Company OAO	Jun 2025	In development <sup>(3)</sup>	8.4	n/a
Erunakovsk-3 Underground	Erunakovsk-3,	Southern Kuzbass Coal	Jun 2025	In development <sup>(3)</sup>	7.1	n/a

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	Erunakovsk	Company OAO Southern Kuzbass				
Lenin Underground	Olzherassk	Coal	Nov 2025	In development <sup>(3)</sup>	19.2	n/a
Nerungrinsk Open Pit	Nerungrinsk	Company OAO Yakutugol OAO	Dec 2014	In production	15.3	1979
Kangalassk Open Pit	Kangalassk	Kangalassk Open Pit Mine OAO <sup>(5)</sup>	Dec 2014	In production	7.7	1962
Dzhebariki-Khaya Underground	Dzhebariki-Khaya	Dzhebariki-Khaya Mine OAO <sup>(5)</sup>	Dec 2013	In production	14.8	1972
Nerungrinsky Open Pit	Piatimetrovy coal-bed, Promezhutochny	Yakutugol OAO	Dec 2025	In development <sup>(3)</sup>	30.0	n/a
Elga Open Pit	Elga	Yakutugol OAO	May 2020	In development	144.1	n/a

(1) Underground denotes an underground mine; open pit denotes a surface mine.

(2) In production refers to sites that are currently producing coal; in development refers to sites where preliminary work is being carried out in accordance with the terms of the relevant subsoil license, such as preparation and approval of the geological survey project (for the Olzherassk license area), geological surveys (for the Olzherassk, Razvedochny, Erunakovsk-3, Piatimetrovy coal seam and Promezhutochny license areas), preparation and approval of construction project documentation (for the Elga license area) and construction (for the Erunakovsk-1 and Elga license areas).

(3) Not included in our mineral reserves.

(4) Deposits of Olzherassk Open Pit are partially included in our reserves, as SEC standards for reserve estimates allow inclusion in reserves of only the mineral deposits that can be extracted with economic benefits during the license period.

(5) In process of re-registration due to merger of the previous license holder into this company.

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In 1994, Sibirginsk Open Pit Mine (currently a branch of Southern Kuzbass Coal Company) received a coal license to develop the mineral deposits of the Uregolsky 1-2 area. Approximately 1.1 million tonnes of coal have been mined by us since that date at the mine site in the license area.

Due to what we believe was a technical error made when the license was originally issued, there is an uncertainty as to whether the Uregolsk license area includes a part of the mine site with 37 million tonnes of coal deposits (the New Uregolsk license area). Applicable Russian regulations lack a procedure for correcting license boundaries in the event of an error, and as recently as 2006, 2007 and 2008, we carried out mining activities on the New Uregolsk license area in coordination with, and with the knowledge of, Rostekhnadzor. Furthermore, Southern Kuzbass Coal Company in coordination with the Kemerovo regional subsoil use agency participated in an auction aimed at resolving the ownership of the New Uregolsk license area. The auction was concluded on June 26, 2008. Southern Kuzbass Coal Company submitted its bids against competing bidders until it believed that the higher bidder's price was not economically justified in light of the estimated reserves in the license area. The final price was significantly higher than Southern Kuzbass Coal Company's last bid. Meanwhile, in May 2008, the Kemerovo region prosecutor's office opened a criminal case on the basis of Southern Kuzbass Coal Company's alleged unlawful usage of the mineral deposits on the New Uregolsk license area. However, upon the results of the investigation the prosecutor's office issued a decision to dismiss the criminal complaint. For more information see Item 8. Financial Information Litigation - New Uregolsk license area.

We and Southern Kuzbass Coal Company believe that the coal mining at the New Uregolsk license area was in compliance with applicable law. Our subsidiary Southern Kuzbass Coal Company could face civil claims; however, we consider it unlikely that such claims will be made. Our mineral reserves and mineral deposits as set forth in this document as of December 31, 2008 do not include minerals within the New Uregolsk license area.

The coking coal produced by our mines is predominately low-sulfur (0.3%) bituminous. Heating values for the coking coal range from 6,861 to 8,488 kcal/kg on a moisture- and ash-free basis. Heating values for the steam coal range from 6,627 to 8,286 kcal/kg on a moisture- and ash-free basis.

The table below summarizes our coal production by mine and type of coal for the periods indicated.

	2008		2007		2006	
	Tonnes	% of Production	Tonnes	% of Production	Tonnes	% of Production
	(In thousands of tonnes) <sup>(1)</sup>					
<b>Coking Coal</b>						
Sibirginsk (Open Pit and Underground) <sup>(2)</sup>	2,522	16.6%	2,181	20.9%	1,759	18.1%
Tomusinsk Open Pit	1,952	12.9%	2,385	22.9%	2,477	25.6%
Olzherassk Open Pit	614	4.1%	880	8.4%	1,613	16.6%
Lenin Underground <sup>(4)</sup>	1,130	7.5%	2,077	20.0%	1,880	19.4%
Sibirginsk Underground	876	5.8%	1,188	11.4%	1,386	14.3%
Olzherassk Underground					582	6.0%
Yakutugol <sup>(3)</sup>						
Nerungrinsk Open Pit	8,053	53.1%	1,708	16.4%		
Total Coking Coal	15,147	100%	10,419	100%	9,697	100%



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	2008		2007		2006		
	Tonnes	% of Production	Tonnes	% of Production	Tonnes	% of Production	
<b>(In thousands of tonnes)<sup>(1)</sup></b>							
<b>Steam Coal</b>							
Krasnogorsk Open Pit	5,525	49.1%	5,630	52.2%	5,587	76.4%	
Sibirginsk (Open Pit and Underground)	797	7.1%	1,469	13.9%	1,703	23.3%	
Olzherassk Open Pit	525	4.7%	868	8.1%	26	0.3%	
Tomusinsk Open Pit	99	0.9%	36	0.3%			
Olzherassk Underground Yakutugol <sup>(3)</sup>	836	7.4%	1,783	16.5%			
Nerungrinsky Open Pit	2,874	25.5%	827	7.7%			
Kangalassk Open Pit	166	1.5%	35	0.3%			
Dzhebariki-Khaya Underground	423	3.8%	127	1.2%			
<b>Total Steam Coal</b>	<b>11,245</b>	<b>100%</b>	<b>10,775</b>	<b>100%</b>	<b>7,316</b>	<b>100%</b>	
<b>Total Coal</b>	<b>26,392</b>		<b>21,194</b>		<b>17,013</b>		
		<b>% Coking Coal</b>		<b>57.4%</b>		<b>49.2%</b>	<b>57.0%</b>
		<b>% Steam Coal</b>		<b>42.6%</b>		<b>50.8%</b>	<b>43.0%</b>

(1) Volumes are reported on a wet basis.

(2) Underground denotes an underground mine; open pit denotes a surface mine.

(3) Includes only post-acquisition production volumes.

(4) At the Lenin underground mine production was suspended because of accidents: on May 30, 2008 there was a cave-in (suspension of operations 17 calendar days) and on July 29, 2008 there was a methane flash (suspension of operations 67 calendar days), both with multiple casualties.

*Coal washing plants*

We operate five coal washing plants located near our coal mines in the Southern Kuzbass. Of the total coal feedstock enriched by our washing plants in 2008, approximately 98.4% (11.9 million tonnes) was supplied by our own mining operations, and 1.6% (0.2 million tonnes) from the nearby Rospadskaya underground mine (owned by Rospadskaya OAO) on a tolling basis. In 2008, the capacity of our washing plants in Russia accounted for 20.1% of the total domestic coking coal washing capacity in Russia by volume, according to the Central Dispatching Department.

*Investments in coal companies*

We own 16.1% of Mezhdurechye OAO, a Russian coal producer whose production volume accounted for 5% of Russian coking coal output and 2% of Russian total coal output in 2008, according to the Central Dispatching Department.

*Acquisition of BCG companies*

In May 2009, our subsidiaries closed a transaction to acquire the BCG companies, U.S. privately-owned companies based in West Virginia, from their owner the Justice family. According to our reserves estimates, the BCG companies coal holdings in West Virginia as of October 24, 2008 include 91.9 million tonnes of proven reserves plus 74.1 million tonnes of probable reserves in accordance with SEC Industry Guide 7. The BCG companies have four mining complexes, together comprising six open pit and four underground mines. In 2008, the BCG companies produced 2.5 million tonnes of coal.

**Table of Contents*****Iron ore and concentrate production***

Korshunov Mining Plant operates three iron ore mines, Korshunovsk, Rudnogorsk and Tatianinsk, as well as a concentrating plant located outside of the town of Zheleznogorsk-Ilimsky, 120 kilometers east of the city of Bratsk in eastern Siberia. The Korshunovsk mine is located near the concentrating plant. The Rudnogorsk mine is located about 85 kilometers to the northwest of the concentrating plant. The Tatianinsk mine is located about 10 kilometers to the north of the concentrating plant. All three mines produce a magnetite ore (Fe<sub>3</sub>O<sub>4</sub>). We acquired Korshunov Mining Plant in 2003.

The table below sets forth the subsoil licenses used by our iron ore mines and the expiration dates thereof.

License Area	License Holder	License		Area (sq. km)	Year
		Expiry Date	Status		Production Commenced
Korshunovsk	Korshunov Mining Plant	June 2014	In production	4.3	1965
Tatianinsk	Krasta ZAO <sup>(1)</sup>	June 2012	In production	1.3	1982
Rudnogorsk	Korshunov Mining Plant	June 2014	In production	5.1	1986
Krasnoyarsk	Korshunov Mining Plant	July 2015	Feasibility study <sup>(2)</sup>	3.0	n/a

(1) In February 2007, Korshunov Mining Plant transferred the Tatianinsk license to its wholly owned subsidiary Krasta ZAO.

(2) Not included in our mineral reserves and deposits.

The table below summarizes our iron ore and iron ore concentrate production for the periods indicated.

	2008		2007		2006	
	Tonnes	Grade (% Fe)	Tonnes	Grade (% Fe)	Tonnes	Grade (% Fe)
	(In thousands of tonnes) <sup>(1)</sup>					
Korshunovsk ore production	5,702	26.3%	6,573	25.8%	6,193	26.2%
Rudnogorsk ore production	5,911	34.6%	5,754	35.6%	5,224	37.1%
Tatianinsk ore production	110	29.2%	468	29.9%	222	32.4%
Total ore production	11,724	30.5%	12,795	30.4%	11,639	31.2%
Iron ore concentrate production	4,700	62.2%	4,963	62.2%	4,976	62.6%

(1) Volumes are reported on a wet basis.

***Limestone production***

The Pugachev limestone quarry is an open pit mine located approximately nine kilometers southwest of the city of Beloretsk in the Ural Mountains. The quarry was developed in 1952 to support Beloretsk Metallurgical Plant's steel-making facilities, which are currently closed. The Pugachev limestone quarry is owned by our Beloretsk Metallurgical Plant, which we acquired in 2002. The current subsoil license is valid until January 2014.

The quarry produces both high-grade flux limestone for use in steel-making and nickel smelting and aggregate limestone for use in road construction. The flux limestone and aggregate limestone are the same grade of limestone, but they are produced in different fraction sizes, which determine their suitability for a particular use. In 2008, approximately 87.6% of the limestone produced at Pugachev was used internally, with 64.3% shipped to Chelyabinsk Metallurgical Plant, 19.7% shipped to Southern Urals Nickel Plant, 3.6% to Izhstal, 9.7% used as auxiliary and the remaining 2.7% sold to third parties. We are capable of internally sourcing 100% of the limestone requirements of our steel operations.

The table below summarizes our limestone production for the periods indicated.

	<b>2008</b>	<b>2007</b>	<b>2006</b>
	<b>(In thousands of tonnes)</b>		
Limestone production	1,692	1,832	2,014

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The decrease of limestone production volumes during from 2006 through 2008 period relates to the improvement in quality of limestone fractions produced and a corresponding decrease in our requirements for 40-80 millimeter and 20-40 millimeter limestone fractions. Producing extra tonnage is not economically justifiable, as it results in increased unutilized inventory. In 2008 the limestone quarry worked on more deep reprocessing of 0-20 millimeter limestone fractions extracted in prior periods and converting them to the 0-5 millimeter fraction, which is needed for our iron smelting plants. Correspondingly, processed limestone production (including reprocessing of already-mined inventory) increased, but extraction of limestone was performed based on our internal needs.

***Mineral reserves (coal, iron ore and limestone)***

Our mineral reserves are based on exploration drilling and geological data, and are that part of a mineral deposit which could be economically and legally extracted or produced at the time of the reserve determination. Each year we update our reserve calculations based on actual production and other factors, including economic viability and any new exploration data. Our reserves, consisting of proven and probable reserves, meet the requirements set by the SEC in its Industry Guide 7. Information on our mineral reserves has been prepared by our internal mining engineers as of December 31, 2008. To prepare this information our internal mining engineers used resource and reserve estimates, actual and forecast production, operating costs, capital costs, geological plan maps, geological cross sections, mine advance maps in plan and cross section and price projections.

Proven reserves presented in accordance with Industry Guide 7 may be combined with probable reserves only if the difference in the degree of assurance between the two classes of reserves cannot be readily defined and a statement is made to that effect. For our Russian properties our proven and probable reserves are presented as combined in this document because, though our deposits have been drilled to a high degree of assurance, due to the methodology used in Russia to estimate reserves the degree of assurance between the two categories cannot be readily defined. We report information on our mineralized material on an annual basis to the Russian State Committee on Reserves ( GKZ ) according to the approved Russian classifications of A, B and C1. In general, provided that Industry Guide 7's economic criteria are met, A+B is equivalent to proven and C1 is equivalent to probable. However, when preparing year-by-year production schedules, due to our practice of preparing our Russian mineralization reports manually and the lack of computerized data and modeling, we do not break out future production by these categories when scheduling and we are not required to do so by the GKZ. These categories are defined for the mine plan as a whole. As these annual production schedules are the basis for estimating our reserves under Industry Guide 7, we are not able to segregate our Industry Guide 7 reserves into proven and probable categories. Although we are in the process of digitizing our data and implementing the use of computerized models and hope to be able to prepare production schedules by category in the future (and hence segregate our Industry Guide 7 reserves by proven and probable categories), currently it would not be commercially feasible for us to do so.

Russian subsoil licenses are issued for defined boundaries and specific periods, generally about 20 years. Our declared reserves are contained within the current license boundary. Additionally, to meet the legally viable requirement of the SEC, only material that is scheduled to be mined during the license period of existing subsoil licenses based on planned production was included in reserves.

Our subsoil licenses expire on dates falling in 2009 through 2033. Our most significant licenses expire between 2012 and 2024. These subsoil licenses, however, may be terminated prior to, or may not be extended at, the time of their expiration. However, we believe that they may be extended at our initiative without substantial cost. We intend to extend such licenses for deposits expected to remain productive subsequent to their license expiry dates. See Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry. Our business could be adversely affected if we fail to obtain or renew necessary licenses and permits or fail to comply with the terms of our licenses and permits, Item 3. Key Information Risk Factors Risks Relating to the Russian Federation and Other Countries Where We Operate Legal risks and uncertainties Deficiencies in the legal framework relating to subsoil licensing subject

our licenses to the risk of governmental challenges and, if our licenses are suspended or terminated, we may be unable to realize our reserves, which could materially adversely affect our business and results of operations and Regulatory Matters Russian Regulation Subsoil licensing.

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In addition to our mineral reserves, we have mineral deposits. Our mineral deposits are similar to our mineral reserves in all respects, except that the deposit is either (1) contained within the license boundary but is scheduled to be extracted beyond the license period or (2) is adjacent to but not contained within the license boundary. In both such cases, we intend to obtain the legal right to extract such deposit in the future. Mineral deposits may not ever be converted into mineral reserves if licenses are not renewed and/or extraction of such mineral deposits does not become economically viable in the future. See Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry Our business could be adversely affected if we fail to obtain or renew necessary licenses and permits or fail to comply with the terms of our licenses and permits and Item 3. Key Information Risk Factors Risks Relating to the Russian Federation and Other Countries Where We Operate Legal risks and uncertainties Weaknesses relating to the Russian legal system and legislation create an uncertain investment climate.

The table below summarizes our reserves (including the reserves associated with our ferroalloys segment) as of December 31, 2008.

Summary	Coal <sup>(1)</sup>					
	Coking	Steam	Iron Ore	Nickel Ore <sup>(2)</sup>	Chrome Ore <sup>(2)</sup>	Limestone
	(Quantities in millions of tonnes)					
Reserves	208.1	271.2	40.7	9.6	18.7	16.4
Grade (%)	43.4% <sup>(3)</sup>	56.6% <sup>(3)</sup>	32.6%	1.0%	42.2%	55.2%
Deposits	290.6	460.0	109.4	69.7		10.1
Grade (%)	38.7% <sup>(3)</sup>	61.3% <sup>(3)</sup>	30.1%	0.9%		55.2%

(1) Does not include the BCG companies 91.9 million tonnes of proven reserves and 74.1 million tonnes of probable reserves estimated as of October 24, 2008.

(2) See Ferroalloys Business Mineral reserves (ferroalloys) for detail on the mineral reserves and deposits of our ferroalloys segment.

(3) Shows percentage of the type of coal.

All of the Southern Kuzbass Coal Company mines are located in the southeast portion of the Kuznetsky Basin in Kemerovo region, Russia. Southern Kuzbass Coal Company operations are located around the city of Mezhdurechensk with the exception of Erunakovsk, which is located northeast of Novokuznetsk. Each of the Southern Kuzbass Coal Company mines, with the exception of Erunakovsk, have railway spurs connected to the Russian rail system, which is controlled by Russian Railways.

*Coal*

As of December 31, 2008, we had coal reserves (proven and probable) totaling 479.3 million tonnes, of which approximately 43.4% was coking coal. The table below summarizes coal reserves by mine.

Coal Reserves <sup>(1)(2)</sup>	Coking Coal <sup>(3)</sup>	Steam Coal <sup>(3)</sup>	Heating Value <sup>(4)(5)</sup>	% Sulfur <sup>(5)</sup>

**(Quantities in millions of tonnes)<sup>(6)(7)(8)</sup>**

Krasnogorsk Open Pit		101.7	5,700	0.40%
Tomusinsk Open Pit	10.3	1.0	8,350	0.30%
Olzherassk Open Pit	3.2	31.7	8,171	0.25%
Olzherassk Underground		16.2	7,900	0.30%
Sibirginsk Open Pit	17.5	11.3	8,449	0.30%
Sibirginsk Underground	41.1		8,531	0.25%
Lenin Underground	12.2		8,467	0.29%
Nerungrinsk Open Pit	62.7	5.6	7,331	0.30%
Elga <sup>(9)</sup>	61.1	103.7	n/a	n/a
Total	208.1	271.2		
% of Total	43.4%	56.6%		

(1) Reserve estimates use the tonnages that are expected to be mined, taking into account dilution and losses.

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- (2) Does not include the BCG companies 91.9 million tonnes of proven reserves and 74.1 million tonnes of probable reserves estimated as of October 24, 2008.
- (3) We own 93.5% of Southern Kuzbass Coal Company mines, 74.4% of Tomusinsk Open Pit Mine, 100% of Yakutugol mine and 71.2% of Elga mine. Reserves and deposits are presented for the mines on an assumed 100% ownership basis.
- (4) Heating values (in kcal/kg) are reported on a moisture- and ash-free basis.
- (5) The figures represent the average for the relevant licensed period.
- (6) Volumes are reported on a wet in-place basis.
- (7) The coal recovery factors for raw coal sent to Siberian Central Processing Plant, Kuzbass Central Processing Plant, Tomusinsk Processing Mills, Krasnogorsk Processing Plant and Nerungrinsk Processing Plant are projected to be 81.5%, 81%, 67%, 60-66% and 67%, respectively.
- (8) In estimating our reserves we use average market or contract prices and currency conversions are carried out at average official exchange rates of the Central Bank of Russia.
- (9) Tonnages are for clean coal product. All other mines are reported on a run-of-mine basis.

As of December 31, 2008, we had coal deposits totaling 750.6 million tonnes, of which approximately 38.7% was coking coal. The table below summarizes coal deposits by mine.

Coal Deposits	Coking Coal	Steam Coal	Heating	%
			Value <sup>(1)(2)</sup>	Sulfur <sup>(2)</sup>
(Quantities in millions of tonnes) <sup>(3)</sup>				
Krasnogorsk Open Pit		103.9	5,771	0.40%
Tomusinsk Open Pit	7.0	1.9	8,350	0.30%
Olzherassk Open Pit	9.9	8.7	8,265	0.25%
Sibirginsk Open Pit	20.4	18.5	8,466	0.30%
Sibirginsk Underground	6.0		8,531	0.25%
Lenin Underground	14.7		8,476	0.31%
Nerungrinsk Open Pit	86.3	5.6	7,670	0.30%
Elga <sup>(4)</sup>	146.3	282.9	n/a	n/a
Erunakovsk		38.5	8,265	0.25%
Total	290.6	460.0		
% of Total	38.7%	61.3%		

(1) Heating values (in kcal/kg) are reported on a moisture- and ash-free basis.

- (2) The figures represent the average for the relevant unlicensed period.
- (3) Volumes are reported on a wet in-place basis.
- (4) Tonnages are for clean coal product. All other mines are reported on a run-of-mine basis.

n/a Not currently available.

All of the Southern Kuzbass Coal Company mines are located in the southeast portion of the Kuznetsky Basin in Kemerovo region, Russia. Southern Kuzbass Coal Company operations are located around the city of Mezhdurechensk with the exception of Erunakovsk, which is located northeast of Novokuznetsk. Each of the Southern Kuzbass Coal Company mines, with the exception of Erunakovsk, have railway spurs connected to the Russian rail system, which is controlled by Russian Railways.

Nerungrinsk Open Pit is located in the southern part of the Sakha Republic in eastern Siberia, south of the capital of Yakutsk near the town of Nerungri. Nerungrinsk Open Pit has a railway spur connected to the Russian rail system, which is controlled by Russian Railways.

The Elga project is located in the Sakha Republic and lies in the South Yakutsk Basin of the Toko Coal-Bearing Region. This region was first discovered and explored in 1952 with the first geological surveys being conducted in

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1954 through 1956 followed by prospecting surveys in 1961 through 1962. Trenching along the outcrops was conducted in 1980 through 1982 followed by exploration drilling that was completed in 1998.

Our Kangalassk Open Pit and Dzhebariki-Khaya Underground mining properties contain neither mineral reserves nor mineral deposits, as we have defined mineral deposits (see Mineral reserves (coal, iron ore and limestone) above). Though these are operating mines and the geological sampling and density requirements have been met, they fail to meet the economic criteria. Our Southern Kuzbass Coal Company subsidiary also has a number of coal mining licenses with which no mineral reserves or deposits are associated.

Elga, a coalfield for which our subsidiary Yakutugol holds a subsoil license, is now an undeveloped property in a remote area of Siberia. Elga is capable of producing large quantities of export-quality coking and steam coal. The region was first discovered and explored in 1952, with the first geological surveys being conducted in 1954 through 1956, followed by prospecting surveys in 1961-1962. Exploration drilling was completed in 1998, and since then there have been several studies on Elga, including geology and resources, mine planning, railway construction and feasibility studies. We plan to mine Elga using open pit mining methods.

There are a number of significant risk factors associated with the Elga project. These risks have the potential to impact the calculation of the Elga reserves by affecting the project's legal or economic viability. Key risks that have been identified include the following:

According to the terms of the subsoil license for the Elga coal deposit, we must construct a rail branch line from the Baikal-Amur Mainline to the coal deposits, approximately 315 kilometers in length, and this branch line must be operational by September 30, 2010. Previous detailed studies have estimated that it will take three to four years to construct such a branch line. The current construction schedule is very aggressive and may not be achievable. If this schedule is not met, the potential exists that our subsoil license for Elga will be suspended or terminated. Though to-date the pace of construction has mostly corresponded to the schedule agreed with the general contractor, there are no assurances that the construction schedule will be met. The deviations from schedule that have occurred to-date have been caused by the need to realize technical and engineering solutions on-site in order to achieve less expensive project completion and optimize construction costs.

The viability of the Elga project is dependent upon the construction of the rail branch line referred to above. Construction of the branch line has begun but a detailed engineering study needs to be conducted to determine construction volumes for earthworks and the total construction costs.

A detailed feasibility study was completed on the Elga project in 2005. A new engineering study needs to be completed on the project to determine project capital and operating costs due to the significant cost inflation that has occurred in the mining industry since 2005. Increases in capital and operating costs have the potential to make the Elga project uneconomical because of the project's sensitivity to these costs.

The Elga project is very sensitive to market prices for coal because of the high initial capital costs and expected high ongoing operating costs. Coal prices will need to be near or above historically high price levels for several years in order for this project to have a positive net present value at a 12% discount rate, which was used for the reserves calculation.

*Iron ore*

As of December 31, 2008, we had iron ore reserves (proven and probable) totaling 40.7 million tonnes at an average iron grade of 32.6%. The table below summarizes iron ore reserves by mine.

<b>Iron Ore Reserves<sup>(1)(2)</sup></b>	<b>Tonnes<sup>(3)(4)</sup></b>	<b>Grade (% Fe)<sup>(5)</sup></b>
	<b>(In millions of tonnes)</b>	
Korshunovsk	4.0	26.2%
Rudnogorsk	33.1	34.2%
Tatianinsk	3.6	25.0%
Total	40.7	32.6%

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- (1) Reserve estimates use the tonnages that are expected to be mined, taking into account dilution and losses.
- (2) In estimating our reserves we use average market or contract prices and currency conversions are carried out at average official exchange rates of the Central Bank of Russia.
- (3) Volumes are reported on a wet basis.
- (4) We own 85.6% of Korshunov Mining Plant mines. Reserves are presented for the mines on an assumed 100% ownership basis.
- (5) Metallurgical recovery is projected to be 70.2%.

As of December 31, 2008, we had iron ore deposits totaling 109.4 million tonnes at an average iron grade of 30.1%. The table below summarizes iron ore deposits by mine.

<b>Iron Ore Deposits<sup>(1)</sup></b>	<b>Tonnes<sup>(2)</sup></b>	<b>Grade (% Fe)<sup>(3)</sup></b>
	<b>(In millions of tonnes)</b>	
Korshunovsk	47.4	26.2%
Rudnogorsk	62.0	34.2%
Total	109.4	30.1%

- (1) Includes adjustments for dilution and mine recovery, based on historical records.
- (2) Volumes are reported on a wet basis.
- (3) Metallurgical recovery is projected to be 70.2%.

All of the iron ore mines and licenses are located in the Irkutsk region. The Korshunovsk and Tatianinsk operations are located near the town of Zheleznogorsk-Ilimsky. The Rudnogorsk Mine is located approximately 85 kilometers to the northwest of Zheleznogorsk-Ilimsky. There is an airport in Bratsk, which has regular flights to Moscow. Transportation to Zheleznogorsk-Ilimsky and the surrounding mines from Bratsk is available by railway and highway.

*Limestone*

As of December 31, 2008, we had limestone reserves (proven and probable) totaling 16.4 million tonnes at 55.2% calcium oxide.

<b>Limestone Reserves<sup>(1)(2)</sup></b>	<b>Tonnes</b>	<b>Grade (% CaO)</b>
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	<b>(In millions of tonnes)</b>	
Pugachev	16.4	55.2%

(1) Reserve estimates use the tonnages that are expected to be mined, taking into account dilution and losses.

(2) We own 90.4% of Beloretsk Metallurgical Plant mines. Reserves are presented for the mines on an assumed 100% ownership basis.

As of December 31, 2008, we had limestone deposits totaling 10.1 million tonnes at 55.2% calcium oxide.

<b>Limestone Deposits<sup>(1)</sup></b>	<b>Tonnes</b>	<b>Grade (% CaO)</b>
	<b>(In millions of tonnes)</b>	
Pugachev	10.1	55.2%

(1) Includes adjustments for dilution and mine recovery, based on historical records.

The Pugachev mine is located approximately nine kilometers southwest of the city of Beloretsk and three kilometers southwest of the village of Lomovka in the White River watershed. The Pugachev mine has a railway spur connected to the Russian rail system, which is controlled by Russian Railways.

**Table of Contents****Steel Business**

Our steel business comprises production and sale of semi-finished steel products, carbon steel long products and specialty steel long products, carbon and stainless flat products, and value-added downstream metal products including hardware, stampings and forgings. Within these product groups, we are further able to tailor steel grades to meet specific end-user requirements. Our steel business is supported by our mining business, which includes coal (steam and coking coal), iron ore and limestone, and our ferroalloys business, which includes nickel, ferrochrome and ferrosilicon.

Our steel business has production facilities in Russia, Lithuania and Romania. Our acquisition of Ductil Steel in early 2008 represents further expansion of our production and marketing capacity into the E.U. The acquisition of Ductil Steel is allowing us to optimize our existing production chain and maximize the efficiency of our intra-group sales structure, while at the same time reducing costs including import duties and logistics expenses associated with bringing billets to our Romanian plants from our Russian steel mills in our growing Romanian steel business.

***Steel manufacturing process and types of steel***

The most common steel manufacturing processes are production in a basic oxygen furnace, or BOF, and production in an electric arc furnace, or EAF.

In blast furnace steel manufacturing, the principal raw materials used to produce pig iron are iron ore products, and the metal is chemically smelted from the ore. Mined iron ore is crushed, concentrated and mixed with limestone and a small amount of coke. The mixture is sintered, crushed and then constantly fed, in alternating layers with more coke, into a blast furnace. At the same time natural gas and oxygen are injected into the furnace to reduce the iron, melt the mixture and obtain pig iron, an intermediate product with an iron content of 94-97%, a carbon content of 2-4% and 1-2% non-ferrous elements. Liquid pig iron is processed further in a BOF to produce molten steel with less than 2% carbon content. The molten steel, depending on the products in which it will be used, undergoes additional refining and is mixed with manganese, nickel, chrome, and titanium ferroalloys and other components to give it special properties. Approximately 60% of the world's steel output is made in a BOF, most typically in large-scale plants that must produce 3-4 million tonnes per year to be economically efficient.

In EAF steel manufacturing, steel is generally produced from remelted scrap. Heat to melt the scrap is supplied from high-voltage electricity that arcs within the furnace between graphite electrodes and the scrap. This process is suitable for producing almost all steel alloys, including stainless steel; however, it is limited in its use for production of high-purity carbon steel. Approximately 35% of world steel output is made in EAFs.

Steel products are broadly subdivided into two categories flat and long products. Flat products are hot-rolled or cold-rolled coils and/or coated sheets that are used primarily in manufacturing industries, such as the white goods and automotive industries. Long products are used for construction-type applications (beams, rebar) and the engineering industry. To create flat and long products, molten raw steel is cast in continuous-casting machines or casting forms (molds). The molten steel is processed and hardened into semi-finished products in the form of blooms, slabs or ingots. Ingots and blooms have a square cross-section and are used for further processing into long products. Slabs have a rectangular cross-section and are used to make flat products. All products are rolled at high temperatures, a process known as hot rolling. They are drawn and flattened through rollers to give the metal the desired dimensions and strength properties. Some flat steel products go through an additional step of rolling without heating, a process known as cold rolling. After cold rolling, annealing in furnaces with gradual cooling that softens and stress-relieves the metal is periodically required. Oil may be applied to the surfaces for protection from rust.

The properties of steel (strength, solidity, plasticity, magnetization, corrosion-resistance) may be modified to render it suitable for its intended future use by the addition by smelting of small amounts of other metals into the structure of the steel, varying the steel's chemical composition. For example, the carbon content of steel can be varied in order to change its plasticity, or chrome and nickel can be added to produce stainless steel. Resistance to corrosion can be achieved through application of special coatings (including polymeric coatings), galvanization, copper coating or tinning, painting and other treatments.

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### ***Description of key products***

*Coke.* Coke is used in the blast furnace as a main source of heat, a reducing agent for iron and a raising agent for charging material in the smelting process. It is a product prepared by pyrolysis (heating in the absence of oxygen) of low-ash, low-phosphorus and low-sulfur coal charging material. We offer customers coke from our Moscow Coke and Gas Plant and Mechel-Coke.

*Coking products.* Coking products are hydrocarbon products obtained as a byproduct of the production of coke. We produce coke in our subsidiaries Moscow Coke and Gas Plant and Mechel-Coke. We offer our customers coal tar, naphthalene and other compounds. Worldwide, coal tar is used in diverse applications, including boiler fuel, food additives and pavement sealants. Naphthalene, a product of the distillation of coal tar, is best known as the active ingredient in mothballs. It is used by the chemical industry to produce chemical compounds used in synthetic dyes, solvents, plasticizers and other products.

*Pig iron.* Pig iron is a high-carbon form of iron produced from smelting iron ore feed (sinter, pellets and other ore materials) in the blast furnace. Cold pig iron is brittle. Liquid pig iron is used as an intermediate product in the manufacturing of steel. Cold pig iron can be used as charging material for steel manufacturing in electric arc furnaces and in manufacturing of cast iron in cupolas. We sell small volumes of pig iron from our Chelyabinsk Metallurgical Plant to third parties.

*Semi-finished products.* Semi-finished products typically require further milling before they are useful to end consumers. We offer semi-finished billets, blooms and slabs. Billets and blooms are precursors to long products and have a square cross section. The difference between billets and blooms is that blooms have a larger cross-section. Slabs are precursors to flat products and have a rectangular cross section. Such types of products can be produced both by continuous casting of liquid steel and by casting of liquid steel in casting forms with subsequent blooming on a continuous rolling mill. We offer our customers billets and blooms produced by Mechel Targoviste, Izhstal, Chelyabinsk Metallurgical Plant and Ductil Steel, as well as slabs produced by Chelyabinsk Metallurgical Plant.

*Long steel products.* Long steel products are rolled products used in many industrial sectors, particularly in the construction and engineering industries. They include various types of products, for example, rebar, calibrated long steel products and wire rod, which could be supplied both in bars and coils with wide range of sizes. Our long products are manufactured at Chelyabinsk Metallurgical Plant, Izhstal and Beloretsk Metallurgical Plant in Russia, and Mechel Campia Turzii, Mechel Targoviste and Ductil Steel in Romania.

We offer our customers a wide selection of long steel products produced from various kinds of steel, including rebar, calibrated long steel products, steel angles, round products, surface-conditioned steel products, wire rod and others.

*Flat steel products.* Flat steel products are manufactured by multiple drafting slabs in forming rolls with subsequent coiling or cutting into sheets. Plates are shipped after hot rolling or heat treatment. Coiled stock can be subject to cutting lengthwise into slit coils or crosswise into sheets. Stainless steel is used to manufacture plates and cold rolled sheets in coils and flat sheets. Hot rolled plates and carbon and alloyed coiled rolled products are manufactured at Chelyabinsk Metallurgical Plant.

*Stampings and forgings.* Stampings are custom parts stamped from flat products. Forgings are specialty products made through the application of localized compressive forces to metal. Forged metal is stronger than cast or machined metal. Our forgings and stampings are offered on a made-to-order basis according to minimum batches depending on the products sizes. Our product offerings include rollers and axles used in vehicle manufacturing; bearings, gears and wheels; bars and others. Our stampings and forgings are produced at Urals Stampings Plant, including its Chelyabinsk branch. Izhstal and Mechel Targoviste also produce stampings and forgings.

*Hardware.* Hardware are products resulting from re-processing of wire rod and which are ready for use in manufacturing and consumer applications. Our hardware is produced at Izhstal, Beloretsk Metallurgical Plant and Vyartsilya Metal Products Plant in Russia, Mechel Campia Turzii in Romania and Mechel Nemunas Co. Ltd. ( Mechel Nemunas ) in Lithuania. Our wide-ranging hardware product line includes spring wire; barbed wire; electrodes; wire for ball bearing manufacturing; precision alloy wire; rebar wire; metal cord; zinc-coated wire; copper-coated wire; various types of nails; cables specially engineered for the shipping, aerospace, oil and gas and construction industries; aerials for electric trams and buses; cables for passenger and freight elevators; general-purpose iron and steel straps and clips; woven wire cloth; and others.

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The following table sets out our production volumes by primary steel product categories and main products within these categories.

	<b>2008</b>	<b>2007</b>	<b>2006</b>
	<b>(In thousands of tonnes)</b>		
Coke	3,326	3,886	2,570
Coking Products	129	129	49
Pig Iron	3,500	3,686	3,631
Semi-Finished Steel Products, including:	1,753	1,705	1,785
Carbon and Low-Alloyed Semi-Finished Products	1,710	1,647	1,716
Long Steel Products, including:	2,772	3,040	2,529
Stainless Long Products	15	17	15
Alloyed Long Products	36	82	79
Rebar	1,535	1,637	1,358
Wire Rod	580	591	367
Low-Alloyed Engineering Steel	606	711	712
Flat Steel Products, including:	357	393	400
Stainless Flat Products	37	37	39
Carbon and Low-Alloyed Flat Products	320	356	361
Forgings, including:	72	80	75
Stainless Forgings	1	2	3
Alloyed Forgings	29	51	24
Carbon and Low-Alloyed Forgings	41	26	48
Forged Alloys	0	1	1
Stampings	86	95	101
Hardware, including:	719	689	611
Wire	556	536	466
Ropes	52	57	55

With the exception of our non-Russian subsidiaries, we manufacture almost all of our steel products using internally sourced coke, pig iron, raw steel and semi-finished steel products.

**Table of Contents*****Sales of steel products***

The following table sets forth our revenues by primary steel segment product categories and our main products within these categories (including as a percentage of total steel segment revenues) for the periods indicated. Steel segment sales data presented in Steel Business do not include intercompany sales.

Revenues	2008		2007		2006	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
	(In millions of U.S. dollars, except for percentages)					
Coke	377.5	7%	248.8	6%	38.7	1%
Coking Products	35.3	1%	36.0	1%	10.3	0%
Pig Iron	19.1	0%	4.1	0%	14.1	0%
Semi-Finished Products, including:	475.7	9%	555.1	13%	397.5	13%
Carbon and Low-Alloyed						
Semi-Finished Products <sup>(1)</sup>	425.1	8%	446.5	10%	299.3	10%
Long Steel Products, including:	2,682.4	49%	1,830.1	42%	1,436.3	47%
Stainless Long Products	53.0	1%	44.8	1%	35.2	1%
Alloyed Long Products	158.0	3%	151.9	4%	131.1	4%
Rebar	1,632.8	30%	1,017.1	24%	753.0	25%
Wire Rod	240.3	4%	190.1	4%	202.3	7%
Carbon and Low-Alloyed						
Engineering Steel	598.3	11%	426.3	10%	314.7	10%
Flat Steel Products, including:	475.6	9%	421.8	10%	304.2	10%
Stainless Flat Products	184.6	3%	193.5	4%	125.2	4%
Carbon and Low-Alloyed Flat						
Products	291.0	5%	228.3	5%	178.9	6%
Forgings, including:	180.9	3%	164.7	4%	81.2	3%
Stainless Forgings	24.5	0%	26.5	1%	9.8	0%
Alloyed Forgings	20.8	0%	20.8	0%	11.9	0%
Carbon and Low-Alloyed Forgings	107.2	2%	86.9	2%	49.1	2%
Forged Alloys	28.3	1%	30.5	1%	10.3	0%
Stampings	236.1	4%	201.4	5%	151.7	5%
Hardware, including:	891.5	16%	603.4	14%	458.0	15%
Wire	640.2	12%	414.5	10%	303.3	10%
Ropes	84.4	2%	73.2	2%	60.6	2%
Other	121.1	2%	241.4	6%	150.8	5%
Total	5,495.1	100%	4,306.9	100%	3,042.8	100%

(1) Excludes revenues from slab sales.

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The following table sets forth by percentage of sales the regions in which our steel segment products were sold for the periods indicated.

<b>Region<sup>(1)</sup></b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
Russia	59.0%	59.2%	58.9%
Other CIS	5.7%	5.9%	5.6%
Europe	24.7%	19.5%	26.6%
Asia	2.2%	1.0%	1.3%
Middle East	5.5%	13.1%	5.6%
United States	0.8%	0.6%	1.7%
Other	2.0%	0.6%	0.3%
Total	100%	100%	100%

(1) The regional breakdown of sales is based on the geographic location of our customers, and not on the location of the end users of our products, as our customers are often distributors that resell and, in some cases, further export our products.

In 2008, our steel segment sales outside of Russia were principally to Europe, CIS and the Middle East. Sales in Europe accounted for 25% of our total steel segment sales. CIS and Middle East sales in 2008 accounted for 6% of our total steel segment sales each.

In 2008, the five largest customers of our steel segment products were Severstal OAO (coke), Balli Klockner Public Limited Company (carbon and low-alloyed semi-finished products, carbon and low-alloyed flat steel, rebar and other steel products), Kosogorskiy Metallurgical Plant OAO (coke), Chelyabinsk Tube Rolling Plant OAO (carbon and low-alloyed forgings, low alloyed engineering long steel, carbon and low-alloyed flat steel and other steel products) and Benico Development S.A. (carbon and low-alloyed semi-finished products and other semi-finished products), which together accounted for 7% of our steel segment sales.

Almost all of our steel segment export sales are made to independent distributors pursuant to framework contracts. These framework contracts generally specify certain ports to which we must deliver our products. The distributors take delivery of our products at these locations, and further on-sell the products to other distributors or end users. When these distributors take delivery of our products, we are provided in certain instances with documentation showing the further destination of our products. We do not have control over the final destination of our products, contractually or otherwise.

Based on such documentation, we are aware that certain of our products are sold to certain countries that are subject to international trade restrictions or economic embargoes that prohibit U.S. incorporated entities, U.S. citizens and residents from engaging in commercial, financial or trade transactions with such countries, including countries such as Iran and Syria (the Sanctioned Countries). We estimate that approximately 2.2% of our total sales in 2008 were sold in the Sanctioned Countries, mostly by independent distributors to other distributors or end-users. Such sales accounted for 6.7% of our total sales in 2007, since we regularly limit sales to the Sanctioned Countries.

In addition, we have a very limited amount of direct sales to customers in the Sanctioned Countries, amounting to approximately 0.4% of our total sales in 2008. We intend to cease these sales in the future

We are aware of governmental initiatives in the United States and elsewhere to adopt laws, regulations or policies prohibiting transactions with or investment in, or requiring divestment from, entities doing business with the Sanctioned Countries. While we are not a U.S. person that would be subject to such regulations, we recognize that dealings with the Sanctioned Countries can have an adverse effect on our international reputation. Accordingly, we intend to work with independent distributors to include provisions in our future framework contracts that would allow us to consent to, or be consulted in advance in relation to, on-sales of our products to the Sanctioned Countries.

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The following table sets forth information on our domestic and export sales of our primary steel product categories for the periods indicated. We define exports as sales by our Russian and foreign subsidiaries to customers located outside their respective countries. We define domestic sales as sales by our Russian and foreign subsidiaries to customers located within their respective countries. See note 25 to our consolidated financial statements in Item 18. Financial Statements.

<b>Products</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
	<b>(In millions of U.S. dollars, except for percentages)</b>		
Coke	377.5	248.8	38.7
Domestic (%)	77.6%	78.0%	95.0%
Export (%)	22.4%	22.0%	5.0%
Coking Products	35.3	36.0	10.3
Domestic (%)	52.6%	64.2%	99.0%
Export (%)	47.4%	35.8%	1.0%
Pig Iron	19.1	4.1	14.1
Domestic (%)	100.0%	93.3%	100.0%
Export (%)	0.0%	6.7%	0.0%
Semi-Finished Steel Products	477.5	555.1	397.5
Domestic (%)	18.7%	12.6%	11.0%
Export (%)	81.3%	87.4%	89.0%
Long Steel Products	2,682.4	1,830.1	1,436.3
Domestic (%)	81.8%	75.4%	76.0%
Export (%)	18.2%	24.6%	24.0%
Flat Steel Products	475.6	421.8	304.2
Domestic (%)	79.7%	79.0%	79.0%
Export (%)	20.3%	21.0%	21.0%
Forgings	180.9	164.7	81.2
Domestic (%)	53.8%	61.4%	48.0%
Export (%)	46.2%	38.6%	52.0%
Stampings	236.1	201.4	151.7
Domestic (%)	84.9%	79.5%	82.0%
Export (%)	15.1%	20.5%	18.0%
Hardware	891.5	603.4	458.0
Domestic (%)	79.4%	77.9%	76.0%
Export (%)	20.6%	22.1%	24.0%
Other	119.2	241.4	150.8
Domestic (%)	83.8%	88.3%	66.1%
Export (%)	16.2%	11.7%	33.9%
<b>Total</b>	<b>5,495.1</b>	<b>4,306.9</b>	<b>3,042.8</b>
Domestic (%)	74.6%	68.5%	67.5%
Export (%)	25.4%	31.5%	32.5%

The end users of our steel products vary. Our rebars are principally used in the construction industry. The main end users of our wire rods are small wire-drawing operations. Our carbon sheet is used in construction (covers, floor

plates), the automotive industry (spare parts) and pipe manufacturing and shipbuilding (non-critical applications). Our high-quality round bars are used in various moving parts manufactured by the automotive industry (spare parts, gear boxes), the machinery industry (hydraulic devices, drill bits), the shipbuilding industry (forged parts), the basic

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materials industry (molds, balls for crushing) and other industries. Our forgings and stampings are primarily used in the automotive, aerospace, petrochemical, textile and food and consumer goods sectors.

The following table sets forth by percentage a breakdown of our shipment volumes of all products produced in Russia by industry sector within the Russian market in 2008.

Use by Industry	Metal Works, Hardware Plants		Pipe Factories	Railway Construction, Repair		Power Generation	Other Industries <sup>(1)</sup>
				Engineering			
Semi-Finished Steel Products	0.0%	82.5%	0.0%	1.8%	0.0%	0.0%	15.6%
Long Steel Products	2.5%	0.5%	68.1%	17.7%	0.0%	0.3%	10.9%
Flat Steel Products	0.3%	11.6%	11.7%	17.4%	0.0%	0.5%	58.4%
Forgings	5.7%	71.2%	0.0%	5.4%	0.8%	0.5%	16.3%
Stampings	3.0%	0.0%	0.0%	85.1%	0.0%	5.5%	6.3%
Hardware	12.0%	2.1%	55.4%	14.3%	4.4%	0.3%	11.6%

(1) Including the defense, aerospace, petrochemical, textile, food and consumer goods sectors.

On November 13, 2008, Mechel OAO and Russian Railways signed an agreement for supply of rails during the 2011-2030 period. The annual supply volume is fixed at a minimum volume of 400,000 tonnes of rails per year.

**Marketing and distribution**

We use flexible sales strategies that are tailored to our customers and the markets we serve. Mechel Trading House, headquartered in Moscow, coordinates our Russian sales and had five branches that performed sales of metals products until December 2008. To segregate Mechel Trading House sales of coal and metals products, we took the decision to directly entrust our production facilities – Chelyabinsk Metallurgical Plant OAO, Izhstal OAO and Urals Stampings Plant – with responsibility for metals products sales and to subsequently transfer the employees of the Chelyabinsk, Urals, Izhevsk, Ulyanovsk and Togliatti branches of Mechel Trading House OOO to production facilities. Due to technical specifics of timelines for production and sales of metals products, the reallocation of sales functions was performed gradually, with all five branches of Mechel Trading House winding up their activities by December 2008. Currently each of our steel production facilities independently sells its metals products in to the market.

Mechel Trading AG, which in December 2008 moved its main offices from Zug to Baar, Switzerland, coordinates exports of our steel products through its branch in Schaan, Liechtenstein. In 2009, Mechel Trading AG will centralize exports of our steel products directly through its new headquarters in Baar.

Our overall sales strategy is to develop long-term, close partnerships with the end users of our products. As part of our end-user strategy, we research sales to distributors to identify the end user and directly market our steel capabilities and products to these customers. With respect to our largest end-user customers, we have established working committees, composed of our manufacturing engineers and customer personnel. These committees meet quarterly to monitor the performance of our products and ensure that our customers' specifications and quality requirements are consistently met. These committees also provide customers the opportunity to discuss their future needs with us. Our

sales force also regularly follows up with these and many of our other customers. We attend industry conferences and advertise in industry periodicals to market our products and capabilities. Through these efforts, we have established a strong brand identity for Mechel throughout Russia and other countries of the CIS, Central and Eastern Europe, Southeast Asia and the Middle East.

*Domestic sales*

The Moscow headquarters of Mechel Trading House serves as the central domestic sales office for coal, coke chemical and iron ore products. The Moscow office provides additional customer services for, and collects feedback from, our largest and most important customers, and the information gathered is directly provided to senior management. The Moscow office, by virtue of its location, is also well suited to develop new customers by

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approaching large Russian manufacturers headquartered in Moscow or those companies that have centralized purchasing offices in Moscow. The Moscow office is also involved in responding to tenders or requests for proposals, which is the most common method by which Russian companies procure the supply of raw materials.

In January 2006, we established Mechel Hardware OOO ( Mechel Hardware ), which in 2006, 2007 and early 2008 sold and marketed products produced at Beloretsk Metallurgical Plant, Vyartsilya Metal Products Plant and Mechel Nemunas to Russian and other markets. In 2008, in order to optimize our product portfolio and save marketing and distribution costs, Mechel Hardware was reorganized in order to merge with Mechel Trading House. As a result of reorganization sales forwarding functions were transferred to production subsidiaries, employees of Mechel Hardware were also transferred to our respective subsidiaries.

Our Russian steel production facilities are located in large industrial areas and have long-standing relationships some dating from the Soviet era with local end-user customers. Mechel Trading House had five branches that handled sales of metals products until December 2008. (See Marketing and distribution above for a description of Mechel Trading House's restructuring and the closing of its branches.). Mechel-Service has over 50 offices throughout Russia to serve our customers. Our service branches help us to develop and service our long-standing customer relationships by virtue of their proximity to both production and customers and thereby allow our local sales forces to provide highly specialized and technical sales and service support to our Russian customers.

Mechel Trading House had approximately 102 employees as of December 31, 2008. Mechel-Service had approximately 802 employees as of December 31, 2008.

### *Export sales*

Most of the export sales in our steel segment are made to independent distributors, which then sell our products to end users. Our subsidiary Mechel Trading has active sales offices in Liechtenstein, Belgium, Switzerland and Romania. In 2008, we closed our sales office in Vietnam. We are in the process of closing our Philippine and Austrian offices, which are inactive and were not used for sales in 2008.

For Mechel Trading's steel business, we had eight agents in 2008. They covered six different countries. However, in September 2008, we terminated relationships with three of them, and thus currently we have five agents covering five countries. We have an internationally oriented sales force which facilitates communications between our production facilities and the end users of our products, taking into account local and international business customs, including language requirements. Our use of a centralized international sales organization offers comprehensive and coordinated logistical and financial services to our export customers.

Our Romanian sales are carried out by our Romanian subsidiaries Mechel Campia Turzii and Mechel Targoviste.

We also sell steel products to wholesalers on a walk-in basis through large open and covered warehouse areas in the Port of Antwerp, Belgium. At this port, we primarily stock both rolled and forged bars, and intend to expand the product offering to cover other products such as wire rods and nails.

Mechel Trading and its branches and representative offices have approximately 54 employees.

### *Distribution*

Rail transportation is used for nearly all shipments from our production facilities and warehouses to our end customers, wholesale warehouses or sea ports.

***Market share and competition***

In our core export markets, we primarily compete with Russian and Ukrainian producers. The leading global steel manufacturers have been increasingly focused on value-added and higher-priced products. The principal competitive factors include price, distribution, product quality and customer service.

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In the Russian market, we compete on the basis of price and quality of steel products, their added value, product range and service, technological innovation and proximity to customers. The Russian steel industry is characterized by relatively high concentration of production, with the six largest integrated steel producers, including us, accounting for 84% of overall domestic steel output in 2008.

Following is a brief description of Russia's other five largest steel producers:

*Magnitogorsk Iron & Steel Works OAO* is Russia's largest steel manufacturer by volume, accounting for 18% of the volume of Russian rolled steel production in 2008. MMK's product mix is comprised mostly of flat products, representing 86% of its commercial steel products output (including production of slabs) in 2008. Domestically, MMK controls a significant portion of the supplies to the oil and gas and automotive sectors. MMK exported 45% of its output in 2008. Its production facilities are located in Magnitogorsk in the southern Urals.

*Evrax Group S.A.*, which includes the steel producers Nizhny Tagil Metallurgical Works OAO, ZapSib and Kuznetsky Metallurgical Works OAO, is the second Russia's largest steel manufacturer by volume on a consolidated basis, accounting for 18% of Russia's total rolled products output (including long products, flat products, semi-finished products) in 2008. Evrax Group focuses on the production of long products, including rebars, wire rods and profiled rolled products (such as rails, beams and channels). Evrax Group also controls iron ore producers Vanady Kachkanar GOK OAO and Vysokogorsky GOK OAO and coking coal producer Yuzhkuzbassugol Coal Company OAO, and has an equity investment in Raspadskaya OAO, which produces coking coal.

*Severstal OAO* had a 17% share by volume of Russian rolled steel production in 2008. The company specializes in flat products which constitute a significant part of its production. Severstal is the third-leading producer of flat products and controls 26% of Russia's total flat product production output. Domestic sales accounted for 69% of Severstal's output in 2008, with the oil and gas industry and automotive sector as its leading customers. Severstal also controls coal producer VorkutaUgol and iron ore producers Karelsky Okatysh and Olenegorsky GOK, which satisfy a portion of Severstal's coking coal and iron ore requirements.

*Novolipetsk Metallurgical Works OAO* had a 15% share by volume of Russian rolled steel production in 2008. The company produces primarily flat products (hot-rolled and cold-rolled), including galvanized products. NLMK exported 67% of its products in 2008. Domestically, NLMK's largest customers are in the construction and oil and gas industries, followed by companies in the automotive sector. NLMK also controls iron ore producer Stoylensky GOK. The company's steel facilities are located in Lipetsk, to the southeast of Moscow.

*Metalloinvest Management Company OOO*, which consists of Oskolsky Electric Metallurgical Works OAO (OEMK) and Ural Steel OAO, had a 9% share of Russian rolled steel production. OEMK produces only long products, and Ural Steel produces both long and flat products. Metalloinvest exported 65% of its rolled steel production in 2008. The company's production facilities are located in the Central and Urals federal districts of Russia. Alisher Usmanov, one of Metalloinvest's main owners, also controls Russia's largest iron ore and pellets production facilities—Lebedinsky GOK OAO and Mikhailovsky GOK OAO.

Source: Company websites; Metall-Expert.

These six companies, including us, can be divided into two groups by product type. MMK, Severstal and NLMK focus mainly on flat products, while we, Evrax Group and Metalloinvest produce primarily long products. Mechel is one of the largest and most comprehensive producers of specialty steel and alloys in Russia, and accounted for 25% of

total Russian specialty steel output by volume in 2008, according to Chernet and Metall-Expert. We are also the second largest producer of long steel products (excluding square billets) in Russia by volume, with significant market shares in both regular long steel products and specialty long steel products, according to Metall-Expert and Chernet.

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In the Russian non-specialty long steel product category, our primary products and our market positions by production volume as of year-end 2008 were as follows, according to Metall-Expert:

*Reinforcement bar ( rebar )* In rebar, we compete in the 6-40 millimeters range. In 2008, the largest domestic rebar producers were Evraz Group (28%), Mechel (22%) Nizhneserginsky MZ (19%) and Severstal (14%). At present, the Russian domestic market for rebar is protected from Ukrainian imports by an import quota. The quota has been imposed by agreement between Russia and Ukraine as the result of a review of the import tariff which was in force until July 14, 2007.

*Wire rod* There were five major producers of wire rod in Russia in 2008: Mechel (33%), Evraz Group (20%), Severstal (20%), MMK (15%) and Nizhneserginsky MZ (12%). We produce some of the highest quality and widest ranges of wire rod (5-10 millimeters) among Russian producers.

OEMK, an electric arc furnace steel mill specializing in long carbon and specialty steel products and our nearest specialty steel competitor, is located in the southwest of Russia and serves customers in the pipe, engineering and ball-bearing industries.

According to Metall-Expert and Chermet, we were one of the leading producers in Russia of specialty long steel products (bearing, tool, high-speed and stainless steel) in 2008, producing 17% of the total Russian output by volume, and we had significant shares of Russian 2008 production volumes of stainless long products (28%), tool steel (33%) and high-speed steel (33%). We were also Russia's largest producer of stainless flat products, with a 67% share of domestic production by volume in 2008. According to the Prommetiz association of Russian hardware manufacturers ( Prommetiz ), we were the first largest producer of hardware in Russia in 2008 with a 31% share in domestic production by volume, followed by Severstal (30%) and MMK (18%). For products in which we specialize, however, our share was substantially higher. For example, we had a 64% share of Russia's spring wire production and a 47% share of Russia's high-tensile wire production by volume during 2008.

The following tables set forth additional information regarding our 2008 market shares in Russia for various categories of steel products.

*All long products (excluding square billets)*

<b>Manufacturer</b>	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Market Share by Production Volume</b>
Evraz Group S.A.	6,355	30.1%
Mechel OAO	3,004	14.2%
Metalloinvest Management Company OOO	2,070	9.8%
Severstal OAO	1,804	8.5%
MMK OAO	1,585	7.5%
Other	6,306	29.9%
<b>Total</b>	<b>21,124</b>	<b>100%</b>

Source: Metall-Expert.

**Table of Contents***Long products Wire rod<sup>(1)</sup>*

<b>Manufacturer</b>	<b>Market Share by Production Volume</b>	
	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Volume</b>
Mechel OAO	885	32.5%
Evraz Group S.A.	548	19.9%
Severstal OAO	542	20.1%
MMK OAO	407	14.9%
Nizhneserginsky Metal and Hardware Plant ZAO	326	12.0%
Other	13	0.6%
<b>Total</b>	<b>2,721</b>	<b>100%</b>

Source: Metall-Expert.

(1) Including wire rod further processed into wire and other products within the same holding company.

*Long products Rebar*

<b>Manufacturer</b>	<b>Market Share by Production Volume</b>	
	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Volume</b>
Evraz Group S.A.	1,619	27.7%
Mechel OAO	1,304	22.3%
Nizhneserginsky Metal and Hardware Plant ZAO	1,100	18.8%
Severstal OAO	790	13.5%
MMK OAO	462	7.9%
Other	565	9.8%
<b>Total</b>	<b>5,840</b>	<b>100%</b>

Source: Metall-Expert.

*Flat stainless steel*

<b>Manufacturer</b>	<b>Production</b>	<b>Market Share by Production Volume</b>
	<b>(In thousands of tonnes, except for percentages)</b>	
Mechel OAO	36.8	67.2%
VMZ Red October	8.5	15.6%
Severstal OAO	6.7	12.2%
MMZ Hammer & Sickle	1.5	2.7%
Other	1.2	2.3%
Total	54.7	100%

Source: Metall-Expert.

**Table of Contents***Hardware*

<b>Manufacturer</b>	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Market Share by Production Volume</b>
Mechel OAO	650	30.5%
Severstal-Metiz OAO	632	29.6%
MMK-Metiz OAO	376	17.7%
Evraz Group S.A.	236	11.1%
Maksi-Group OAO	143	6.7%
Other	94	4.4%
Total	2,131	100%

Source: Prommetiz, manufacturers data.

*Hardware Spring wire*

<b>Manufacturer</b>	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Market Share by Production Volume</b>
Mechel OAO	53.4	64.4%
Severstal-Metiz OAO	24.9	30.0%
MMK-Metiz OAO	4.6	5.6%
Total	82.9	100%

Source: Manufacturers data.

*Hardware High-tensile wire*

<b>Manufacturer</b>	<b>Production</b>	<b>Market Share by Production Volume</b>
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	<b>(In thousands of tonnes, except for percentages)</b>	
Mechel OAO	62.2	46.8%
Severstal-Metiz OAO	57.7	43.4%
MMK-Metiz OAO	13.1	9.8%
Total	133.0	100%

Source: Manufacturers' data.

### ***Raw materials***

The principal raw materials we use in the making of steel are coke (produced from coking coal), iron ore, nickel, ferrous scrap and limestone. We supplied 60% of our own group-wide coking coal needs in 2008, although our total coking coal production volume exceeded our group's needs. We process coking coal concentrate into coke at Mechel-Coke, located in the Urals, and Moscow Coke and Gas Plant, which we acquired in 2006. Coke is used both in our steel-making operations at Chelyabinsk Metallurgical Plant, Izhstal and in our ferroalloys production. In 2008, we produced and internally used 2.2 million tonnes of coke in our production facilities and produced and sold another 1.1 million tonnes of coke to third parties. Our coal also fuels our power generation business: in 2008,

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Southern Kuzbass Coal Company supplied to Southern Kuzbass Power Plant 790,055 tonnes of steam coal and middlings for power generation.

Our steel-making operations use iron ore in the form of pellets, sinter, concentrate and sinter ore. The ultimate form of the iron ore feed into the steel-making process, however, consists of pellets and sinter only. In 2008, our steel-making operations used 5.7 million tonnes of iron ore feed, approximately 22% in the form of pellets and 78% in the form of sinter, and we internally sourced 33% of our total iron ore feed requirements during this period. Our Korshunov Mining Plant supplied us with 2.0 million tonnes of iron ore concentrate in 2008. Iron ore concentrate is converted into sinter at Chelyabinsk Metallurgical Plant. We purchase most of the remaining part of our iron ore feed, mainly in the form of pellets, from Russian domestic suppliers such as Kostomukshinsky GOK, Lebedinsky GOK and Mikhailovsky GOK under annual contracts on market terms.

In 2008, we used 3,826 tonnes of nickel in the production of stainless and other specialty steels. We sourced approximately 87% of our nickel requirements in 2008 from our nickel mining and smelting operations at Southern Urals Nickel Plant. We source other nickel grades from Norilsk Nickel, UfaLeynickel and other smaller nickel producers.

We produce 58% of steel in basic oxygen furnaces. Ferrous scrap represents approximately 46% of feedstock, and we are approximately 40% self-sufficient in this raw material, sourcing the balance from various scrap traders.

In March 2006, we acquired Metals Recycling, a Chelyabinsk-based metal scrap processing company, in line with our policy of ensuring the steel segment's self-sufficiency in raw materials. Metals Recycling processes scrap steel that we melt in our steel manufacturing facilities' electric arc furnaces and reprocess into steel products.

We internally source all of our limestone requirements from our Pugachev quarry. In 2008, we used approximately 1.2 million tonnes of limestone in the production of steel.

Steel-making requires significant amounts of electricity to power electric arc furnaces and rolling mills and to convert coal to coke. In 2008, our steel operations consumed approximately 3.1 billion kWh of electricity, of which 2.3 billion kWh was used at Chelyabinsk Metallurgical Plant, 563 million kWh was used at other Russian facilities and 165 million kWh was used at our Eastern European plants. Chelyabinsk Metallurgical Plant, Moscow Coke and Gas Plant and Mechel-Energo have power co-generation facilities, which produced 1.4 billion kWh of electricity for internal consumption in 2008, yielding 45% self-sufficiency overall for our group (including mining operations), which consumed 3.2 billion kWh of electricity in 2008. The balance was purchased from local utilities. Aside from Southern Kuzbass Power Plant and Toplofikatsia Rouse, which run on steam coal, our power-generating facilities work on blast furnace and coke gas, which are by-products of our steel-making operations, and natural gas, which we purchase from Gazprom. In 2008, we consumed 915.0 million cubic meters of blast furnace gas, 37.0 million cubic meters of coke gas and 2.0 billion cubic meters of natural gas.

Large amounts of water are also required in the production of steel. Water serves as a solvent, accelerator and washing agent. Water is used to cool the steel, to carry away waste, to help produce and distribute heat and power and to dilute liquids. One of the principal sources of water is rivers, and many of our facilities recirculate a portion of water used for their production needs. For example, Chelyabinsk Metallurgical Plant sources 9% of its water needs from a local river and the rest from recycled water. Vyartsilya Metal Products Plant sources 100% of its water needs from a local river. Southern Urals Nickel Plant sources 41% of its water needs through recycling, 56% from a local river. Mechel Targoviste sources 6% of its production water needs from a local river and the rest is recycled/recirculated water. To-date water consumption from local rivers has not resulted in any significant environmental issues, though we make no assurances that such issues will not arise in the future. The companies effect payments for the use of water resources and we believe their emissions and discharges are within the permissible

limits.

Transportation costs are a significant component of our production costs and a factor in our price-competitiveness in export markets. Rail transportation is our principal means of transporting raw materials from our mines to processing facilities and products to domestic customers and to ports for shipment overseas. For a description of our railway freight and forwarding subsidiary, see [Steel Business](#) [Marketing and distribution](#) [Distribution](#) above.

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For a description of how seasonal factors impact our use and reserve levels of raw materials see Item 5. Operating and Financial Review and Prospects Trend Information.

***Steel production facilities***

Most of our metallurgical plants have obtained a certificate of quality under ISO international standards. For example, the main manufacturing processes at Chelyabinsk Metallurgical Plant, Beloretsk Metallurgical Plant, Urals Stampings Plant, Izhstal, Mechel Campia Turzii and Mechel Targoviste are ISO 9001:2000 certified through 2009. Wire-drawing workshop No. 3 of Mechel Campia Turzii is ISO 14001 certified through 2011.

***Chelyabinsk Metallurgical Plant***

Chelyabinsk Metallurgical Plant produces semi-finished products for further milling in Russia for our internal needs. Chelyabinsk Metallurgical Plant is an integrated coke and gas, sintering production, blast furnace, BOF/EAF steel mill and rolling production. It produces semi-finished steel products, flat and long carbon and stainless steel products. Its customer base is largely comprised of customers from the construction, engineering, hardware and ball-bearing industries. We acquired Chelyabinsk Metallurgical Plant in 2001.

The plant sources all of its coking coal needs from Southern Kuzbass Coal Company and from Yakutugol and most of its iron ore needs from our Korshunov Mining Plant and a majority of its nickel needs from our Southern Urals Nickel Plant. In 2006, coke production and specialty steel production were separated from Chelyabinsk Metallurgical Plant into separate entities which are wholly owned subsidiaries of Chelyabinsk Metallurgical Plant. In August 2007, ownership of Chelyabinsk Metallurgical Plant's specialty steel operations was transferred to the Chelyabinsk branch of Urals Stampings Plant, though for presentation purposes Chelyabinsk Metallurgical Plant's specialty steel operations are presented in this section.

Chelyabinsk Metallurgical Plant's (including the Chelyabinsk branch of Urals Stampings Plant) principal steel and wire production lines include a BOF workshop equipped with three converters; three EAF workshops equipped with electric arc ovens, including two large ovens of 100 and 125 tonnes, respectively; small-capacity direct- and alternating-current furnaces, vacuum induction and plasmic furnaces; vacuum arc and electroslag remelting furnaces; five comprehensive steel treatment machines; two steel vacuum-degassed machines, an argon-oxygen refining machine; four continuous billet-casters; a blooming machine with continuous rolling mill for 200-320 millimeter and 80-180 millimeter billets; six long product mills for 8-190 millimeter diameter round bar and 75-156-millimeter square bar, 6.5-10 millimeter wire rod, rebar steel, bands and shaped beams; a hot-rolled flat product workshop with a thick sheet continuous rolling mill for hot-rolled sheets of up to 1,800 millimeters wide and up to 20 millimeters thick; a semi-continuous rolling mill for up to 1,500 millimeters wide and up to 6 millimeters thick hot-rolled coils; a cold-rolled product workshop for 0.3-4 millimeter cold-rolled stainless sheet; a forged piece hammer workshop; and a forging and pressing workshop equipped with five presses and forging machines of 1,250-2,000 tonnes. Also we have at our Chelyabinsk Metallurgical Plant, together with Mechel-Coke, eight coking batteries, seven sintering machines and three blast furnaces. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for each of Chelyabinsk Metallurgical Plant's principal production areas.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		

Sintering	5,800	81.9%	700
Pig Iron	3,800	92.1%	
Steel-making	5,100	92.3%	
Rolling	4,730	86.8%	
Forging and pressing	100	69.0%	
Coking	3,100	71.0%	

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Chelyabinsk Metallurgical Plant produced, together with its wholly owned subsidiary Mechel-Coke, 4.7 million tonnes of raw steel, 4.1 million tonnes of rolled products and 2.2 million tonnes of coke in 2008.

In the second half of the year ended December 31, 2007, we began an upgrade of Chelyabinsk Metallurgical Plant's arc-furnace melting shop No. 6 to increase continuous slab production capacity to 1.2 million tonnes per year. Danieli is the basic equipment provider for concasting machine and out-of-furnace processing complex. Currently, construction works are being carried out and equipment is being supplied to the site.

On June 30, 2008, our subsidiary Chelyabinsk Metallurgical Plant entered into an agreement with Danieli & C. Officine Meccaniche S.p.A., an Italian supplier of equipment and plants to the metals industry, to build and install a 1.0 million tonne-per-year rolling mill for production of steel rails, structural beams and sections. The total value of the contract is 250.0 million, including 239.4 million for rolling mill equipment, 4 million plus VAT for engineering works and 6.6 million plus VAT for other services. In accordance with the contract, Danieli is scheduled to complete the installation of the new rolling mill by December 2010.

On October 29, 2008, Chelyabinsk Metallurgical Plant signed a contract with the Chinese construction company Minmetals Engineering Co. Ltd. ( Minmetals ) for a turnkey project to rebuild a rolling mill and install a universal mill. The new universal mill is intended to produce high-quality, 100-meter rails under our supply contract with Russian Railways OAO ( Russian Railways ). The contract's total value is approximately \$355.1 million. The project completion date under the construction contract is November 3, 2010, which Minmetals has a right to extend. The contract is subject to the occurrence of certain conditions and has not yet come into force.

*Izhstal*

Izhstal is a specialty steel producer located in the western Urals city of Izhevsk, in the Udmurt Republic, a Russian administrative region also known as Udmurtia. Its customer base is largely comprised of companies from the aircraft, defense, automotive, agricultural, power, oil and gas and construction industries. We acquired Izhstal in 2004.

Izhstal's principal production lines include five EAFs of 30 tonnes each; aggregate ladle stove and ladle vacuum machine with oxygen decarburization; three open hearth furnaces of 130-135 tonnes each; blooming machine for 100-220 millimeter square billets; three medium-sized long products rolling mills for 30-120 millimeter round bars, 30-90 millimeter square bars, bands and hexagonal bars; and one continuous small long products wire mill for 5.5-29 millimeter round, 12-28 millimeter square and 12-27 millimeter hexagonal light sections, reinforced steel and bands. It also has a hardware workshop, equipped with various drawing mills, a pickling line and a forging workshop, equipped with a number of sledgehammers and press-cutters. The following table sets forth the capacity and the capacity utilization rate for each of Izhstal's principal production areas.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Steel-making	700	73.1%	
Rolling	1,000	32.2%	
Hardware	98	38.4%	
Forging and stamping	60	28.9%	

Izhstal produced approximately 511.6 thousand tonnes of raw steel, 321.7 thousand tonnes of rolled products, 37.6 thousand tonnes of hardware and 17.3 thousand tonnes of stampings and forgings in 2008.

In 2008, Izhstal's total output was reduced as part of our strategy to focus on high-quality products. Other reasons for Izhstal's low capacity utilization rates were reduced customer orders and the inefficiency of running high-capacity industrial processes like blooming mills at a low utilization rate. To improve Izhstal's efficiency, in the second half of 2007 we began the first stage of an upgrade at the Izhstal mill, including the installation of a new modern electric arc furnace with a total capacity of 40 tonnes and an out-of-furnace processing complex and new concasting machine, reconstruction of rolling mill No. 250 and the disposal of outdated open-hearth furnaces. Currently, construction works are being carried out and equipment is being supplied to the site. The upgrade process

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is expected to result in: (1) significant reductions in consumption of metal, natural gas and electric power in rolled product manufacturing, and (2) improvements in product quality to meet current international standards and expansion of product range, and (3) environmental improvement in the city.

*Beloretsk Metallurgical Plant*

Beloretsk Metallurgical Plant is a hardware plant in the city of Beloretsk, in the southern Ural mountain range, that produces wire rod and a broad range of hardware from semi-finished steel products supplied by Chelyabinsk Metallurgical Plant. Its customers are largely from the construction and engineering industries. We acquired Beloretsk Metallurgical Plant in 2002.

Beloretsk Metallurgical Plant's principal production lines include a steel-rolling workshop equipped with a wire mill for production of wire rod of 5.5-12 millimeters in diameter and a number of hardware workshops equipped with drawing, winding, unwinding, rewinding, polishing and rope machines and thermal treatment ovens. In 2007, we invested \$3.1 million to improve product quality, increase output, reduce production costs, and increase profitability. Due in part to this investment, in February 2008 we succeeded in introducing an advanced technology to produce stabilized reinforcing wire for prestressed concrete structures used in the construction industry. In 2008, the new stranding machine was commissioned at Beloretsk Metallurgical Plant. We invested \$2.5 million to improve product quality and production efficiency. We built a warehouse complex for finished products. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for each of Beloretsk Metallurgical Plant's principal production areas.

<b>Production Areas</b>	<b>Capacity in 2008 (In thousands of tonnes, except for percentages)</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
Rolling	560	96.6%	
Hardware	417	97.7%	

Beloretsk Metallurgical Plant produced a total of 614,811 tonnes of steel products made from semi-finished steel products in 2008, including 207,575 tonnes of wire rod and 407,236 tonnes of hardware.

*Vyartsilya Metal Products Plant*

Vyartsilya Metal Products Plant is a hardware plant in the Karelian Republic, an administrative region in northwestern Russia near the Finnish border, that produces low carbon, welding and structural wire, zinc-plated nails, and steel and polymeric-coated nets, from wire rod supplied by Chelyabinsk Metallurgical Plant and Beloretsk Metallurgical Plant. The plant's customers are largely from the construction, automotive and furniture industries. We acquired Vyartsilya Metal Products Plant in 2002.

Vyartsilya Metal Products Plant's principal production facilities include drawbenches and nail-making and mesh-weaving machines. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Vyartsilya Metal Products Plant's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
Hardware	91	101%	

Vyartsilya Metal Products Plant produced 91,953 tonnes of hardware in 2008.

*Urals Stampings Plant*

Urals Stampings Plant is Russia's largest producer of stampings from specialty steels and heat-resistant and titanium alloys for the aerospace, oil and gas, heavy engineering, railway transportation, power and other industries. Urals Stampings Plant sources its specialty steel needs from Chelyabinsk Metallurgical Plant. We acquired Urals Stampings Plant in 2003.

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Urals Stampings Plant's principal production facilities include 1.5-25 tonne swages and hydraulic presses. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Urals Stampings Plant's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008 (In thousands of tonnes, except for percentages)</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
Stampings and forgings	100	68.5%	

Urals Stampings Plant produced 58,506 tonnes of specialty steel stampings in 2008.

*Mechel Targoviste*

Mechel Targoviste is a major Romanian EAF steel mill that produces specialty and carbon long products, forgings, and hardware. Mechel Targoviste is the largest producer of long products in Romania and the second largest producer of raw steel in Romania, according to UniRomSider, a Romanian association of steel manufacturers. The plant's customers are largely from the engineering, automotive, tool, ball-bearing, tube, hardware and construction industries. We acquired Mechel Targoviste in 2002.

Mechel Targoviste's principal production lines include an EAF workshop equipped with one modernized electric arc furnace with a 75-tonne capacity; steel vacuum processing and two stove-basket aggregates; a continuous billets caster; a blooming machine for 80-400 millimeter square and 90-145 millimeter round billets; and two continuous long products rolling mills for 20-80 millimeter round bars, 24-57 millimeter hexagonal bars, 60-70 millimeter square bars, bands of 6-12 millimeter thickness and 60-120 millimeter width, 12-26 millimeter bundle rod and reinforcing steel; and a press-forging workshop. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for each of Mechel Targoviste's principal production areas.

<b>Production Areas</b>	<b>Capacity in 2008 (In thousands of tonnes, except for percentages)</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
Steel-making	550	86.9%	
Forging and pressing	37	7.2%	
Rolling	780	57.5%	
Hardware	18	3.6%	

Mechel Targoviste produced 477,829 tonnes of raw steel and 448,744 tonnes of rolled products in 2008.

In 2008, Mechel Targoviste experienced low rolling capacity utilization rates due to efforts to reduce production costs and increase quality, as well as due to the inefficiency of running its blooming process, involving high-capacity machinery with high power requirements, at low capacity utilization levels.

*Mechel Campia Turzii*

Mechel Campia Turzii is a leading Romanian domestic hardware plant that produces different kinds of hardware (including various types of wire, ropes, nets, welding electrodes and nails) as well as long steel products. The plant's customers are largely from the construction and engineering industries. We acquired Mechel Campia Turzii in 2003.

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Mechel Campia Turzii's principal production lines include several hardware workshops equipped with drawing, nail-making and zinc-plating machines. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for each of Mechel Campia Turzii's principal production areas.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Rolling <sup>(1)</sup>	300	79.6%	
Hardware	100	73.1%	

(1) Includes steel rolled for further processing in the hardware manufacturing process as well as rolling of products ready for sale.

Mechel Campia Turzii produced 162,482 tonnes of rolled products and 73,089 tonnes of hardware in 2008.

One arc-furnace melting workshop and two rolling mills were taken off-line in the course of our reorganization of the production line at Mechel Campia Turzii.

*Mechel Nemunas*

Mechel Nemunas is a Lithuanian hardware plant that produces wire, calibrated steel products, nails, rods and nets. Its customers are primarily from the construction, engineering and furniture industries. We acquired Mechel Nemunas in 2003.

Mechel Nemunas's principal production facilities include drawing mills, and nail-making, threading, net-weaving, net-wicking and contact-welding machines. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Mechel Nemunas's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Hardware	70	92.5%	

Mechel Nemunas produced 52,125 tonnes of hardware products in 2008.

*Ductil Steel*

In April 2008, we acquired a 100% stake in Ductil Steel S.A. ( Ductil Steel ) for a purchase price of \$224.0 million. Ductil Steel is a Romanian company that owns the Ductil Steel Buzau plant, which produces carbon and low alloyed steel rolled and wire products, and the Otelu Rosu plant, which produces steel and billets for rolling. The Otelu Rosu plant's products are supplied to the Buzau plant and to third parties both domestically within Romania and abroad for further processing. From the date of acquisition in April 2008 through December 2008, Ductil Steel produced 218,284 tonnes of raw steel, 118,303 tonnes of long products, 26,632 tonnes of wire mesh, 21,966 tonnes of wire, 4,882 tonnes of nails, and 1,225 tonnes of wire ropes, as well as 211,722 tonnes of continuous-cast billets. The results of operations of Ductil Steel are included in our consolidated financial statements from April 8, 2008, the date when we acquired control of it.

Before this acquisition, we had already owned two steel plants in Romania: Mechel Targoviste and Mechel Campia Turzii. Following our acquisition of Ductil Steel, in order to enhance the performance and efficiencies of our Romanian subsidiaries, we established Mechel East Europe Metallurgical Division, effective from October 22, 2008.

The main objective of the Mechel East Europe Metallurgical Division will be to coordinate the operations of Mechel's steel subsidiaries in Eastern Europe, including investment, modernization, streamlining and production cost reduction efforts through the implementation of efficient logistics planning for raw material purchases and product marketing. Additionally, the Mechel East Europe Metallurgical Division will handle human resources

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policy and coordinate contacts with banks and other financial institutions. The division's top priority will be the modernization of the Ductil Steel Buzau, Otelu Rosu and Mechel Campia Turzii steel plants.

Ductil Steel's principal production facilities include a continuous billets caster, a continuous rolling mill and several hardware workshops equipped with drawing, nail-making and zinc-plating machines. The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Ductil Steel's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Steel-making	388	71.8%	
Rolling	300	66.2%	
Hardware	105	74.0%	

Ductil Steel produced 278.4 tonnes of raw steel and 198.5 tonnes of rolled products in 2008.

***Trade restrictions***

Trade restrictions in the form of tariffs, duties and quotas are widespread in the steel industry. However, we are less exposed than most other Russian steel producers to these trade restrictions as restrictions on Russian exports have mainly been directed against flat products, whereas most of our exports consist of long products, such as wire rods and rebar. In addition, the abolition by the Russian government of steel export duties in 2002 has also effectively improved exports of Russian steel. See Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry We face numerous protective trade restrictions in the export of our steel products and ferroalloys, and we may face export duties in the future.

In 2008, approximately 12% of our steel segment export sale revenues were derived from sales of steel products that were subject to import restrictions. We describe below the main applicable trade restrictions in our key markets.

***European Union***

Our steel sales to the E.U. in 2008 were approximately \$1.3 billion, or 24% of our total steel segment revenues. The Russian government and the E.U. have an export quota system in place whereby Russian exports to the E.U. are limited to certain stipulated quantities for each product category. The quota by product category is distributed among Russian producers based on a procedure jointly developed by the Ministry of Economic Development and Trade of the Russian Federation and the Ministry of Industry and Energy of the Russian Federation. Effective May 13, 2008, these ministries have been reorganized into the Ministry of Economic Development and the Ministry of Industry and Trade, respectively, with the old Ministry of Industry and Energy's energy functions being transferred to a new Ministry of Energy and the trade functions of the old Ministry of Economic Development and Trade being transferred to a new Ministry of Industry and Trade. The procedure provides that for each product category, a company's export quota allocation is calculated on the basis of shipments by the company of the particular product over the previous years to the E.U. market (which is given a 70% weight), and on the company's market share in domestic production of the particular product (which is given a 30% weight). After the quotas are calculated, the Russian Ministry of Industry

and Trade confirms quota allocations and issues export licenses for these quotas. In 2008, the quota covered approximately 49% of our steel segment products exported to the E.U.

In 2008, the total E.U. quota for Russian steel was 3,183 thousand tonnes, and we received 346.1 thousand tonnes of the total quota. We have used 73% of our individual quotas both in long and flat steel products. The E.U.-Russia Steel Agreement for 2009 provides for the total Russian quota to be 3,107 thousand tonnes. Our quota is set at approximately 318.5 thousand tonnes, which includes 20.5 thousand tonnes for flat products and 298.0 thousand tonnes for long products. Our supply of wire rod to Mechel Nemunas, our hardware plant in Lithuania, and to our Romanian subsidiary Mechel Campia Turzii is also subject to the E.U. export quota system, and our quota for those supplies is 105.5 thousand tonnes for 2009. See Item 3. Key Information Risk

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**Factors Risks Relating to Our Business and Industry** We face numerous protective trade restrictions in the export of our steel products and ferroalloys, and we may face export duties in the future.

In addition, an antidumping E.U. import duty in the amount of 50.7% was applicable to steel ropes and cables manufactured by our Beloretsk Metallurgical Plant until October 2007. After a review procedure conducted by the E.U., in October 2007, this duty was reduced to 36.2% and imposed for a period of five years.

### *United States*

The United States has a quota system in place with respect to imports of hot rolled flat-rolled carbon quality steel and thick steel plate. Intergovernmental quota agreements provide for quotas and reference prices on Russian exports of these products to the United States. A distribution of quotas between specific Russian producers and the execution of export licenses is carried out in accordance with the same procedure that applies to exports to the E.U. market. There are no trade restrictions applicable to the export of our Romanian or Lithuanian products to the United States.

## **Ferroalloys Business**

### ***Mining and manufacturing processes***

*Nickel ore.* Both the Sakhara and Buruktal mining operations run by our Southern Urals Nickel Plant are typical of Russian open pit mines of their size. The weathered lateritic ores and overburden (the layers of soil covering the ore-bearing stratum) can be directly loaded by electric shovel and dragline into haul trucks without any drilling or blasting. The ore is stockpiled and then loaded into railcars for shipment to Southern Urals Nickel Plant. Overburden waste is hauled to dumping locations inside the mined-out pits whenever possible or placed in dumps adjacent to the pit.

*Low-ferrous ferronickel.* Nickel ores from both mines are transported by rail to our nickel production plant in the city of Orsk, which lies east of the southern extremity of the Ural Mountains, close to the border with Kazakhstan. At this plant, ores are mixed in a 1:1 ratio and sintered in sintering machines. Sinter with the addition of coke, sulfur pyrite and limestone is smelted in shaft furnaces that produce matte. This matte is then divided into converter matte and waste slag in oxygen converters. Converter matte is processed into nickel monoxide and nickel monoxide is further processed into ferronickel. Ferronickel is shipped via rail from Orsk to our Chelyabinsk Metallurgical Plant and to St. Petersburg or Kaliningrad for further international delivery.

*Ferrosilicon.* Ferrosilicon is produced in electric arc furnaces in a continuous ore smelting process. Silicon is reduced from quartzite with coke and coal carbon and alloyed with steel cutting iron. Ferrosilicon is discharged from the furnace periodically. After cooling, metal ingots are split and sorted into various commercial fractions.

*Ferrochrome.* Carbon ferrochrome is produced in electric arc furnaces in a continuous ore smelting process. Chrome and iron are reduced from chrome ore concentrate with coke carbon, with up to 8% of the carbon being dissolved in this alloy. Carbon ferrochrome is discharged from the furnace periodically. After cooling, metal ingots are split and sorted into various commercial fractions.

### ***Description of key products***

*Ferrosilicon.* Ferrosilicon is used in ferrous metallurgy as a deoxidizer or as an alloying element for production of electrotechnic, spring wire, corrosion-resistant and heat resistant steel grades, or as a pig iron modifier. In nonferrous metallurgy, ferrosilicon is used as a reducing agent for production of nonferrous metals and alloys. We offer our customers ferrosilicon from our Bratsk Ferroalloy Plant.

*Low-ferrous ferronickel.* Low-ferrous ferronickel is used in production of corrosion-resistant and heat resistant steel grades. Southern Urals Nickel Plant offers low-ferrous ferronickel to export customers, as well as to a number of companies within Russia and within our group.

*Ferrochrome.* Carbon ferrochrome is used in the iron industry to alloy construction steel and heat-resistant and stainless steels. We produce carbon ferrochrome at our Tikhvin Ferroalloy Plant and we use it both internally within our group and for export, as well as for domestic sales within Russia.

**Table of Contents*****Sales of ferroalloy products***

The following table sets forth our revenues by primary ferroalloys segment product categories (including as a percentage of total ferroalloys segment revenues) for the periods indicated. Ferroalloys segment sales data presented in Ferroalloys Business do not include intersegment sales.

Revenues	2008		2007		2006	
	Amount	% of Revenues	Amount	% of Revenues	Amount	% of Revenues
	(In millions of U.S. dollars, except for percentages)					
Nickel <sup>(1)</sup>	281.3	64.8%	468.9	93.6%	258.7	99.5%
Ferrosilicon	79.3	18.2%	29.0	5.8%	0.0	0.0%
Ferrochrome	68.2	15.7%	0.0	0.0%	0.0	0.0%
Other	5.2	1.3%	3.2	0.6%	1.2	0.5%
Total	434.0	100%	501.1	100%	259.9	100%

(1) Sales of nickel contained in ferronickel and converter matte.

The following table sets forth by percentage of sales the regions in which our ferroalloys segment products were sold for the periods indicated.

Region <sup>(1)</sup>	2008	2007	2006
Russia	23.0%	6.3%	0.5%
Other CIS	0.1%	0.0%	0.0%
Europe	74.4%	93.6%	99.5%
Asia	1.4%	0.1%	0.0%
Middle East	0.0%	0.0%	0.0%
United States	1.1%	0.0%	0.0%
Other	0.0%	0.0%	0.0%
	100%	100%	100%

(1) The regional breakdown of sales is based on the geographic location of our customers, and not on the location of the end users of our products, as our customers are often distributors that resell and, in some cases, further export our products.

In 2008, our ferroalloys segment sales outside of Russia were principally to Europe. Sales in Europe accounted for 74% of our total ferroalloys segment sales.

<b>Customer</b>	<b>% of Total Ferroalloys Segment Sales</b>	<b>Product</b>	<b>% of Total Products Sales</b>
Glencore International AG	43.2%	Nickel	50.0%
		Chrome	68.2%
Stratton Metals LTD	18.8%	Nickel	29.0%
Outokumpu Rossija Oy	9.4%	Nickel	14.4%
		Chrome	0.2%
Metalloinvest-steel OOO	5.5%	Ferrosilicon	30.0%
Kola Metals & Mining Company OAO	4.3%	Nickel	6.6%

In 2008, the five largest customers of our ferroalloys segment products were Glencore International AG, Stratton Metals Limited, Outokumpu Rossija Oy, Metalloinvest-steel OOO and Kola Metals & Mining Company OAO, which together accounted for 81% of our ferroalloys segment sales.

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The following table sets forth information on our domestic and export sales of our primary ferroalloys categories for the periods indicated. We define exports as sales by our Russian and foreign subsidiaries to customers located outside their respective countries. We define domestic sales as sales by our Russian and foreign subsidiaries to customers located within their respective countries. See note 25 to our consolidated financial statements in Item 18. Financial Statements.

<b>Products</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>
	<b>(In millions of U.S. dollars, except for percentages)</b>		
Nickel <sup>(1)</sup>	281.3	468.9	258.7
Domestic (%)	6.6%	0.0%	0.0%
Export (%)	93.4%	100.0%	100.0%
Ferrosilicon	79.3	29.0	0.0
Domestic (%)	92.0%	97.3%	
Export (%)	8.0%	2.7%	
Ferrochrome	68.2		
Domestic (%)	6.0%		
Export (%)	94.0%		
Other	5.2	3.3	1.2
Domestic (%)	94.3%	100.0%	100.0%
Export (%)	5.7%	0.0%	0.0%
<b>Total</b>	<b>434.0</b>	<b>501.1</b>	<b>259.9</b>
Domestic (%)	23.2%	6.3%	0.5%
Export (%)	76.8%	93.7%	99.5%

(1) Sales of nickel contained in ferronickel and converter matte.

**Marketing and distribution***Domestic sales*

Nickel is supplied to the Russian domestic market, primarily within our group. Only 7% of total nickel revenues were received from domestic converter matte sales in 2008. Converter matte is an intermediate product in the regular ferronickel production chain containing nickel and cobalt. In 2008, converter matte was supplied from Southern Urals Nickel Plant to Kola MMC, one of Norilsk Nickel production facilities.

Ferrosilicon in 2008 was sold into the Russian domestic market to such consumers as Metalloinvest-Steel OOO, Evraz Group AG enterprises (Zapsib, NTMK, NKMK) and Severstal OAO, which together accounted for 82% of the total ferrosilicon sales by revenue and 15% of the total ferroalloys segment revenues.

Metalloinvest holding enterprises (OEMK and Urals Steel) were major domestic ferrochrome customers in 2008. Such sales accounted for 6% of the total ferrochrome sales and 1% of the total ferroalloys segment revenues.

*Export sales*

All of our nickel export sales in 2008 were delivered to three customers: Glencore International AG, Stratton Metals Ltd. and Outokumpu Rossija Oy. Those sales together accounted for 93% of our total nickel sales and 60% of our total ferroalloys segment revenues. Prices are settled on the basis of nickel prices quoted by the London Metal Exchange (LME), less a certain discount. The nickel is delivered by railway from Southern Urals Nickel Plant to either the port of St. Petersburg or to the Russian-Finnish border.

In the fourth quarter of 2008, we resumed deliveries of ferrosilicon for export after an 18 month hiatus. This hiatus was caused by high demand for ferrosilicon in the domestic market. Ferrosilicon was sold to Japan only in

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2008. Deliveries to Japanese customers were effected on CFR delivery terms (including transportation by railway, handling in ports of Vanino and Nakhodka and chartering vessels to major Japanese ports).

Ferrochrome sales in 2008 were effected mainly through such trading companies as Glencore International AG and DCM DECOMetal GmbH to the European and U.S. markets. Those sales together accounted for 86% of our total ferrochrome sales and 13% of the total ferroalloys segment revenues. Ferrochrome was delivered by railway to the ports of St. Petersburg or Klaipeda.

**Market share and competition**

According to Metall-Expert, Mechel is the third largest Russian producer of ferrosilicon and ferrochrome by volume. In 2008, we had a 15% and 12% market share by volume of Russian ferrosilicon and ferrochrome production, respectively.

Following is a brief description of Russia's other largest ferroalloys producers, according to Metall-Expert and the companies' data:

*Kuznetsk Ferroalloys OAO* is the largest Russian ferrosilicon producer, with a 53% market share by production volume in 2008. It controls Yurginsk Ferroalloys Plant OAO. Kuznetsk Ferroalloys produces microsilica and quartzite. It is primarily export-oriented, having exported 88% of its ferrosilicon production volume in 2008.

*Chelyabinsk Electro-Metallurgical Plant OAO (ChEMK)* is the largest Russian ferrochrome producer, with a 53% market share by production volume in 2008. It is also the second largest ferrosilicon producer with a 19% production share in 2008. It also produces silicomanganese and silicocalcium. ChEMK exports most of its production. In 2008, it exported 93% and 57% by volume of its ferrochrome and ferrosilicon production, respectively.

*Serov Ferroalloys Plant OAO* is the second largest Russian ferrochrome producer, with a 34% market share by production volume in 2008. It is also one of Russia's largest ferrosilicon producers, with a 6% production share in 2008. The plant is controlled by the Kazakh industrial group ENRC, which is one of the largest chrome ore and ferrochrome producers in the world, according to CRU. Serov also produces ferrosilicochrome. Serov exported 75% of its ferrochrome production volume in 2008, and almost all of the ferrosilicon it produced in 2008 was supplied domestically.

*Ferroalloys Ferrosilicon*

<b>Manufacturer</b>	<b>Region</b>	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Market Share by Production Volume, %</b>
Kuznetsk Ferroalloys OAO	Kemerov region	296.4	52.6%
Chelyabinsk Electro-Metallurgical Plant OAO	Chelyabinsk	109.4	19.4%
Bratsk Ferroalloy Plant OAO	Irkutsk region	84.3	15.0%
Serov Ferroalloys Plant OAO	Sverdlovsk region	31.5	5.6%
Novolipetsk Metallurgical Plant OAO	Lipetsk region	24.0	4.3%
Yurginsk Ferroalloys Plant OAO	Kemerov region	17.8	3.1%

Total	563.4	100%
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Source: Metall-Expert.

**Table of Contents***Ferroalloys Ferrochrome*

<b>Manufacturer</b>	<b>Region</b>	<b>Production (In thousands of tonnes, except for percentages)</b>	<b>Market Share by Production Volume, %</b>
Chelyabinsk Electro-Metallurgical Plant OAO	Chelyabinsk	242.7	53.2%
Serov Ferroalloys Plant OAO	Sverdlovsk region	155.6	34.1%
Tikhvin Ferroalloy Plant ZAO	Leningrad region	55.3	12.1%
Klyuchevsk Ferroalloys Plant OAO	Sverdlovsk region	2.2	0.6%
Total		455.8	100%

Source: Metall-Expert.

The Russian nickel market is heavily dominated by Norilsk Nickel OAO, which according to its company website produced 232,300 tonnes of nickel in 2008 at its Russian facilities and has more than a 90% share of Russian domestic nickel output by volume.

***Nickel ore and nickel production***

Southern Urals Nickel Plant operates two open-pit nickel ore mines, Sakhara and Buruktal, as well as a nickel production plant in Orsk. The Sakhara mine is located east of the Ural Mountains in Chelyabinsk region, about 370 kilometers north of Orsk. The Buruktal mine is located east of the southern tip of the Ural Mountains, in Orenburg region, close to the border with Kazakhstan. It is located 230 kilometers east of Orsk. We acquired Southern Urals Nickel Plant in 2001.

The table below sets forth the subsoil licenses used by our nickel mines and the expiration dates thereof.

<b>License Area</b>	<b>License Holder</b>	<b>License Expiry Date</b>	<b>Status</b>	<b>Area (sq. km)</b>	<b>Year Production Commenced</b>
Buruktal	Southern Urals Nickel Plant	December 2012	In production	11.9	1968
Sakhara	Southern Urals Nickel Plant	April 2013	In production	2.2	1994

The following table summarizes our nickel ore and nickel products production for the periods indicated:

<b>2008</b>		<b>2007</b>		<b>2006</b>	
<b>Tonnes</b>	<b>Grade (% Ni)</b>	<b>Tonnes</b>	<b>Grade (% Ni)</b>	<b>Tonnes</b>	<b>Grade (% Ni)</b>

(In thousands of tonnes)<sup>(1)</sup>

Sakhara ore production	1,025.7	1.07%	1,236.1	1.13%	1,118.3	1.10%
Buruktal ore production	1,436.4	1.05%	1,591.3	1.05%	1,240.3	1.05%
Total ore production	2,462.1	1.06%	2,827.4	1.09%	2,358.6	1.07%
Nickel production	16,158.0		17,111.0		14,436.0	

(1) Volumes are reported on a wet basis.

### ***Chrome ore and silicate nickel ore production***

Oriel Resources Ltd. holds two licenses in the Republic of Kazakhstan to mine chrome ore at the Voskhod deposit in Aktyubinsk region and silicate nickel ore at the Shevchenko deposit in Kustanay region, and owns a processing plant located near the Voskhod underground mine.

Voskhod is located in the Chrometau district of Aktyubinsk region 110 kilometers east of Aktobe and seven kilometers northeast of Chrometau. Chrome ore mining commenced at the Voskhod underground mine in December 2008.

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The Shevchenko deposit of silicate nickel ore is located in Kazakhstan's Kustanay region and we plan to produce nickel ore there using the open-pit mining method for further processing into marketable ferronickel.

The table below sets forth the subsoil licenses used by our chrome ore and silicate nickel ore properties and the expiration dates thereof.

<b>License Area</b>	<b>License Holder</b>	<b>License Expiry Date</b>	<b>Status</b>	<b>Area (sq. km)</b>	<b>Year Production Commenced</b>
Voskhod	Voskhod-Oriel	October 2029	In production	1.54	2008
Shevchenko	Kazakhstansky Nickel Mining Company	March 2017	Feasibility study	135	n/a

***Quartzite production***

Bratsk Ferroalloy Plant holds the license for exploration and mining of the Uvatskoye deposit of quartzite and quartzite sandstones, a raw material for ferrosilicon production. The deposit is accessible by unpaved road and located 20 km southwest of Nizhneudinsk in Irkutsk region. After completion of additional exploration at the deposit in 2011 we plan to start mining quartzite to be supplied to our Bratsk Ferroalloy Plant.

The table below sets forth the subsoil license held in respect of our quartzite project and the expiration date thereof.

<b>License Area</b>	<b>License Holder</b>	<b>License Expiry Date</b>	<b>Status</b>	<b>Area (sq. km)</b>	<b>Year Production Commenced</b>
Uvatskoye	Bratsk Ferroalloy Plant	July 2033	Exploration	18.21	n/a

***Mineral reserves (ferroalloys)***

Please see Mining Business Mineral reserves (coal, iron ore and limestone) for a description of our mineral reserves and mineral deposits generally and our reporting of proven and probable reserves.

***Nickel ore***

As of December 31, 2008, we had nickel ore reserves (proven and probable) totaling 9.6 million tonnes at an average nickel grade of 1.0%. The table below summarizes our nickel ore reserves by mine.

<b>Nickel Ore Reserves<sup>(1)(2)(3)</sup></b>	<b>Tonnes<sup>(4)</sup></b>	<b>Grade (% Ni)<sup>(5)</sup></b>
	<b>(In millions of tonnes)</b>	
Sakhara	4.0	1.2%
Buruktal	5.6	0.9%

Total	9.6	1.0%
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- (1) Reserve estimates use the tonnages that are expected to be mined, taking into account dilution and losses.
- (2) We own 79.9% of Southern Urals Nickel Plant mines. Reserves are presented for the mines on an assumed 100% ownership basis.
- (3) In estimating our reserves we use average market or contract prices and currency conversions are carried out at average official exchange rates of the Central Bank of Russia.
- (4) Volumes are reported on a dry basis.
- (5) Metallurgical recovery is projected to be 73.8%.

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As of December 31, 2008, we had nickel ore deposits totaling 69.7 million tonnes at an average nickel grade of 0.9%. The table below summarizes nickel ore deposits.

<b>Nickel Ore Deposits<sup>(1)</sup></b>	<b>Tonnes<sup>(2)</sup> (In millions of tonnes)</b>	<b>Grade (% Ni)<sup>(3)</sup></b>
Buruktal	69.7	0.9%

(1) Includes adjustments for dilution and mine recovery, based on historical records.

(2) Volumes are reported on a dry basis.

(3) Metallurgical recovery is projected to be 73.8%.

The Buruktal mine is located approximately 230 kilometers east of the city of Orsk, in Orenburg region, northeast of the town of Svetly. The mine is situated just east of the southern tip of the Ural Mountains, the same geological region as the Sakhara mine.

The Sakhara mine is the most northern property and is 50 kilometers east of Magnitogorsk in the Chelyabinsk region and 370 kilometers north of Orsk, where Southern Urals Nickel Plant's process smelter is located.

Both the Buruktal and Sakhara mines have railway spurs connected to the Russian rail system, which is controlled by Russian Railways.

Through our acquisition of Oriel Resources in April 2008, we acquired a 100% interest in the Voskhod chrome project ( Voskhod ) and a 90% interest in the Shevchenko nickel project ( Shevchenko ), both located in northwestern Kazakhstan. In January 2009, we acquired the remaining 10% interest in Shevchenko, giving us a current 100% interest in both Voskhod and Shevchenko.

The subsoil license relating to the silicate nickel ore deposit at Shevchenko was issued by the government of Kazakhstan in 1997 for a period of 20 years. Shevchenko is an exploration stage mineral asset without reportable reserves. Currently, relevant engineering studies are being undertaken.

*Chrome ore*

The subsoil license relating to the chrome deposit at Voskhod was issued by the government of Kazakhstan in 2004 for a period of 25 years. According to our internal estimates, Voskhod has total proven and probable reserves of 18.7 million tonnes at an average grade of 42.2% Cr<sub>2</sub>O<sub>3</sub>, comprising 0.9 million tonnes of proven and 17.8 million tonnes of probable reserves. Voskhod commenced producing commercial volumes of chrome ore in December 2008. Chrome ore concentrate from Voskhod is used in the Tikhvin Ferroalloy Plant ( Tikhvin ) in Russia, which is another asset acquired in 2008 as part of Oriel Resources.

The Voskhod chrome project is situated in the Chrometau district of Aktyubinsk region, northwestern Kazakhstan. The site is accessed by road seven kilometers north-northeast from the nearby town of Chrometau, which lies on the highway from the regional center of Aktobe.

***Ferroalloy production facilities***

*Southern Urals Nickel Plant*

Southern Urals Nickel Plant is located in the city of Orsk, in Orenburg region. We acquired Southern Urals Nickel Plant in 2001.

The plant includes a sinter plant equipped with five sintering machines; a melting workshop equipped with eight blast furnaces and 14 thirty-tonne converters; and a roasting workshop equipped with two electric arc furnaces with a capacity of 12 megawatts each.

The plant can produce up to 17,500 tonnes per year of low-ferrous ferronickel in pure nickel equivalent.

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The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Southern Urals Nickel Plant's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Low-ferrous ferronickel production	16,158	92%	

Southern Urals Nickel Plant produced 16,158 tonnes of nickel in 2008.

*Bratsk Ferroalloy Plant*

Bratsk Ferroalloy Plant is the largest enterprise in Eastern Siberia producing high grade ferrosilicon. Ferrosilicon is used in the steel-making industry for manufacturing carbon and stainless steel deoxidizers of most kinds of steel grades or alloying elements for production of insulating, acid-proof and heatproof steel grades, or pig iron modifier, as well as reducing agents for production of nonferrous metals and alloys. Ferrosilicon is a primary raw material for alloyed steels produced by Chelyabinsk Metallurgical Plant. We acquired Bratsk Ferroalloy Plant in 2007.

The main production facilities of the plant include four ore-thermal ovens with a capacity of 25 megavolt-amperes.

The following table sets forth the capacity, the capacity utilization rate and the planned increase in capacity for Bratsk Ferroalloy Plant's principal production area.

<b>Production Areas</b>	<b>Capacity in 2008</b>	<b>Capacity Utilization Rate in 2008</b>	<b>Planned Increase (2009-2011)</b>
	<b>(In thousands of tonnes, except for percentages)</b>		
Ferrosilicon production	91,110	100%	113

Bratsk Ferroalloy Plant produced 91,110 tonnes of ferrosilicon in 2008.

*Tikhvin Ferroalloy Plant*

Tikhvin Ferroalloy Plant is designed to smelt chrome ore into high carbon ferrochrome for use predominantly in the stainless steel industry. The other raw materials used in the ferrochrome smelting process are metallurgical coke as a reducing agent and a quartzite flux. The plant is situated in the small town of Tikhvin, 200 kilometers southeast of St. Petersburg, Russia. It comprises four semi-closed submerged arc AC furnaces with a full production capacity of 22.5 megavolt-amperes each (with a combined annual capacity of 140,000 tonnes of high carbon ferrochrome) and four gas cleaning plants. Tikhvin Ferroalloy Plant commenced production in April 2007 using imported ore. Since April 1, 2009, the plant has moved to ferrochrome production using only concentrate from the Voskhod chrome processing plant. Four furnaces are used in production. In the fourth quarter of 2008 and in the first quarter of 2009, the furnaces operated at low capacity (60%) because of the low profitability of ferrochrome production using imported ore and

difficulties in marketing its output.

***Trade restrictions***

In February 2008, an antidumping duty in the amount of 17.8% was imposed on exports to the E.U. of ferrosilicon produced by our Bratsk Ferroalloy Plant for a period of five years.

**Power Business**

***Southern Kuzbass Power Plant***

Southern Kuzbass Power Plant is located in the city of Kaltan in the Kemerovo region, which is south of Russia's coal-rich Kuzbass district. It has a total installed capacity of 554 MW and installed heat capacity of 1,500 Gcal/h as of December 31, 2008. The electricity output of the plant for the year ended December 31, 2008 was 2.1 million kWh. The heat power generated by the plant for the year ended December 31, 2008 was 737,356 Gcal. We acquired Southern Kuzbass Power Plant in 2007.

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Southern Kuzbass Power Plant uses steam coal as fuel, which is supplied to it from local sources, including our Southern Kuzbass Coal Company. In 2008, it consumed 790,055 tonnes of steam coal from Southern Kuzbass Coal Company.

The generation facilities of Southern Kuzbass Power Plant are listed below.

<b>Generation Unit No.</b>	<b>Year of Manufacture</b>	<b>Month and Year of Commissioning at Southern Kuzbass Power Plant</b>	<b>Installed Capacity (MW)</b>	<b>Electricity Production in 2008 (million kWh)</b>
VK-50-2 LMZ	1950	April 1951	53	193,659
VK-50-2 LMZ	1950	November 1951	53	224,788
VK-50-2 LMZ	1950	August 1952	53	294,343
VK-50-2 LMZ	1952	February 1953	53	143,131
T-115-8,8 LMZ	1996	December 2003	113	390,104
T-88/106-90 LMZ	1953	July 1954	88	429,963
VK-50-2 LMZ	1954	December 1954	53	184,749
T-88/106-90 LMZ	1953	September 1956	88	265,305
Total Installed Capacity			554	
Total Electricity Production				2,126,042

The plant sells electricity and capacity on the wholesale market only, as well as heat energy directly to consumers. In Russia it is common for thermal power plants to produce and sell heat energy, sometimes in the form of industrial steam and sometimes in the form of hot water, for business and residential heating and household use, which is distributed in towns and cities by a network of hot water distribution pipes. Southern Kuzbass Power Plant's heat energy is distributed at regulated prices in the form of hot water in the city of Kaltan and in the city of Osinniki.

***Kuzbass Power Sales Company***

Kuzbass Power Sales Company is located in the Kemerovo region and is the largest power distributing company in Siberia. Its distributed power volume in 2008 amounted to 13.3 billion kWh. We acquired Kuzbass Power Sales Company in 2007. The addition of Kuzbass Power Sales Company, along with Southern Kuzbass Power Plant, allows us to improve the utilization of our existing power co-generation capabilities and provides a base for growth in the power industry.

Kuzbass Power Sales Company sells electricity on the retail market. The company sells electricity to the public, to social infrastructure companies, housing and public utilities and large industrial companies. Due to its area of operation, its primary industrial customers are in the mining and processing industries. It supplies electricity to end-consumers directly and also through four regional agents.

The company is appointed as guaranteeing supplier in the Kemerovo region. For a discussion of guaranteeing suppliers, see Regulatory Matters Russian Regulation Regulation of electricity market Sales of electricity Retail electricity market.

***Toplofikatsia Rousse***

Toplofikatsia Rousse is a power plant located on the bank of the Danube River in close proximity to the harbor of Rousse, Bulgaria. We acquired 49% of Toplofikatsia Rousse in December 2007. Currently, the plant generates 290 MW, which is below its installed capacity of 400 MW. Pursuant to our capital improvements program, we are upgrading the equipment at Toplofikatsia Rousse to fully utilize its installed capacity. The plant has a total heat capacity of 35 Gcal/h and uses steam coal as fuel, most of which is supplied to it from our coal mines in Russia. The plant has approximately 700 employees.

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### ***Mechel-Energo OOO***

Established in 2001, Mechel-Energo OOO is located in the city of Moscow. Mechel-Energo's core activity is generation and sale of electricity, capacity, and heat energy in the form of hot water and steam. In addition, the priority line in its activities is supplying our production facilities with energy. The company has separate structural units in the cities of Beloretsk, Vidnoye, Izhevsk, Mezhdurechensk, Chebarkul and Chelyabinsk.

Mechel-Energo supplies heat energy (in the form of hot water and steam) at regulated prices to its consumers, including residential consumers and commercial customers, of the cities of Vidnoye, Chelyabinsk, Chebarkul, Beloretsk, Mezhdurechensk and Myski.

Mechel-Energo has cogeneration facilities and operates using, mainly, blast furnace gas and coke oven gas, which is a byproduct of steelmaking, and natural gas, which we purchase from Gazprom.

Mechel-Energo's sales amounted to 4,162 billion kWh of electricity and 4,121 million Gcal of heat energy in 2008.

### **Capital Improvements Program**

We plan to spend approximately \$2.9 billion for our capital improvements program for the four-year period of 2009-2012. Our capital improvements program is primarily targeted at expanding the mining segment and increasing the efficiency of the steel segment. The split is approximately \$1.4 billion in mining, approximately \$1.2 billion in steel, approximately \$110.0 million in ferroalloys and approximately \$36.0 million in the power segment. Our ability to realize our capital improvements program is constrained by our ability to generate cash flow, obtain additional financing and refinance or restructure existing indebtedness.

We continually review our capital improvements program in light of our cash flow, liquidity position, results of operations and market conditions. In light of the above factors, we may adjust our capital improvements program. See Item 3. Key Information Risk Factors Risks Relating to Our Financial Condition and Financial Reporting Servicing and refinancing of our indebtedness may materially adversely affect our cash flow, Item 3. Key Information Risk Factors Risks Relating to Our Financial Condition and Financial Reporting We could be materially adversely affected if we do not comply with our loan agreements and Item 3. Key Information Risk Factors Risks Relating to Our Financial Condition and Financial Reporting We will require a significant amount of cash to fund our capital improvements program.

In the mining segment we expect to direct approximately \$1.6 billion to the development of the Elga coal deposit and construction of a rail branch line of approximately 315 kilometers in length in 2008-2011. Investments in Southern Kuzbass Coal Company will amount to \$188.0 million. In the iron ore business, we will invest approximately \$59.0 million in Korshunov Mining Plant. Projects aimed at the development of the Erunakovsk deposit and increasing coal production at the Olzherassk and Sibirginsk mines, as well as construction of a load-haul-dump system, have been suspended.

Steel segment projects are targeted at improving efficiency while maintaining existing output, and will be mainly focused on Chelyabinsk Metallurgical Plant and Izhstal. The main project, started in 2008, is the construction of a universal rail and structural steel mill aimed at increasing rolling capacity to 1.1 million tonnes and decreasing the proportion of lower-value semi-finished product sales by increasing the production of high quality rolled steel products and rails. Preliminary engineering works have been completed, an equipment delivery contract and construction contract have been signed and the project is planned to be completed in 2011.



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The following table sets out by segment and facility the major items of our capital expenditures currently in progress or expected to be commenced in 2009-2010.

		<b>Approximate Total Planned Expenditures<sup>(1)</sup> (In millions)</b>	<b>Year of Project Launch</b>	<b>Estimated Year of Completion</b>
<b>Mining Business</b>				
Maintenance expenditures	Maintaining current coal and iron ore mining and coal and iron ore concentrate production	\$ 293.2	2009	2012
<b><i>Yakutugol</i></b>				
Construction of a rail branch to the Elga coal deposit and the development of the Elga coal deposit	Providing access to deposit and the development of the deposit	\$ 1,644.8	2008	2011
<b>Steel Business</b>				
Maintenance expenditures	Maintaining current output capacity	\$ 182.5	2009	2012
<b><i>Chelyabinsk Metallurgical Plant</i></b>				
Construction of rolling facilities in blooming building	Introducing new types of rolled products for construction industry with a design capacity of 1.1 million tonnes per annum	\$ 700.4	2008	2011
<b><i>Izhstal</i></b>				
Modernization of arc-furnace melting facilities; renovation of arc-furnace shop No. 23	Increase of arc-furnace steel melting capacity to 480,000 tonnes per annum and steel quality improvements; decommissioning older open-hearth furnace	\$ 125.3	2007	2009
Reconstruction of mill No. 250	Increase in capacity to 300,000 tonnes per annum and increase of quality of rolled products	\$ 62.6	2007	2009
Infrastructure of arc-furnace shop No. 23 and mill No. 250		\$ 7.1	2007	2009
<b>Ferroalloys business</b>				
Maintenance expenditures	Maintaining current output capacity	\$ 59.1	2009	2012
<b>Transport division</b>				
Maintenance expenditures	Maintaining current output capacity	\$ 7.5	2009	2012
Technical modernization of Port Posiet	Increase of production capacity by 7.0 million tonnes per annum	\$ 71.3	2004	2010
<b>Power business</b>				
Maintenance expenditures		\$ 35.5	2009	2012

Maintaining current output  
capacity

- (1) We estimate that approximately \$709.0 million of the aforementioned planned expenditures for these projects have been made as of December 31, 2008. In 2008, we spent \$1.2 billion in total for capital expenditures.

**Research and Development**

We maintain research programs at the corporate level and at certain of our business units to carry out research and applied technology development activities. At the corporate level, we have a Division of Reconstruction and Development of Metallurgical Facilities at Mechel Management (12 employees), Division of Mining Production at Mechel Management (12 employees), Department of Hardware Production Development at Mechel Management

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(two employees), and a Department of Production and Technical Policy at Mechel Ferroalloys Management (seven employees).

In the course of our research and development we also contract with third-party consultants and Russian research institutions.

In addition to these activities performed at our corporate level, each of Chelyabinsk Metallurgical Plant, Beloretsk Metallurgical Plant, Southern Urals Nickel Plant, Izhstal, Urals Stampings Plant, Mechel Targoviste and Yakutugol have specialized research divisions with a total of 465 researchers involved in the improvement of existing technologies and products.

Our research and development expenses in the years ending December 31, 2008, 2007 and 2006 were not significant.

## **Insurance**

Most of our Russian production facilities have no comprehensive insurance coverage against the risks associated with the business in which we operate, other than insurance required under the Russian law, existing collective agreements, loan agreements or other undertakings. Our Russian facilities have various compulsory insurance policies: legal liability for pollution, compulsory motor vehicle insurance and other forms of insurance. Some of our facilities provide their workers with medical insurance and accident and health insurance in accordance with existing collective employment agreements. In addition, some of our Russian facilities have motor vehicle insurance, property insurance (real property and machinery insurance, goods), third party liability insurance and cargo.

Some of our international production facilities are not covered by comprehensive insurance typical for such operations in Western countries. However, they all have the compulsory insurance coverage required under the law of their respective jurisdictions: motor vehicle insurance, pollution legal liability insurance, employer liability and others. Furthermore, some of our international production facilities also carry insurance coverage for their property (real property and machinery insurance, goods), liability (third party liability, professional and product liability), cargo (including freight insurance), as well as medical insurance and accident and health insurance for their workers.

## **Regulatory Matters**

### **Russian Regulation**

We describe below certain regulatory matters that are applicable to our Russian operations.

### **Licensing of operations**

We are required to obtain numerous licenses, authorizations and permits from Russian governmental authorities for our operations. The Federal Law On Licensing of Certain Types of Activities, dated August 8, 2001, as amended, as well as other laws and regulations, set forth the activities subject to licensing and establish procedures for issuing licenses. In particular, some of our companies need to obtain licenses, authorizations and permits to carry out their activities, including, among other things:

the use of subsoil, which is described in more detail in Subsoil licensing below;

the use of water resources;

the discharge of pollutants into the environment;

the handling of hazardous waste;

storage and use of explosive, flammable and/or dangerous materials;

operation of industrial facilities featuring fire and explosion hazard (including mining and surveying activities);

construction;

fire control and security;

medical operations; and

transportation activities.

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These licenses and permits are usually issued for a period of five years and may be extended upon application by the licensee. Licenses for the use of natural resources may be issued for shorter or longer periods. Upon the expiration of a license, it may be extended upon application by the licensee, but usually subject to prior compliance with regulations.

Regulatory authorities maintain considerable discretion in the timing of issuing licenses and permits. The requirements imposed by these authorities may be costly, time-consuming and may result in delays in the commencement or continuation of exploration or production operations. Further, private individuals and the public at large possess rights to comment on and otherwise participate in the licensing process, including through challenges in the courts. For example, individuals and public organizations may make claims or applications to the Federal Agency for Subsoil Use regarding subsoil abuse, damage to the subsoil and general environmental issues. The Federal Agency for Subsoil Use is required by law to review such claims and applications and to respond to those who file them. The agency can initiate further investigation in the course of reviewing claims and applications, and such investigations can lead to suspension of the subsoil license if the legal grounds for such suspension are identified in the course of the investigation. Additionally, citizens may make claims in court against state authorities for failing to enforce environmental requirements (for example, if a breach by the licensee of its license terms caused damage to an individual's health, legal interests or rights), and pursuant to such a claim the court may order state authorities to suspend the subsoil license. Accordingly, the licenses we need may not be issued, or if issued, may not be issued in a timely fashion, or may impose requirements which restrict our ability to conduct our operations or to do so profitably.

As part of their obligations under licensing regulations and the terms of our licenses and permits, some of our companies must comply with numerous industrial standards, employ qualified personnel, maintain certain equipment and a system of quality controls, monitor operations, maintain and make appropriate filings and, upon request, submit specified information to the licensing authorities that control and inspect their activities.

### **Subsoil licensing**

In Russia, mining minerals requires a subsoil license from the Federal Agency for Subsoil Use with respect to an identified mineral deposit, as well as the right (through ownership, lease or other right) to use the land where such licensed mineral deposit is located. In addition, as discussed above, operating permits are required with respect to specific mining activities.

The primary law regulating subsoil licensing is the Federal Law On Subsoil, dated February 21, 1992, as amended (the Subsoil Law), which sets out the regime for granting licenses for the exploration and production of mineral resources. The Procedure for Subsoil Use Licensing, adopted by Resolution of the Supreme Soviet of the Russian Federation on July 15, 1992, as amended (the Licensing Regulation), also regulates the exploration and production of mineral resources. According to both the Subsoil Law and the Licensing Regulation, subsurface mineral resources are subject to the jurisdiction of the federal authorities.

Among different licenses required for mining minerals in Russia, the two major types of licenses are: (1) an exploration license, which is a non-exclusive license granting the right of geological exploration and assessment within the license area, and (2) a production license, which grants the licensee an exclusive right to produce minerals from the license area. In practice, many of the licenses are issued as combined licenses, which grant the right to explore, assess and produce minerals from the license area. A subsoil license defines the license area in terms of latitude, longitude and depth.

There are two major types of payments with respect to the extraction of minerals: (1) periodic payments for the use of subsoil under the Subsoil Law and (2) the minerals extraction tax under the Tax Code. Failure to make these payments could result in the suspension or termination of the subsoil license. The Subsoil Law-mandated payments are not

material to our mining segment's results of operations. The minerals extraction tax is calculated as a percentage of the value of minerals extracted. Currently the tax rates are 4% for coal, 4.8% for iron ore and 8% for nickel. In 2008, we incurred minerals extraction taxes in the amount of \$52.3 million, which is included in the statement of income and comprehensive income as production related overheads. See note 22 to our consolidated financial statements in Item 18. Financial Statements.

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The term of the license is set forth in the license. Prior to January 2000, exploration licenses could have a maximum term of five years, production licenses a maximum term of 20 years, and combined exploration, assessment and production licenses a maximum term of 25 years. After amendments to the Subsoil Law in January 2000 and in August 2004, exploration licenses still have a maximum term of five years; in the event that a prior license with respect to a particular field is terminated early (for example, when a license is withdrawn due to non-usage of the licensed subsoil), a production license may have a one year term until a new licensee is determined, but is generally granted to another user for the term of the expected operational life of the field based on a feasibility study; and combined exploration, assessment and production licenses can be issued for the term of the expected operational life of the field based on a feasibility study. These amendments did not affect the terms of licenses issued prior to January 2000, but permit licensees to apply for extensions of such licenses for the term of the expected operational life of the field in accordance with the amended Subsoil Law. The term of a subsoil license runs from the date the license is registered with the Russian Federal Agency for Subsoil Use.

### ***Issuance of licenses***

Subsoil licenses are issued by the Federal Agency for Subsoil Use. Most of the currently existing production licenses owned by companies derive from (1) pre-existing rights granted during the Soviet era and up to the enactment of the Subsoil Law to state-owned enterprises that were subsequently reorganized in the course of post-Soviet privatizations; or (2) tender or auction procedures held in the post-Soviet period. The Russian Civil Code, the Subsoil Law and the Licensing Regulation contain the major requirements relating to tenders and auctions. The Subsoil Law allows production licenses to be issued without a tender or auction procedure only in limited circumstances, such as instances when a mineral deposit is discovered by the holder of an exploration license at its own expense during the exploration phase.

### ***Extension of licenses***

The Subsoil Law permits a subsoil licensee to request an extension of a production license in order to complete the production from the subsoil plot covered by the license or the procedures necessary to vacate the land once the use of the subsoil is complete, provided the user complies with the terms and conditions of the license and the relevant regulations.

In order to extend a period of a subsoil license, a company must file an application with the federal authorities to amend the license.

Order of the Ministry of Natural Resources No. 439-R, dated October 31, 2002, recommends that the following issues be considered by the relevant governmental authorities when determining whether to approve an amendment (including an extension) of a license: (1) the grounds for the amendments, with specific information as to how the amendments may impact payments by the licensee to the federal and local budgets; (2) compliance of the licensee with the conditions of the license; and (3) the technical expertise and financial capabilities that would be required to implement the conditions of the amended license.

The factors that may, in practice, affect a company's ability to obtain the approval of license amendments (including extensions) include (1) its compliance with the license terms and conditions; (2) its management's experience and expertise relating to subsoil issues; and (3) the relationship of its management with federal and/or local governmental authorities, as well as local governments. For a description of additional factors that may affect Russian companies' ability to extend their licenses, see Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry Our business could be adversely affected if we fail to obtain or renew necessary licenses and permits or fail to comply with the terms of our licenses and permits. See also Item 3. Key Information Risk Factors Risks Relating to the Russian Federation and Other Countries Where We Operate Legal risks and uncertainties Deficiencies in the

legal framework relating to subsoil licensing subject our licenses to the risk of governmental challenges and, if our licenses are suspended or terminated, we may be unable to realize our reserves, which could materially adversely affect our business and results of operations and Item 3. Key Information Risk Factors Risks Relating to the Russian Federation and Other Countries Where We Operate Legal risks and uncertainties Weaknesses relating to the Russian legal system and legislation create an uncertain investment climate.

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### ***Maintenance and termination of licenses***

A license granted under the Subsoil Law is accompanied by a licensing agreement. The law provides that there be two parties to any subsoil licensing agreement: the relevant state authorities and the licensee. The licensing agreement sets out the terms and conditions for the use of the subsoil.

Under a licensing agreement, the licensee makes certain environmental, safety and production commitments. For example, the licensee makes a production commitment to bring the field into production by a certain date and to extract an agreed-upon volume of natural resources each year. The license agreement may also contain commitments with respect to social and economic development of the region. When the license expires, the licensee must return the land to a condition which is adequate for future use. Although most of the conditions set out in a license are based on mandatory rules contained in Russian law, certain provisions in a licensing agreement are left to the discretion of the licensing authorities and are often negotiated between the parties. However, commitments relating to safety and the environment are generally not negotiated. We expect that we will be able to meet the commitments set forth in our licensing agreements.

The fulfillment of a licensee's conditions is a major factor in the good standing of the license. If the subsoil licensee fails to fulfill the licensee's conditions, upon notice, the license may be terminated or the subsoil user's rights may be restricted by the licensing authorities. However, if a subsoil licensee cannot meet certain deadlines or achieve certain volumes of exploration work or production output as set forth in a license, it may apply to amend the relevant license conditions, though such amendments may be denied.

The Subsoil Law and other Russian legislation contain extensive provisions for license termination. A licensee can be fined or the license can be suspended or terminated for repeated breaches of the law, upon the occurrence of a direct threat to the lives or health of people working or residing in the local area, or upon the occurrence of certain emergency situations. A license may also be terminated for violations of material license terms. Although the Subsoil Law does not specify which terms are material, failure to pay subsoil taxes and failure to commence operations in a timely manner have been common grounds for limitation or termination of licenses. Consistent underproduction and failure to meet obligations to finance a project would also likely constitute violations of material license terms. In addition, certain licenses provide that the violation by a subsoil licensee of any of its obligations may constitute grounds for terminating the license.

If the licensee does not agree with a decision of the licensing authorities, including a decision relating to a license termination or the refusal to re-issue an existing license, the licensee may appeal the decision through administrative or judicial proceedings. In certain cases prior to termination the licensee has the right to attempt to cure the violation within three months of its receipt of notice of the violation. If the issue has been resolved within such a three month period, no termination or other action may be taken.

### **Land use rights**

Russian legislation prohibits the carrying out of any commercial activity, including mineral extraction, on a land plot without appropriate land use rights. Land use rights are needed and obtained for only the portions of the license area actually being used, including the plot being mined, access areas and areas where other mining-related activity is occurring.

Under the Land Code, companies generally have one of the following rights with regard to land in the Russian Federation: (1) ownership; (2) right of perpetual use or (3) lease.

A majority of land plots in the Russian Federation are owned by federal, regional or municipal authorities which, through public auctions or tenders or through private negotiations, can sell, lease or grant other use rights to the land to third parties.

Companies may also have a right of perpetual use of land that was obtained prior to the enactment of the Land Code; however, the Federal Law On Introduction of the Land Code, dated October 25, 2001, with certain exceptions, requires companies using land pursuant to rights of perpetual use by January 1, 2010 either to purchase the land from, or to enter into a lease agreement relating to the land with, the relevant federal, regional or municipal authority acting as owner of the land. See Item 3. Key Information Risk Factors Risks Relating to Our

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**Business and Industry** The potential implementation by the Russian government of a law requiring Russian companies to purchase or lease the land on which they operate may have a material adverse effect on our financial condition.

Our mining subsidiaries generally have a right of perpetual use of their plots or have entered into long-term lease agreements. Under Russian law a lessee generally has a priority right to enter into a new land lease agreement with a lessor upon the expiration of a land lease. In order to renew a land lease agreement, the lessee must apply to the lessor (usually state or municipal authorities) for a renewal prior to the expiration of the agreement. Any land lease agreement for a term of one year or more must be registered with the relevant state authorities.

We generally own, lease or have a right of perpetual use of the land on which our steel production facilities are located.

## **Environmental legislation**

We are subject to laws, regulations and other legal requirements relating to the protection of the environment, including those governing the discharge of substances into the air and water, the formation, distribution and disposal of hazardous substances and waste, the cleanup of contaminated sites, flora and fauna protection and wildlife protection. Issues of environmental protection in Russia are regulated primarily by the Federal Law On Environmental Protection, dated January 10, 2002, as amended (the Environmental Protection Law ), as well as by a number of other federal, regional and local legal acts.

At a Russian government press conference on June 3, 2008, it was announced that a new draft law aimed at improving environmental regulation is being prepared and would be submitted to the State Duma by October 1, 2008. The law is not effective by now. The Russian government intends to improve the state environmental monitoring system, to develop a better allocation of functions among state environmental agencies on the federal and regional levels, as well as to increase fines for companies noncompliance with environmental laws and regulations. In addition, a proposal was outlined to create a comprehensive system regulating the levels of permissible environmental impact and a differentiated system of water, air and soil quality standards, as well as to improve the technical regulation system to raise the energy efficiency of industry. No proposals or drafts have been made publicly available. See Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry More stringent environmental laws and regulations or more stringent enforcement of existing environmental laws and regulations in the jurisdictions where we operate may have a significant negative effect on our operating results.

### ***Pay-to-pollute***

The Environmental Protection Law and other Russian environmental protection legislation establish a pay-to-pollute regime administered by federal and local authorities. Pay-to-pollute (or payments for environmental pollution) is a form of mandatory reimbursement to the Russian government of damage caused to the environment.

The Russian government has established standards relating to the permissible impact on the environment and, in particular, limits for emissions and disposal of substances, waste disposal and resource extraction. A company may obtain temporary approval for exceeding these statutory limits from Rostekhnadzor, depending on the type and scale of environmental impact. As a primary condition to such approval, a plan for the reduction of the emissions or disposals to the standard legal maximum limits must be developed by the company and cleared with Rostekhnadzor. The emission reduction plan is generally required to be implemented within a specific period. If, by the end of that period, a company's discharges of pollutants are still in excess of statutory limits, a new emission reduction plan must be submitted to Rostekhnadzor for approval.

Fees for discharge per tonne of each contaminant into air and water and fees for waste disposal are established by governmental authorities. These fees are assessed on a sliding scale for both the statutory or individually approved limits on emissions and effluents and for pollution in excess of these limits: the lowest fees are imposed for pollution within the statutory limits, intermediate fees are imposed for pollution within the individually approved temporary limits, and the highest fees are imposed for pollution exceeding such limits (above-limit fees).

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Payments of above-limit fees for violation of environmental legislation do not relieve a company from its responsibility to take environmental protection measures and undertake restoration and clean-up activities. In 2008, we incurred above-limit fees and penalties in the amount of about \$3.9 million.

### ***Ecological expert examination***

According to the Federal Law On Ecological Expert Examination, dated November 23, 1995, as amended (the Ecology Law ), ecological expert examination is a process of verifying compliance of business or operational documentation with ecological standards and technical regulations established pursuant to the Ecology Law for the purpose of preventing a negative environmental impact of such business or operations. The Ecology Law provides for the main principles for conducting ecological expert examination and for the type of documentation which is subject to such inspection.

In relation to our operating companies, all documentation underlying the issuance of some of our licenses, in particular licenses issued by federal authorities to conduct activities related to collection, usage, sterilization, transportation and disposal of dangerous wastes, are subject to ecological expert examination.

Examination of documentation related to capital construction is regulated under the Urban Development Code. The Urban Development Code provides for governmental inspection to verify compliance of project documentation with relevant technical regulations, including sanitary-epidemiological and ecological regulations, requirements on protection of objects of cultural heritage, as well as fire, industrial, nuclear, radiation and other kinds of safety requirements, and also compliance of results of engineering surveys with relevant technical regulations.

### ***Environmental enforcement authorities***

Currently state environmental regulation is administered by several federal services and agencies and their regional subdivisions, in particular, the Federal Service for the Supervision of the Use of Natural Resources, Rostekhnadzor, the Federal Service for Hydrometrology and Environmental Monitoring, the Federal Agency for Subsoil Use, the Federal Agency for Forestry and the Federal Agency for Water Resources. Included in these agencies sphere of responsibility are environmental preservation and control, enforcement and observance of environmental legislation, drafting and approving regulations and filing court claims to recover environmental damages. The statute of limitations for such claims is 20 years.

The Russian federal government and the Ministry of Natural Resources and Ecology are responsible for coordinating the work of the federal services and agencies engaged in state environmental regulation.

The structure of environmental enforcement authorities described above was established in 2004. This structure was subjected to certain changes in 2008. In particular, the Ministry of Natural Resources was transformed into the Ministry of Natural Resources and Ecology and Rostekhnadzor is now under its supervision. For these reasons, the authorities are currently redistributed among federal bodies, on one hand, and among federal central and regional executive bodies, on the other hand.

### ***Environmental liability***

If the operations of a company violate environmental requirements or cause harm to the environment or any individual or legal entity, a court action may be brought to limit or ban these operations and require the company to remedy the effects of the violation. Any company or employees that fail to comply with environmental regulations may be subject to administrative and/or civil liability, and individuals may be held criminally liable. Courts may also impose clean-up obligations on violators in lieu of or in addition to imposing fines or other penalties to compensate for damages.

Subsoil licenses generally require certain environmental commitments. Although these commitments can be substantial, the penalties for failing to comply and the reclamation requirements are generally low; however, failure to comply with reclamation requirements can result in a suspension of mining operations.

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### ***Reclamation***

We conduct our reclamation activities for land damaged by production in accordance with the Basic Regulation on Land Reclamation, Removal, Preservation, and Rational Use of the Fertile Soil Layer, approved by Order No. 525/67 of December 22, 1995, of the Ministry of Natural Resources. In general, our reclamation activities involve both a technical stage and a biological stage. In the first stage, we backfill the pits, grade and terrace mound slopes, level the surface of the mounds, and add clay rock on top for greater adaptability of young plants. In the biological stage, we plant conifers (pine, larch, cedar) on horizontal and gently sloping surfaces and shrubs and bushes to reinforce inclines. Russian environmental regulations do not require mines to achieve the approximate original contour of the property as is required, for example, in the United States.

### ***Environmental protection programs***

We have been developing and implementing environmental protection programs at all of our mining, steel, ferroalloys, power and logistics subsidiaries. Such programs include measures to enforce our adherence to the requirements and limits imposed on air and water pollution, as well as allocation of industrial waste, introduction of environmentally friendly industrial technologies, the construction of purification and filtering facilities, the repair and reconstruction of industrial water supply systems, the installation of metering systems, reforestation and the recycling of water and industrial waste.

### ***Kyoto Protocol***

In December 1997, in Kyoto, Japan, the signatories to the United Nations Convention on Climate Change established individual, legally binding targets to limit or reduce greenhouse gas emissions by developed nations. This international agreement, known as the Kyoto Protocol, came into force on February 16, 2005. As of November 2007, 175 states (including Russia) and regional economic integration organizations (such as the E.U.) had ratified the Kyoto Protocol. We do not currently anticipate that the implementation of the Kyoto Protocol will have a material impact on our business beyond our plants in Bulgaria and Romania. All E.U. countries, including Bulgaria and Romania, are accepting national plans for allocation of greenhouse gas emission quotas starting from 2008. Toplofikatsia Rousse, located in Bulgaria, and our three Romanian steel plants are also obtaining greenhouse gas emission quotas for 2008-2012 period. According to our production program, both surpluses within quota and quota overruns may occur. Quota overruns will result in a requirement to acquire emission reduction units under the European Union Greenhouse Gas Emission Trading Scheme.

### ***Health and safety***

Due to the nature of our business, much of our activity is conducted at industrial sites by large numbers of workers, and workplace safety issues are of significant importance to the operation of these sites.

The principal law regulating industrial safety is the Federal Law On Industrial Safety of Dangerous Industrial Facilities, dated July 21, 1997, as amended (the Safety Law). The Safety Law applies, in particular, to industrial facilities and sites where certain activities are conducted, including sites where lifting machines are used, where alloys of ferrous and non-ferrous metals are produced, where hazardous substances are stored and used (including allowed concentrations) and where certain types of mining is done.

Our employees are covered by medical insurance purchased by us. Our employees have regular medical examinations and if necessary are offered preventative treatments in sanatoriums and preventative medicine facilities. Our employees who work in mines and other facilities with potentially hazardous working conditions have access to special food, and we provide hot meals to our employees during working hours. Our industrial production staff

members are provided with special protective clothing and safety equipment and our facilities are equipped with emergency stations.

There are also regulations that address safety rules for coal mines, the production and processing of ore, the blast-furnace industry, steel smelting, alloy production and nickel production. Additional safety rules also apply to certain industries, including metallurgical and coke chemical enterprises, and the foundry industry.

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Any construction, reconstruction, liquidation or other activities in relation to regulated industrial sites is subject to a state industrial safety review. Any deviation from project documentation in the process of construction, reconstruction and liquidation of industrial sites is prohibited unless reviewed by a licensed expert and approved by Rostekhnadzor.

Companies that operate such industrial facilities and sites have a wide range of obligations under the Safety Law and the Labor Code of Russia of December 30, 2001, effective February 1, 2002, as amended (the Labor Code ). In particular, they must limit access to such sites to qualified specialists, maintain industrial safety controls and carry insurance for third-party liability for injuries caused in the course of operating industrial sites. The Safety Law also requires these companies to enter into contracts with professional wrecking companies or create their own wrecking services in certain cases, conduct personnel training programs, create systems to cope with and inform the Rostekhnadzor of accidents and maintain these systems in good working order.

In certain cases, companies operating industrial sites must also prepare declarations of industrial safety which summarize the risks associated with operating a particular industrial site and measures the company has taken and will take to mitigate such risks and use the site in accordance with applicable industrial safety requirements. Such declarations must be adopted by the chief executive officer of the company, who is personally responsible for the completeness and accuracy of the data contained therein. The industrial safety declaration, as well as a state industrial safety review, are required for the issuance of a license permitting the operation of a dangerous industrial facility.

Rostekhnadzor has broad authority in the field of control and management of industrial safety. In case of an accident, a special commission led by a representative of Rostekhnadzor conducts a technical investigation of the cause. The company operating the hazardous industrial facility where the accident took place bears all costs of an investigation. Rostekhnadzor officials have the right to access industrial sites and may inspect documents to ensure a company's compliance with safety rules. Rostekhnadzor may suspend or terminate operations of companies and/or impose administrative liability on officers of such companies.

Any company or individual violating industrial safety rules may incur administrative and/or civil liability, and individuals may also incur criminal liability. A company that violates safety rules in a way that negatively impacts the health of an individual may also be obligated to compensate the individual for lost earnings, as well as health-related damages.

## **Antimonopoly regulation**

The Federal Law On Protection of Competition, dated July 26, 2006, as amended (the Competition Law ), provides for a mandatory pre-approval by the Russian Federal Antimonopoly Service (the FAS ) of the following actions:

an acquisition by a person (or its group) of more than 25% of the voting shares of a joint-stock company (or one-third of the interests in a limited liability company), except upon incorporation, and the subsequent increase of these stakes to more than 50% of the total number of shares and more than 75% of the voting shares (one-half and two-thirds of the interests in a limited liability company), or acquisition by a person (or its group) of ownership or rights of use with respect to the core production assets and/or intangible assets of an entity if the balance sheet value of such assets exceeds 20% of the total balance sheet value of the core production and intangible assets of such entity, or obtaining rights to determine the conditions of business activity of an entity or to exercise the powers of its executive body by a person (or its group), if, in any of the above cases, the aggregate asset value of an acquirer (or its group) together with a target (or its group) exceeds RUR 3 billion and at the same time the total asset value of the target (or its group) exceeds RUR 150 million, or the total annual revenues of such acquirer (or its group) and the target (or its group) for the preceding calendar year exceed RUR 6 billion and at the same time the total asset value of the target (or its group) exceeds RUR 150 million, or an acquirer, and/or a target, or any entity within the acquirer's group or a target's group are

included in the Register of Entities Having a Market Share in Excess of 35% on a Particular Commodity Market (the Monopoly Register );

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mergers and consolidations of entities, if their aggregate asset value (the aggregate asset value of the groups of persons to which they belong) exceeds RUR 3 billion, or total annual revenues of such entities (or groups of persons to which they belong) for the preceding calendar year exceed RUR 6 billion, or if one of these entities is included in the Monopoly Register; and

foundation of an business entity, if its charter capital is paid by the shares (or limited liability company interests) and/or the assets of another business entity and the newly founded business entity acquires rights in respect of such shares (or limited liability company interests) and/or assets as specified above, provided that the aggregate asset value of the founders (or group of persons to which they belong) and the business entities (or groups of persons to which they belong) which shares (or limited liability company interests) and/or assets are contributed to the charter capital of the newly founded business entity exceeds RUR 3 billion, or total annual revenues of the founders (or group of persons to which they belong) and the business entities (or groups of persons to which they belong) which shares (or limited liability company interests) and/or assets are contributed to the charter capital of the newly founded business entity for the preceding calendar year exceed RUR 6 billion, or if an business entity whose shares (or limited liability company interests) and/or assets are contributed to the charter capital of the newly founded business entity is included in the Monopoly Register.

The above requirements for a mandatory pre-approval by FAS will not apply if the transactions are performed by members of the same group, if the information about such a group of persons was disclosed to the antimonopoly authority and there were no changes within 30 days prior to the date of the transaction within a group of persons. In this case, FAS must be notified of the transactions subsequently in accordance with Russian anti-monopoly legislation.

The Competition Law provides for a mandatory post-transactional notification (within 45 days of the closing) to FAS in connection with actions specified above if the aggregate asset value or total annual revenues of an acquirer (or its group) and a target (or its group) for the preceding calendar year exceed RUR 200 million and at the same time: (1) the total asset value of the target (or its group) exceeds RUR 30 million; or (2) an acquirer and/or a target, or any entity within the acquirer's group or a target's group are included in the Monopoly Register and if the aggregate asset value or total annual revenues of the business entities being merged or consolidated for the preceding calendar year exceed RUR 200 million.

A transaction entered into in violation of the above requirements may be invalidated by a court decision pursuant to a claim brought by FAS in case if this transaction leads to the limitation of competition. The FAS may also issue binding orders to companies that have violated the applicable antimonopoly requirements and to bring court claims seeking liquidation, split-up or spin-off of business entities if a violation of antimonopoly laws was committed in the establishment of such business entities.

## **The Strategic Industries Law**

On April 29, 2008, the Strategic Industries Law was adopted in Russia. It regulates foreign investments in companies with strategic importance for the national defense and security of the Russian Federation ( Strategic Companies ). The Strategic Industries Law provides an exhaustive list of strategic activities, engagement in which makes a company subject to restrictions. Among others, the list of such activities includes exploration and/or production of natural resources on subsoil plots with federal importance. Subsoil plots with federal importance include plots with deposits of uranium, diamonds, high-purity quartz ore, nickel, cobalt, niobium, lithium, beryllium, tantalum, yttrium-group rare-earth metals and platinoid metals. They also include deposits of oil, gas, vein gold and copper which are above certain size limits specified in the Subsoil Law, as well as subsoil plots of the internal sea, territorial sea and continental shelf; and subsoil plots, the use of which requires the use of land plots included in the category of national

defense and security land. The List of subsoil plots of federal importance was officially published in a printed publication determined by the Government *Rossiyskaya Gazeta* on March 5, 2009. Services rendered by business entities included into the register of natural monopolies pursuant to the Federal Law On Natural Monopolies, dated August 17, 1995, as amended, with certain exceptions, are also considered to constitute strategic activity. Furthermore, the activity of a business entity which is deemed to occupy a dominant position in the production and sale of metals and alloys with special features which are used in production of

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weapons and military equipment is also deemed to be strategic activity. The production and distribution of industrial explosives as well as the use of sources of radioactivity are also deemed to be activities of strategic importance for national defense and homeland security.

Investments resulting in a foreign investor or a group of entities receiving control over a Strategic Company require prior approval from state authorities. The procedure for issuing such consent will involve a special governmental commission on control of foreign investments (the Governmental Commission), which was established by a government resolution dated July 6, 2008 as the body responsible for granting such consents, and the FAS, which is authorized to process applications for consent from foreign investors. Control for these purposes means an ability to determine, directly or indirectly, decisions taken by a Strategic Company, whether through voting at the general shareholders (or limited liability company interest-holders) meeting of the Strategic Company, participating in the board of directors or management bodies of the Strategic Company, or acting as the external management organization of the Strategic Company or otherwise. Thus, generally, control will be deemed to exist if any foreign investor or a group of entities acquires more than 50% of the shares (or limited liability interests) of a Strategic Company, or if by virtue of a contract or ownership of securities with voting rights it is able to appoint more than 50% of the members of the board of directors or of the management board of a Strategic Company. However, there are special provisions for Strategic Companies involved in the exploration or production of natural resources on plots of federal importance (Subsoil Strategic Companies): a foreign investor or group of entities is considered to have control over a Subsoil Strategic Company when such foreign investor or group of entities holds directly or indirectly 10% or more of the voting shares of the Subsoil Strategic Company or holds the right to appoint its sole executive officer and/or 10% or more of its management board or has the unconditional right to elect 10% or more of its board of directors.

Furthermore, in case a foreign investor or group of entities which is a holder of securities of a Strategic Company, Subsoil Strategic Company or other entity which exercises control over these companies becomes a direct or indirect holder of voting shares in amount which is considered to give them direct or indirect control over these companies in accordance with the Strategic Industries Law due to a change in allocation of voting shares pursuant to the procedures provided by Russian law (e.g., as a result of a buy-back by the relevant company of its shares, conversion of preferred shares into common shares, holders of preferred shares becoming entitled to vote at a general shareholders meeting in the events provided under Russian law), such shareholders will have to apply for state approval of their control within three months after they received such control. If the Governmental Commission refuses to grant the approval the shareholders shall sell the relevant part of their respective shares or participatory interest, and if they do not comply with this requirement a Russian court can deprive such foreign investor or group of entities of its voting rights in such Strategic Company upon claim of the competent authority. In such case, its shares are not counted for the purposes of establishing quorum and voting at the general shareholders meeting of the Strategic Company.

If a foreign investor or group of entities obtains control over a Strategic Company in violation of the Strategic Industries Law, the relevant transaction is void, and in certain cases a Russian court can deprive such foreign investor or group of entities of its voting rights in such Strategic Company upon claim of the competent authority. In addition, resolutions of the general shareholders meetings or other management bodies of a Strategic Company adopted after a foreign investor or group of entities obtained control over the Strategic Company in violation of the Strategic Industries Law, as well as transactions entered into by the Strategic Company after obtaining such control, may be held invalid in court upon claim of the competent authority. See Item 3. Key Information Risk Factors Risks Relating to the Russian Federation and Other Countries Where We Operate Legal risks and uncertainties Expansion of limitations on foreign investment in strategic sectors could affect our ability to attract and/or retain foreign investments.

***Standardization***

The Federal Law On Technical Regulation, dated December 27, 2002, as amended (the Technical Regulation Law ), introduced new rules relating to the development, enactment, application and enforcement of obligatory technical requirements and the development of voluntary standards relating to manufacturing processes, operations, storage, transportation, selling and utilization, as well as provisions on certification, accreditation of certification agencies and test laboratories, state supervision over compliance with the

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requirements of technical regulations, penalties for violations of technical regulations, product withdrawals and other related issues. The Technical Regulation Law supersedes the Laws of the Russian Federation On Certification of Goods and Services dated June 10, 1993 and On Standardization dated June 10, 1993 and will be followed by the revision of existing legislation and technical rules falling within the scope of its regulation. The Technical Regulation Law provides for a seven year (from 2003 through 2009) transition period, during which Russia will carry out such revision of existing legislation and technical rules. During the development of this new system, Russia's existing certification system will generally remain in effect. Currently, Rostekhnadzor is responsible for developing and enacting new technical rules relating to the industrial safety of mining and production operations that relate to our group's operations.

## **Employment and labor**

Labor matters in Russia are primarily governed by the Labor Code. In addition to this core legislation, relationships between employers and employees are regulated by federal laws, such as the Law On Employment in the Russian Federation, dated April 19, 1991, as amended, and the Federal Law On Compulsory Social Insurance Against Industrial Accidents and Occupational Diseases, dated July 24, 1998, as amended; legal acts of executive authorities; and local government acts related to labor issues.

### ***Employment contracts***

As a general rule, employment contracts for an indefinite term are entered into with all employees. Russian labor legislation expressly limits the possibility of entering into fixed-term employment contracts, including contracts with senior management. However, an employment contract may be entered into for a fixed term of up to five years in certain cases where labor relations may not be established for an indefinite term due to the nature of the duties or the conditions of the performance of such duties, as well as in other cases expressly identified by the Labor Code or other federal law. In some cases it is also possible to enter into an employment contract for the employee to perform specified tasks. All terms and conditions of employment contracts are regulated by the Labor Code.

Under Russian law, employment may be terminated by mutual agreement between employer and employee, at the end of the term of a fixed-term employment contract or on the grounds set out in the Labor Code as described below. An employee has the right to terminate his or her employment contract with a minimum of two weeks' notice (or one month's notice for a company's chief executive officer), unless the employment contract is terminated before the notice period ends by mutual agreement between employer and employee.

An employer may terminate an employment contract only on the basis of the specific grounds enumerated in the Labor Code, including but not limited to:

liquidation of the enterprise or downsizing of staff;

failure of the employee to comply with the position's requirements due to incompetence, as confirmed by the results of an attestation;

repeated failure of the employee to fulfill his or her work duties without valid reason, provided that the employee has been disciplined previously;

entering the workplace under the influence of alcohol, narcotics or other intoxicating substances;

a single gross breach by an employee of his or her work duties, including truancy;

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disclosure of state secrets or other confidential information, which an employee has come to know during fulfillment of his professional duties;

embezzlement, willful damage or destruction of assets, and misappropriation as confirmed by a court decision or a decision by another competent government authority;

failure to comply with safety requirements in the workplace if such failure to comply caused injuries, casualties or catastrophe;

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provision by the employee of false documents upon entry into the employment contract; and

in the case of a chief executive officer or his or her deputy, a single gross breach of employment duties.

An employee dismissed from an enterprise due to downsizing or liquidation is entitled to receive compensation and salary payments for a certain period of time, depending on the circumstances.

The Labor Code also provides protections for specified categories of employees. For example, except in cases of liquidation of an enterprise and other events specified in the Labor Code, an employer cannot dismiss minors, pregnant women, mothers with a child under the age of three, single mothers with a child under the age of 14 or other persons caring for a child under the age of 14 without a mother.

Any termination by an employer that is inconsistent with the Labor Code requirements may be invalidated by a court, and the employee may be reinstated. Lawsuits resulting in the reinstatement of illegally dismissed employees and the payment of damages for wrongful dismissal are increasingly frequent, and Russian courts tend to support employees rights in most cases. Where an employee is reinstated by a court, the employer must compensate the employee for unpaid salary for the period between the wrongful termination and reinstatement, as well as for mental distress.

### ***Work time***

The Labor Code generally sets the regular working week at 40 hours. Any time worked beyond 40 hours per week, as well as work on public holidays and weekends, must be compensated at a higher rate.

For employees working in hazardous or harmful conditions, the regular working week is decreased by four hours in accordance with government regulations. Some of our employees working on steel, mining, and power production entities qualify for this reduced working week.

Annual paid vacation leave under the law is 28 calendar days. Our employees who work in mines and pits or work in harmful conditions may be entitled to additional paid vacation ranging from seven to 42 working days.

The retirement age in the Russian Federation is 60 years for males and 55 years for females. However, employees who work in underground and open pit mines or do other work in potentially harmful conditions have the right to retire at an earlier age. The rules defining such early retirement ages are established by the Federal Law On Labor Pensions in the Russian Federation, dated December 17, 2001, as amended.

### ***Salary***

The minimum monthly salary in Russia, as established by federal law, was RUR 2,300 beginning September 1, 2007 and was increased to RUR 4,330 beginning January 1, 2009. Although the law requires that the minimum wage be at or above a minimum subsistence level, the current minimum wage is generally considered to be less than a minimum subsistence level.

### ***Strikes***

The Labor Code defines a strike as the temporary and voluntary refusal of workers to fulfill their work duties with the intention of settling a collective labor dispute. Russian legislation contains several requirements for legal strikes. Participation in a legal strike may not be considered by an employer as grounds for terminating an employment contract, although employers are generally not required to pay wages to striking employees for the duration of the

strike. Participation in an illegal strike may be adequate grounds for termination of employment.

***Trade unions***

Although Russian labor regulations have decreased the authority of trade unions compared with the past, they retain influence over employees and, as such, may affect the operations of large industrial companies in Russia, such as Mechel. In this regard, our management routinely interacts with trade unions in order to ensure the appropriate treatment of our employees and the stability of our business.

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The activities of trade unions are generally governed by the Federal Law On Trade Unions, Their Rights and Guarantees of Their Activity, dated January 12, 1996, as amended (the Trade Union Law ). Other applicable legal acts include the Labor Code, which provides for more detailed regulations relating to activities of trade unions.

The Trade Union Law defines a trade union as a voluntary union of individuals with common professional and other interests that is incorporated for the purposes of representing and protecting the rights and interests of its members. National trade union associations, which coordinate activities of trade unions throughout Russia, are also permitted.

As part of their activities, trade unions may:

- negotiate collective contracts and agreements such as those between the trade unions and employers, federal, regional and local governmental authorities and other entities;

- monitor compliance with labor laws, collective contracts and other agreements;

- access work sites and offices, and request information relating to labor issues from the management of companies and state and municipal authorities;

- represent their members and other employees in individual and collective labor disputes with management;

- organize and participate in strikes; and

- monitor redundancy of employees and seek action by municipal authorities to delay or suspend mass layoffs.

Russian laws require that companies cooperate with trade unions and do not interfere with their activities. Trade unions and their officers enjoy certain guarantees as well, such as:

- legal restrictions as to rendering redundant employees elected or appointed to the management of trade unions;

- protection from disciplinary punishment or dismissal on the initiative of the employer without prior consent of the management of the trade union and, in certain circumstances, the consent of the relevant trade union association;

- retention of job positions for those employees who stop working due to their election to the management of trade unions;

- protection from dismissal for employees who previously served in the management of a trade union for two years after the termination of the office term, except when a company is liquidated or the employer is otherwise entitled to dismiss the employee; and

- provision of the necessary equipment, premises and vehicles by the employer for use by the trade union free of charge, if provided for by a collective bargaining contract or other agreement.

If a trade union discovers any violation of work condition requirements, notification is sent to the employer with a request to cure the violation and to suspend work if there is an immediate threat to the lives or health of employees. The trade union may also apply to state authorities and labor inspectors and prosecutors to ensure that an employer does not violate Russian labor laws. Trade unions may also initiate collective labor disputes, which may lead to strikes.

To initiate a collective labor dispute, trade unions present their demands to the employer. The employer is then obliged to consider the demands and notify the trade union of its decision. If the dispute remains unresolved, a reconciliation commission attempts to end the dispute. If this proves unsuccessful, collective labor disputes are generally referred to mediation or labor arbitration. Although the Trade Union Law provides that those who violate the rights and guarantees provided to trade unions and their officers may be subject to disciplinary, administrative and criminal liability, no specific consequences for such violations are set out in Russian statute.

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### **Regulation of electricity market**

#### ***Industry background***

The Russian utilities sector landscape has undergone dramatic change within the past several years, since the introduction of electricity industry reform under Government Resolution On Restructuring of Electricity Industry of the Russian Federation No. 526 dated July 11, 2001 ( Resolution No. 526 ). Currently liquidated monopoly RAO Unified Energy System of Russia OAO (the UES ), was a diversified utilities holding company, separated in accordance with the spheres of business: electricity and heat generation, transmission (high voltage trunk grid), distribution (medium- and low-voltage infrastructure) and supply (sale of electricity to customers).

The electricity generation sector is now principally comprised of six thermal wholesale generating companies (called OGKs based on the Russian acronym for Wholesale Generating Company), one HydroOGK, 14 territorial generating companies ( TGKs ), RAO Eastern Energy Systems OAO, various nuclear generation complexes (owned and/or operated by the Rosenergoatom Federal State Unitary Enterprise), as well as a number of independent diversified electricity producers (Irkutskenergo, Bashkirenergo, Tatenergo, Novosibirskenergo).

#### ***Sales of electricity***

The Russian electricity market consists of wholesale and retail electricity and capacity markets. The wholesale market encompasses European territory of the Russian Federation and Siberia. The market provides a framework for large-scale, often interregional, energy trades. The retail electricity and capacity markets operate within specific Russian regional territories and provide a framework for mid-scale and end-consumer energy trades. These markets are regulated by the respective Regional Energy Committees (the RECs ).

#### ***The wholesale electricity market***

The wholesale market is a system of contractual relationships between all of its participants linked together by the process of production, transmission, distribution, purchase and sale and consumption of electricity within unified energy system. Unified energy system encompasses six regional unified energy systems, which are the following: North-West, Central, Urals, Mid-Volga, South and Siberia.

The wholesale market participants mainly include:

producers of electricity and capacity: generating companies (OGKs, TGKs, various other generators);

electricity supply companies (energy traders) which have purchased electricity and capacity for further resale on wholesale and retail markets; and

purchasers of electricity and capacity: major power consumers and generating companies which at certain points in time may elect to purchase electricity to fulfill their supply obligations instead of generating their own.

The infrastructure of the wholesale market is operated by the Non-commercial Partnership Market Council and the Trade System Administrator OAO (the TSA ) which organize the trading and calculate supply payments; a system operator established in the form of an open joint-stock company (the System Operator ) by the former UES; the Federal Grid Company (the FGK ), which owns and runs the federal transmission network of the electric grids; OAO Holding MRSK, which owns and runs region transmission networks of the electric grids; and the Financial Settlement Center ZAO, which is a clearance and settlement organization for the wholesale electricity and capacity market.

According to publicly available information, the restructuring of UES was completed in June 2008.

A company that intends to participate in the sale or purchase of electricity on the wholesale market must register with the TSA as a participant of the wholesale market. For that reason the company must meet the following requirements:

a supplier of electricity must own facilities with a total capacity of at least 25 MW and of at least 5 MW at each group of supply spots, or have a right to sell electricity generated by such facilities;

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a consumer of electricity must own power receiving facilities with a total capacity of at least 20 MVA and of at least 750 kVA at each group of supply spots;

any participant of the wholesale market must be able to collect, process and transfer to the TSA data about the electricity generated (consumed) at each supply spot, and must have entered into electricity transmission agreements and into dispatching services agreements.

### *The new wholesale electricity market*

On August 31, 2006, the Russian government enacted new wholesale market rules as another step in fully liberalizing the former wholly regulated electricity and capacity markets. Currently electricity is traded on the basis of the following trading mechanisms:

#### Regulated bilateral contracts

Regulated contracts which replaced the former regulated market, are effectively take-or-pay obligations at regulated prices defined by the Federal Tariff Service (the FTS) for electricity and capacity volumes. The volumes of electricity to be traded by the generators under regulated contracts are set up by the FTS annually based on percentages of the volumes of electricity generated in the previous year. Under Government Resolution No. 205 dated April 7, 2007, starting from 2008 the volumes of electricity to be traded under regulated contracts are to gradually decline for the wholesale market to become fully liberalized by the year 2011. The volumes of electricity to be traded under regulated contracts in 2009 are set at 75% for the first half of 2009 (ending on June 30, 2009) and at 50% for the remainder of 2009.

A generator may provide the volumes of electricity it must sell under regulated contracts either through own generation or through the purchase of electricity on the spot market at market prices. Similarly, its customers receive electricity at regulated prices in the volumes agreed under the regulated contracts, regardless of their actual needs, and can freely trade the imbalance on the spot market at market prices (either by purchasing additional volumes, if needed, or, selling the excess electricity volumes). Each year, the supplier and consumer under a regulated contract have an option to terminate their contract upon mutual consent. If they exercise the option, the generator can sell and the customer will have to purchase the respective electricity/capacity volumes under non-regulated contracts or on other markets. For the rest of the year, neither party will have the option to revert to the terminated regulated contract; however, they can enter into a new regulated contract at the beginning of the next year.

The payments under regulated contracts go through the settlement body of the Financial Settlement Center.

#### Non-regulated bilateral contracts

Electricity supply volumes which are not agreed upon under regulated contracts, as well as all new generation capacity commissioned after January 1, 2007, can be traded by participants of the wholesale market under non-regulated contracts, on the one-day-ahead spot market or on the balancing market.

All terms of electricity supply under non-regulated contracts are subject to free negotiation between sellers and purchasers.

#### One-day-ahead spot market

On the spot market generators submit offers and customers submit bids for electricity volumes to be supplied at certain hour of the next trading day. The TSA matches these offers and bids using a minimal price criterion, thus determining the volumes and equilibrium prices for each hour of the next day. The volumes traded under regulated contracts are taken into account when dispatching the balance on the spot market.

Non-regulated bilateral sale and purchase capacity contracts

The volumes of capacity which are not agreed upon under regulated contracts as well as all new generation capacity commissioned after January 1, 2007 can be traded by participants of the wholesale market under non-regulated contracts on the capacity market.

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### **Balancing market**

The balancing market is used to cover any deviations between the electricity volumes scheduled for supply on the spot market and the actual generated and purchased volumes.

#### *Retail electricity market*

New retail market rules were introduced in August 2006 to govern the interaction between wholesale and retail market participants during the restructuring of the electricity industry. The retail market currently includes sales companies that do not generate electricity, but purchase it from generators on the wholesale market.

The retail electricity market operates on the following main principles: (1) end consumers are free to choose between sales companies; (2) end consumers purchase at free prices set on the market, except for contracts with guaranteeing suppliers; and (3) guaranteeing suppliers cannot refuse to enter into a contract with an end consumer.

Starting from 2010, guaranteeing suppliers will be appointed pursuant to public tenders. Currently the sale companies which spun off from former regulated regional electricity companies are appointed as guaranteeing suppliers. Their areas of operation across the country are determined by regional authorities. Our Kuzbass Power Sales Company has been appointed as a guaranteeing supplier in Kemerovo region.

The new retail market rules also establish new system of pricing within the retail market. Guaranteeing suppliers sell electricity under prices set by the respective regional authorities subject to the minimum and maximum levels defined by the FTS. These levels are calculated under a formula based on the average weighted target (indicative) price of one unit of electric power (1 kWh) on the wholesale market (published annually by the TSA). The formula also takes account of the regulated prices for power transmission services, for services provided by the TSA and the higher prices paid by retail customers.

The new retail market rules provide for liberalization of the retail market alongside the wholesale market. All consumers, except for households and alike, have already started purchasing electricity at free prices.

#### *Generation capacity market*

Under the new wholesale market rules, capacity is traded separately from electricity. Capacity payments represent a standby compensation for a generator's availability to produce electricity. Regulated capacity payments (under regulated contracts) are set individually for each generator on the basis of its fixed costs divided by planned and preliminarily dispatched capacity. To sell capacity, generators must maintain their generating facilities in proper condition in order to be always ready to produce electricity meeting the required volumes and the specifications set by the System Operator. Capacity payments depend on fulfillment of these obligations.

According to the new wholesale market rules, excessive capacity (not traded under regulated contracts) and new capacity (commissioned after January 1, 2007) are to be traded at free prices determined on the results of auctions.

#### *Heat market*

Heat markets are regional retail markets and heat prices are regulated and set within the general guidelines provided by the FTS and by regional authorities. Minimum and maximum prices for heat energy traded on the retail markets are set by the FTS separately for each administrative region of Russia for a period of at least one year. Regional authorities establish the prices for relevant territories within the range set by the FTS and subject to the types and prices of fuel used to produce the heat and the volumes of heat purchased on the relevant territory.

Our Southern Kuzbass Power Plant delivers heat energy (in the form of hot water) at regulated prices to residential and commercial customers in the city of Kaltan and in the city of Osinniki. Mechel-Energo delivers heat energy (in the form of hot water and steam) at regulated prices to residential and commercial customers in the cities of Vidnoe, Chelyabinsk, Chebarkul, Beloretsk, Mezhdurechensk and Myski.

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### **U.S. Environmental, Health, Safety and Related Regulation**

The BCG companies, like the rest of the coal mining industry in the United States, are subject to a variety of federal, state and local laws and regulations with respect to matters such as: the pollution, protection, investigation, reclamation and restoration of the environment, human and animal health and safety, and natural resources; the use, generation, handling, transport, treatment, storage, recycling, disposal, presence, release and threatened release of and exposure to hazardous substances or waste; noise, odor, mold, dust and nuisance; and cultural and historic resources, land use and other similar matters. We are required to incur significant costs to comply with these requirements.

Violators of the laws summarized below may generally be subject to fines, in most cases applicable on a per day, per violation basis. In some cases even seemingly minor violations may add up to significant penalties. In addition, most U.S. environmental, health and safety laws authorize citizen suits, permitting third parties to make claims for violations of law.

We endeavor to conduct our operations in compliance with all applicable regulatory requirements, but violations may occur from time to time. If we fail to comply with any present or future regulations, we could be subject to liabilities, required changes to or the suspension of operations, and fines and penalties. In addition, such regulations would restrict our ability to expand our facilities or could require us to acquire costly equipment or incur other significant expenses. Often, private suits for personal injury, property damage or diminution, or similar claims may be initiated in connection with alleged regulatory infractions.

Certain environmental laws impose liability for the costs of removal or remediation of hazardous or toxic substances on an owner, occupier or operator of real estate, even if such person or company was unaware of or not responsible for the presence of such substances. Soil and groundwater contamination may have occurred at, near or arising from some of our facilities, including instances in which contamination may have existed prior to our ownership or occupation of a site. As a result, we may incur cleanup costs in such potential removal, remediation or reclamation efforts.

From time to time new regulations are enacted, or existing requirements are changed, and it is difficult to anticipate how such regulations will be implemented and enforced. We continue to evaluate the necessary steps for compliance with regulations as they are enacted.

The following is a summary of various U.S. environmental, health and safety and similar regulations that we believe have a material impact on our U.S. coal business, based in West Virginia.

#### ***Surface Mining Control and Reclamation Act and corresponding West Virginia law***

The federal Surface Mining Control and Reclamation Act, which is administered by the U.S. Department of Interior's Office of Surface Mining Reclamation and Enforcement, establishes mining, environmental protection and reclamation requirements for all aspects of surface mining, as well as many aspects of underground mining. States that have adopted comprehensive mining regulatory programs may obtain federal approval and become the regulatory authority with primary control and enforcement of these standards. The West Virginia Surface Coal Mining and Reclamation Act ( SCMRA ) was enacted as an approved state program for administration of the federal Surface Mining Control and Reclamation Act.

SCMRA and the rules promulgated thereunder set forth detailed design, construction and performance standards for surface and underground mines that parallel the requirements of the federal regulations. SCMRA prohibits any person from engaging in surface mining operations without a permit from the state Department of Environmental Protection ( DEP ). Permit requirements generally track, but are not identical to, the federal regulations. The state regulations, for example, contain special procedures for ascertaining the ownership, control and compliance status of the applicant. In

addition, provisions relating to bonding, prospecting and inactive status differ from the federal regulations.

Underground coal mining operations must also maintain permits for their above-ground effects. Permit requirements include submitting a subsidence control plan that describes the type of mining to be conducted and its probable surface impacts. The plan must generally include measures to minimize subsidence and related damages.

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Administrative enforcement provisions include civil penalties, cessation orders and permit revocation. Appeals from DEP actions are heard by the Surface Mining Board and limited judicial review is available upon appeal to the circuit court of the county in which the mine is located. Suits by private citizens may also be brought to obtain injunctions or damages.

Prospecting activity must be preceded by a notice of intent to prospect. Where more than a specified amount of coal is to be removed, public notice and an opportunity for comments must be given before obtaining the required approval from DEP.

Under SCMRA, surface mining operations must also comply with monitoring requirements and effluent limitations set forth in the federal Clean Water Act. In addition, the state Water Pollution Control Act requires that a permit be obtained to construct, install, modify, reopen, operate or abandon any mine, quarry or preparation plant from which any discharges or pollution are expected. See below for further discussion of the Clean Water Act and other water related regulatory issues.

Like its federal counterpart, SCMRA also provides for the designation of certain areas as unsuitable for all or certain types of surface mining.

The West Virginia Abandoned Mine Lands and Reclamation Act, created pursuant to Title IV of SCMRA, establishes an abandoned mine reclamation fund for reclamation and restoration activities and preventive and remedial measures associated with past mining.

***Surety bonds and mine closure costs***

Federal and state laws require mining operations to obtain surety bonds or other forms of financial security to secure payment of certain long-term obligations, including mine closure and reclamation costs, federal and state workers compensation costs and other miscellaneous obligations. Many of these bonds are renewable on an annual basis. In recent years, surety bond premiums have increased and the market terms of surety bonds have generally become less favorable. The number of companies willing to issue surety bonds has also declined. We cannot predict with certainty our future ability to obtain, or the cost of, surety bonds that may be required for our operations.

***Mine safety and health***

The U.S. coal mining industry is subject to extensive and comprehensive regulation with respect to worker health and safety. In 1977 the Federal Mine Safety and Health Act consolidated all federal health and safety regulations of the mining industry (coal and non-coal) under a single statutory scheme. The Act strengthened and expanded the rights of miners, and enhanced the protection of miners from retaliation for exercising those rights. The Act also created the Mine Safety and Health Administration ( MSHA ), which administers the provisions of the Act and enforces compliance with mandatory safety and health standards. MSHA has authority over all mining and mineral processing operations in the United States, regardless of size, number of employees, commodity mined or method of extraction. The Federal Mine Safety and Health Review Commission independently reviews MSHA s enforcement actions. West Virginia also maintains a program for mine safety and health regulation, inspection and enforcement.

In response to certain highly publicized mine incidents in recent years, legislative and regulatory bodies at the federal and state levels, including MSHA, have promulgated or proposed various new statutes, regulations and policies relating to mine safety and mine emergencies, including the federal MINER Act passed in 2006 and the recently proposed S-MINER Act. Some of the new obligations include, for example, improved technologies and safety practices, tracking and communication, emergency response plans and equipment. In addition, federal black lung benefits laws and coal industry health benefits laws, among others, may impact us. Regulatory efforts in this area are

ongoing. At this time, it is not possible to predict with accuracy the full effect of new and future U.S. mine health and safety regulation on our business.

*Clean Air Act ( CAA )*

The CAA and corresponding state rules regulate emissions of materials into the air and affect our U.S. coal operations both directly and indirectly. Certain sources of air pollution, for example, including coal mining and

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processing operations, must obtain and maintain operating permits, which are generally reviewed every five years and contain compliance requirements such as compliance certification, testing, monitoring, reporting and recordkeeping. Such operations are also subject to emission restrictions, including for particulate matter and fugitive dust. The CAA also indirectly affects coal mining operations by extensively regulating the emissions of coal-fueled power plants and industrial boilers. In general, there has been increased interest in recent years in legislation focused on power plant emissions. Construction of new sources of air pollution (including in some cases reconstruction and modification of existing sources) also triggers preconstruction review and approval by authorities, with typically more stringent control technology and permitting requirements.

Some of the CAA requirements that may materially directly or indirectly affect our operations are briefly described below. West Virginia has also promulgated regulations relating to acid rain, emissions limitations for specific pollutants, and permit standards for the construction, major modification or relocation of major stationary sources of air pollution. Standards governing air pollution from coal refuse disposal, coal preparation plants, coal handling operations and ambient air quality for particular pollutants, as well as procedures relating to air pollution emergencies, are also established under the state regulations.

*Acid rain.* One of the regulatory programs established under the CAA concerns the control of sulfur dioxide and nitrogen oxide ( NO<sub>x</sub> ), precursors of acid deposition. Through an emission allowance and trading program, Title IV of the CAA imposes a two-phase cap on total sulfur dioxide emissions from sources including electric utilities. All of the Phase I and Phase II allowances offered by the U.S. Environmental Protection Agency (the EPA ) have been purchased each year since there is no minimum bid requirement. In general, affected power plants have also sought to comply with these requirements by switching to lower sulfur fuels, installing pollution control equipment, and reducing electricity generation levels. The program also directs the EPA to impose NO<sub>x</sub> emissions rate limits on coal-fired electricity generating sources. At this time, we believe that these regulations have affected coal prices but we cannot predict with certainty the future effect of these CAA provisions on our business.

*Emissions standards for particulate matter and ozone.* A significant component of the CAA is the national ambient air quality standard ( NAAQS ) program, which addresses pervasive pollution that endangers public health and welfare. NAAQS have been established for a number of pollutants, including particulate matter and ozone. For each of these pollutants, NAAQS are set at certain levels and areas that do not meet one or more of the NAAQS are known as nonattainment areas and must comply with a number of special requirements. NAAQS are to be reviewed and revised as appropriate at least every five years. In recent years the EPA has made a number of decisions regarding the NAAQS program that have been the subject of controversy and litigation, and may have important implications for future regulation under the CAA. Regulation and enforcement of new standards for particulate matter and ozone will affect many power plants, especially in nonattainment areas, and significant emissions control expenditures may be required to meet these current and emerging standards.

*Clean Air Interstate Rule.* The Clean Air Interstate Rule ( CAIR ) is a program for approximately 28 eastern states, including West Virginia, that contribute to downwind states nonattainment of NAAQS. CAIR applies to sulfur dioxide and NO<sub>x</sub>. It interacts with, and in some cases supersedes, other existing programs under the CAA such as the Acid Rain program, the Regional Haze rule and the NO<sub>x</sub> SIP Call. The CAIR requires states to revise their State Implementation Plans ( SIPs ) to reduce emissions of sulfur dioxide and NO<sub>x</sub>. The CAIR has been the subject of litigation since its promulgation and it is currently unclear how the EPA will modify the CAIR in response. The existing CAIR, however, is generally expected to require many coal-fueled power plants to install additional pollution control equipment or to incur other costs, and further changes to the CAIR rules may increase these burdens. All of the foregoing could adversely affect the purchase of our coal by customers.

*Clean Air Mercury Rule.* In 2005, the Clean Air Mercury Rule ( CAMR ) became the first regulation to directly address mercury contamination. The rule would have applied to new and existing coal-fueled electric utility steam generating units nationwide and creates a cap-and-trade system. Each affected unit would be required to have a continuous emission monitoring system or an effective long-term system that can trap an uninterrupted sample of mercury, and maintain records and report periodically to demonstrate

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compliance with the mercury limits. The rule, however, was recently vacated during litigation, and EPA has announced plans for a new rulemaking. Separate state standards may also be passed. Regardless of whether these or other measures are implemented, rules imposing stricter limitations on mercury emissions from power plants may adversely affect the demand for coal.

*Regional haze.* The EPA has initiated a regional haze program to address visibility issues in and around national parks and wilderness areas. Among other things, the program requires state permitting authorities to consider the effects of new major facilities on federally protected lands, and may require existing facilities to undertake additional pollution control measures. These limitations could affect the future market for coal.

### ***Climate change***

A major by-product of burning coal is carbon dioxide, which is considered a greenhouse gas and generally a source of concern in connection with global warming and climate change. Regulation of greenhouse gases in the United States is currently subject to complicated domestic and international political, policy and economic dynamics. As climate change issues become more prevalent, the U.S. and other governments are seeking to respond to these concerns.

For example, in 2007 the United States Supreme Court confirmed that the EPA has authority to classify carbon dioxide and other greenhouse gases as pollutants and regulate them under the CAA. In April 2009, the EPA issued a proposed endangerment finding that carbon dioxide and five other greenhouse gases endanger the public health and welfare. Also in April 2009, the EPA published a proposed rule on greenhouse gas emissions reporting, which would cover a wide range of sources including electricity generation and coal mines. On the legislative side, the proposed federal Clean Energy and Security Act of 2009 was recently introduced in the U.S. Congress that would require national reductions in greenhouse gas emissions and would require utilities to generate a certain percentage of their electricity supply from renewable sources. A number of state and regional greenhouse gas initiatives are also being developed.

This increasing governmental focus on global warming could result in new environmental regulations that may negatively affect us and our customers. Future regulation of greenhouse gases in the United States could occur pursuant to future U.S. treaty obligations, regulatory changes under the CAA or other existing legislation, federal, state or regional adoption of greenhouse gas regulatory schemes, or any combination of the foregoing or otherwise. This could cause us to incur additional direct costs in complying with any new regulations, as well as increased indirect costs resulting from our customers incurring additional compliance costs and potentially reducing their consumption of coal. These costs may adversely impact our operations and financial condition.

### ***Clean Water Act ( CWA ) and Safe Drinking Water Act ( SDWA )***

The CWA establishes a number of programs designed to restore and protect the quality of U.S. waters by eliminating the discharge of pollutants into surface waters. These programs include the National Pollutant Discharge Elimination System ( NPDES ) permit program, the dredge and fill permit program and municipal wastewater treatment programs. Coal extraction and related activities subject to the West Virginia SCMRA and Water Pollution Control Act are exempt from certain of these requirements.

The NPDES system implements CWA's prohibition on unauthorized discharges by requiring a permit for every discharge of pollutants from a point source to navigable waters of the United States. NPDES permits give the permittee the right to discharge specified pollutants from specified outfalls, usually for a period of five years. The permit normally sets numerical limits on the discharges and imposes conditions on the permittee (including filing periodic discharge and monitoring reports); discharges that require a permit include industrial process wastewater, non-contact cooling water and collected or channeled storm water runoff. The CWA also

requires many facilities to develop and maintain plans for preventing and responding to spills of hazardous substances, called Spill Prevention Control and Countermeasure ( SPCC ) Plans, and certain high-volume hazardous substance handling/storage facilities are required to prepare and maintain a more extensive plan called a Facility Response Plan.

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EPA has delegated NPDES permitting authority to West Virginia. West Virginia water pollution law is generally broader than its federal counterparts. For example, among other things, state law regulates discharges into all waters of the state, including groundwater, and requires permits for the construction of disposal systems.

Coal companies are required to maintain a CWA Section 404 permit from the Army Corps of Engineers generally authorizing the disposal of dredged and fill material from coal mining activities into the waters of the United States, for the purpose of creating slurry ponds, water impoundments, refuse disposal areas, valley fills and other mining activities. Permits issued under Section 404 are subject to court challenge, and in recent years both nationwide and individual permits have been litigated, including in West Virginia.

SDWA primarily targets public water systems, which generally includes any system for the provision of water to the public for human consumption through pipes or other constructed conveyances if such system has at least 15 service connections or regularly serves at least 25 individuals. This broad definition can include informal and transient water systems (*e.g.*, businesses such as coal mining operations having their own wells or water supplies for on-site workers). West Virginia state law prohibits the installation or establishment of any system or method of drainage, water supply or sewage disposal without first obtaining a permit from the Bureau of Public Health. The Department of Health and Human Resources has promulgated rules which adopt the National Drinking Water Regulations under the SDWA. These rules, among other things, require chlorination of public water systems and set fluorination standards.

### ***Comprehensive Environmental Response, Compensation and Liability Act ( CERCLA )***

CERCLA is designed to address comprehensively the problems associated with contaminated land, especially inactive and abandoned hazardous waste sites, listed on the National Priorities List ( NPL ). Many states maintain analogous programs.

CERCLA's central provisions authorize the EPA to clean up these sites using money from the so-called Superfund (generated by tax revenues) and then to recover the cleanup costs from so-called potentially responsible parties ( PRPs ) who have contributed to the contamination. In addition, private parties may implement EPA-approved cleanups.

Under CERCLA a PRP's liability is strict, joint, several and retroactive; in other words, liability may be imposed regardless of fault, may relate to historical activities or contamination, may require one party to bear the costs of the entire cleanup and has no requirement that the party's activities or hazardous substances have actually caused the contamination. Categories of liable parties under CERCLA include current owners, lessees and operators, former owners, lessees and operators, waste generators or arrangers, and transporters. Accordingly, it is possible for us to become subject to investigation or cleanup obligations (or related third-party claims) in connection with onsite or offsite contamination issues, including those caused by predecessors.

CERCLA contains a cost recovery provision generally authorizing one PRP to initiate a private claim against another PRP for cleanup liabilities.

### ***Other U.S. environmental, health and safety laws***

We are or may be required to comply with a number of additional federal, state and local environmental, health, safety and similar requirements in addition to those discussed above, including, for example, the Resource Conservation and

Recovery Act ( RCRA ), Toxic Substances Control Act ( TSCA ), the Emergency Planning and Community Right-to-Know Act ( EPCRA ), Occupational Safety and Health Act ( OSHA ), Endangered Species Act ( ESA ) and others.

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**Item 5. *Operating and Financial Review and Prospects***

*The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes and other information in this document. This Item 5 contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in forward-looking statements as a result of various factors, including the risks described in Item 3 and under the caption *Cautionary Note Regarding Forward-Looking Statements*.*

In this Item, the term *domestic* describes sales by a production subsidiary within the country where its operations are located. This category is further divided between subsidiaries in Russia and subsidiaries in other countries. The term *export* describes cross-border sales by a subsidiary regardless of its location. See note 25 to our consolidated financial statements in Item 18. Financial Statements.

**Going Concern**

***Russian business environment***

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. The ongoing global financial crisis has resulted in capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions within Russia. While the Russian government has introduced a range of stabilization measures aimed at providing liquidity and supporting debt refinancing for Russian banks and companies, there continues to be uncertainty regarding the access to capital and cost of capital for the group and its counterparties, which could affect our group's financial position, results of operations and business prospects. These considerations similarly apply to other jurisdictions where our group operates.

Our group's activities in all our operating segments have been adversely affected by the uncertainty and instability in international financial, currency and commodity markets resulting from the global financial crisis. The recession is affecting most economic regions, forcing us to reduce production, cut costs, manage increased risk factors and strengthen our competitiveness, including curtailing production, halting non-critical capital expenditures, accelerating new strategies for raw materials, initiating headcount reductions, suspending major investment programs, and making other liquidity enhancements.

We believe we are taking appropriate measures to support the sustainability of our business in the current circumstances. We believe our operational cash flow in 2009 will be sufficient to fund proprietary capital expenditure projects and permit us to operate the business in a profitable fashion during 2009. However, further market deterioration could negatively affect our consolidated results, financial position and cash flow in a manner not currently determinable.

***Going concern***

The current economic environment is challenging and we believe that the outlook for the next several years presents significant challenges in terms of sales volume and pricing as well as input costs. Specifically, the current economic conditions create uncertainty about (1) the level of demand for our products; (2) the pricing of major commodities mined or manufactured by us; (3) the exchange rate between the Russian ruble and U.S. dollar and its impact on the cost of our inventories; and (4) the availability of bank financing in the foreseeable future.

We believe we have taken measures to deal with the uncertainties in our operating environment and that our operating cash flows in 2009 will be sufficient to allow us continue to operate in the normal course of business including routine working capital and priority capital projects, assuming the successful restructuring of our debt as described below.

As of December 31, 2008, we breached a number of financial and non-financial covenants (as discussed in [Liquidity and Capital Resources](#) [Covenant breaches](#) below) and as a result, the lenders can request accelerated repayment of a substantial portion of our long-term debt. As of December 31, 2008, we had \$5.149 million of loans repayable during 2009, including \$1.564 million of long-term debt that was classified as short-term liabilities as of that date because of the covenant violations. We do not have the resources to enable us to repay the total of these loans if repayment were called.

Our group has commenced discussions with our bankers about additional facilities to be provided on a long-term basis. Our group is also seeking to refinance and/or restructure the terms and conditions of our existing debt to extend

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maturities beyond 2009 and provide greater working capital flexibility. Our group is currently in negotiations with the consortium of banks, but it is likely that the terms and agreement on the conditions of these borrowing arrangements will not be completed until the second half of 2009. Based on negotiations conducted to-date, we believe that we will successfully refinance or restructure the terms and conditions of (1) \$1,000.0 million out of the \$1,500.0 million Oriel credit facility and (2) its \$1,781.0 million Yakutugol syndicated loan. To repay the remaining \$500.0 million of the Oriel credit facility, we plan to use half of the credit line obtained from Gazprombank referred to below.

We have succeeded in obtaining additional financing by reaching the following credit line agreements:

*Gazprombank* \$1,000.0 million U.S. dollar-denominated credit facility repayable in quarterly installments in 2010-2012 for a partial repayment of its Oriel and Yakutugol credit facilities. As a security for these credit facilities the group pledged 35% of the shares in Yakutugol and Southern Kuzbass Coal Company;

*VTB* 15 billion rubles (\$510.1 million) credit facility expiring in November 2009 under the guarantees issued by Mechel and pledges of Southern Kuzbass Coal Company and Chelyabinsk Metallurgical Plant production assets;

*Sberbank* 3.3 billion rubles (\$112.3 million) credit facility due in 2010.

We are also pursuing alternative sources of funding in the event the above mentioned negotiations do not result in adequate funding. Specifically, in February 2009, our group registered one-year ruble-denominated bonds in an aggregate principal amount of 30 billion rubles (\$824.6 million) with the Moscow Interbank Currency Exchange (MICEX). Subsequently, in May 2009, the group registered another ruble-denominated bond issue of 45 billion rubles (\$1,406.9 million) with the FFMS. Issuance of these bonds would be subject to market conditions at the time, and while we have not formally decided to proceed with the issuance of these bonds, if issued, these bonds would provide us with additional financing flexibility.

Furthermore, our group has been included in the Russian Government's list of strategic businesses that are eligible for state financial support in the current economic environment. Subsequently, in January 2009 our group received an approval from the state-owned Vneshekonombank (VEB) for a one-year \$1,500.0 million facility to refinance the Oriel credit facility, which to-date we have elected not to use. There is no assurance, however, as to how much further state financial support, if any, may be received by us.

We have concluded that the uncertainty about our refinancing and restructuring of our outstanding debt described above represents a material uncertainty that casts significant doubt upon our ability to continue as a going concern. However, based on our plans as noted herein, we believe that we have, or will secure, adequate capital resources and liquidity to continue in operational existence for the foreseeable future and have presented our consolidated financial statements on a going concern basis of accounting.

See Item 3. Key Information Risk Factors Risks Relating to Our Financial Condition and Financial Reporting There is substantial doubt about our ability to continue as a going concern and Item 3. Key Information Risk Factors Risks Relating to our Financial Condition and Financial Reporting We could be materially adversely affected if our lenders accelerate our debt due to our current and future failures to comply with our loan agreements.

## **The Reorganization**

Mechel OAO was incorporated on March 19, 2003, under the laws of the Russian Federation, in connection with a reorganization to serve as a holding company for various mining and steel companies owned by Mr. Zyuzin and Vladimir Iorich or parties affiliated with them. These individuals acted in concert from 1995 until December 2006

pursuant to an Ownership, Control and Voting Agreement which required them to vote the same way. The reorganization involved the contribution of these companies by these individuals to Mechel in exchange for all the outstanding capital stock of Mechel. Many of the contributed companies had shareholders other than Messrs. Zyuzin and Iorich, and these shareholders were not involved in the reorganization and continue to retain minority interests in certain of our subsidiaries.

During the period from March through December 2006, Mr. Iorich disposed of his entire interest in Mechel OAO to Mr. Zyuzin, and the Ownership, Control and Voting Agreement terminated on December 21, 2006.

**Table of Contents****Business Structure*****Segments***

We have organized our businesses into four segments:

the mining segment, comprising the production and sale of coal (coking and steam) and iron ore, which supplies raw materials to our steel business and also sells substantial amounts of raw materials to third parties, and includes logistical assets, such as our seaports on the Black Sea and the Pacific Ocean and our railway transportation assets;

the steel segment, comprising the production and sale of semi-finished steel products, carbon and specialty long products, carbon and stainless flat products, value-added downstream metal products including hardware, forgings and stampings, as well as steel industry materials such as limestone, coke and coking products, and our river port in the Volga River watershed;

the ferroalloys segment, comprising the production and sale of nickel ore, low-ferrous ferronickel, ferrochrome and ferrosilicon, which supplies raw materials to our steel business and also sells substantial amounts of raw materials to third parties, the largest of which is Glencore International; and

the power segment, comprising power generating facilities, which supply power to our mining and steel segments and also sell a portion of the power generated to third parties, and a power distribution company.

The table below sets forth by segment our key mining, steel, ferroalloys and power subsidiaries, presented in chronological order by date of acquisition.

<b>Name</b>	<b>Location of Assets</b>	<b>Product/Business</b>	<b>Date Control Acquired</b>	<b>Voting Interest<sup>(1)</sup>%</b>
<b><i>Mining Segment</i></b>				
Southern Kuzbass Coal Company <sup>(2)</sup>	Russia	Coking coal concentrate, steam coal, steam coal concentrate	January 1999	95.4%
Tomusinsk Open Pit Mine	Russia	Coking coal, steam coal	January 1999	74.5%
Korshunov Mining Plant	Russia	Iron ore concentrate	October 2003	85.6%
Port Posiet	Russia	Seaport: coal warehousing and loading	February 2004	97.1%
Transkol	Russia	Railway transportation	May 2007	100.0%
Yakutugol	Russia	Coking coal, steam coal	October 2007	100.0%
Elgaugol <sup>(3)</sup>	Russia	Coking coal, steam coal (in development)	October 2007	71.2%
Port Temryuk <sup>(4)</sup>	Russia	Seaport: coal transshipment	March 2008	100.0%
Port Vanino	Russia	Coal transshipment complex (under construction)	November 2008	100.0%
Mechel Bluestone Inc.	United States	Coking coal	May 2009	100.0%

**Steel Segment**

Chelyabinsk Metallurgical Plant	Russia	Semi-finished steel products, carbon and specialty long and flat steel products, forgings, coke and coking products	December 2001	94.2%
Vyartsilya Metal Products Plant	Russia	Hardware	May 2002	93.3%
Beloretsk Metallurgical Plant	Russia	Long steel products, hardware, limestone <sup>(5)</sup>	June 2002	91.4%
Mechel Targoviste	Romania	Carbon and specialty long steel products, forgings, hardware	August 2002	86.6%
Urals Stampings Plant	Russia	Stampings	April 2003	93.8%
Mechel Campia Turzii	Romania	Long steel products, hardware	June 2003	86.6%

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<b>Name</b>	<b>Location of Assets</b>	<b>Product/Business</b>	<b>Date Control Acquired</b>	<b>Voting Interest<sup>(1)</sup>%</b>
Mechel Nemunas	Lithuania	Hardware	October 2003	100.0%
Izhstal	Russia	Specialty and carbon steel long products, hardware, stampings and forgings	May 2004	88.4%
Port Kambarka	Russia	River port	April 2005	90.4%
Metals Recycling	Russia	Metal scrap processing	March 2006	100.0%
Moscow Coke and Gas Plant	Russia	Coke and gas works, organic chemicals	October 2006	99.5%
Ductil Steel	Romania	Carbon steel, low-alloyed steel rolled and wire products	April 2008	100.0%
HBL Holding GmbH	Germany	Steel trading and distribution, servicing, cutting and processing steel products, warehousing system	September 2008	100.0%
<b><i>Ferroalloys Segment</i></b>				
Southern Urals Nickel Plant	Russia	Ferronickel	December 2001	84.1%
Bratsk Ferroalloy Plant	Russia	Ferrosilicon	August 2007	100.0%
Oriel Resources	Russia, Kazakhstan	Chrome and nickel mining and processing	April 2008	100.0%
Tikhvin Ferroalloy Plant	Russia	Ferrochrome	April 2008	100.0%
<b><i>Power Segment</i></b>				
Southern Kuzbass Power Plant	Russia	Electricity	April 2007	98.3%
Kuzbass Power Sales Company	Russia	Electricity distribution	June 2007	72.1%

- (1) Except where the acquisition date occurred after December 31, 2008 (in which case the percentage is given as of the date of completion of the acquisition), the percentages provided in this table are as of December 31, 2008. Some of our Russian subsidiaries have preferred shares outstanding that have voting rights commensurate with common shares if dividends on those shares have not been paid. We have calculated voting interests by including these preferred shares for subsidiaries where dividends have not been paid.
- (2) In 2005, we commenced the restructuring of Southern Kuzbass Coal Company, during the course of which we merged the company with certain of its subsidiaries. As a result of the merger of these subsidiaries into Southern Kuzbass Coal Company, our current ownership stake in Southern Kuzbass Coal Company is 95.4%.
- (3) With effect upon the end of the first quarter of 2008, the subsoil license to the Elga coal deposit was transferred from Elgaugol to Yakutugol.
- (4)

Port Temryuk is a seaport located at the Taman shore of the Sea of Azov, an inlet of the Black Sea, and is primarily utilized for small tonnage river-sea type vessels in southern Russia. In order to organize coal transshipment we purchased the Temryuk-Sotra, Soyuztranzit and Tekhnoprodintorg companies. The assets of the acquired companies, as well as the acquired assets of a Russian Railways transshipment complex were transferred to the balance sheet of the newly created Port Temryuk company. Temryuk-Sotra, Soyuztranzit and Tekhnoprodintorg are in the process of liquidation, which is expected to be completed by the end of 2009. We plan to use Port Temryuk mainly for transshipment.

(5) Our Pugachev limestone quarry is 100% owned by Beloretsk Metallurgical Plant and is within the steel segment.

***Intersegment sales***

We are an integrated mining, steel, ferroalloys and power group. As such, within our group the companies in our reporting segments supply materials to other companies in the same reporting segment or different reporting segments. In the year ended December 31, 2008, the mining segment supplied approximately 60% of the steel segment's coking coal requirements, approximately 70% of the steel segment's iron ore concentrate requirements,

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approximately 75% of the power segment's coal requirements and 100% of the ferroalloys segment's coal requirements. The ferroalloys segment supplied 100% of the steel segment's requirements in ferrochrome, ferrosilicon and nickel. The steel segment also supplies wires, ropes, hardware and other metal products to the mining segment for use in its day-to-day operations, as well as 100% of coke for use in the production of nickel, ferrochrome and ferrosilicon by the ferroalloys segment. The power segment supplies approximately 57% of the group's overall electricity requirements, with the remainder of the electricity sold to third parties. The prices at which we record these transfers are based on market prices, and these transactions are eliminated as intercompany transactions for the purposes of our consolidated financial statements. For the years ended December 31, 2008, 2007, and 2006, mining segment sales to the steel segment amounted to \$659.6 million, \$575.1 million and \$296.7 million, respectively. For the years ended December 31, 2008, 2007 and 2006, steel segment sales to the mining segment amounted to \$7.0 million, \$6.0 million and \$3.3 million, respectively. For the years ended December 31, 2008, 2007 and 2006, mining segment sales to the power segment amounted to \$27.7 million, \$11.3 million and \$0.4 million, respectively. For the years ended December 31, 2008, 2007 and 2006 steel segment sales to the power segment amounted to \$174.8 million, \$22.5 million and \$17.2 million, respectively. For the years ended December 31, 2008, 2007 and 2006, power segment sales to the mining segment amounted to \$53.1 million, \$30.4 million and \$24.3 million, respectively. For the years ended December 31, 2008, 2007 and 2006, power segment sales to the steel segment amounted to \$257.4 million, \$38.6 million and \$41.1 million, respectively. For the years ended December 31, 2008, 2007 and 2006 ferroalloys segment sales to the steel segment amounted to \$150.6 million, \$135.5 million and \$79.9 million, respectively. For the years ended December 31, 2008, 2007 and 2006 steel segment sales to the ferroalloys segment amounted to \$96.8 million, \$79.1 million and \$20.4 million, respectively. For the years ended December 31, 2008, 2007 and 2006 mining segment sales to the ferroalloys segment amounted to \$11.3 million, \$12.1 million and \$11.5 million, respectively. For the years ended December 31, 2008, 2007 and 2006 power segment sales to the ferroalloys segment amounted to \$29.5 million, \$26.2 million and \$8.5 million, respectively.

***Acquisitions***

Our acquisitions enhance the vertical and geographical integration of our group and contribute to the growth of our business segments. We have sought to purchase strategy and under-performing assets which we believe offer significant upside potential, particularly as we make capital investments and implement improvements in working practices and operational methods. Immediately following the acquisition, there is a period of time during which we implement our strategies and do not realize their full benefits and, consequently, our margins are initially adversely affected after each acquisition.

Set out below are our key acquisitions during the periods under review in this section. For more detail see note 4 to our consolidated financial statements in Item 18. Financial Statements. Each of the acquisitions was accounted for using the purchase method of accounting, and the results of operations of each acquired business are included in our consolidated statements of income and comprehensive income from their respective dates of acquisition of control. In certain cases where we acquired our interest in a business over a period of time and control was not acquired until subsequent acquisitions of shares, such acquisitions were accounted for using the equity method of accounting or at cost, as appropriate, until such controlling stake was acquired. Our results of operations for the periods presented herein are thus not comparable from period to period due to these acquisitions and their accounting treatment.

*Southern Kuzbass Power Plant.* Southern Kuzbass Power Plant OAO ( Southern Kuzbass Power Plant ) was separated in July 2006 from Kuzbassenergo as the result of Kuzbassenergo's reorganization. The plant is located in the city of Kaltan in the Kemerovo region, in the southern part of Russia's coal-rich Kuzbass region. As of December 31, 2008, the plant's installed electric power capacity was 554 MW, and its heat power capacity was 1,500 Gcal/hour. In addition to electricity sales to the power grid, Southern Kuzbass Power Plant supplies hot water to the city of Kaltan and to the city of Osinniki. In 2008, Southern Kuzbass Power Plant consumed 709,055 tonnes of steam coal and middlings supplied by Southern Kuzbass Coal Company. In April 2007, we acquired at auction from UES, Kuzbassenergo OAO

and SUEK OAO a 94.3% interest in Southern Kuzbass Power Plant for \$270.8 million. We increased our stake in Southern Kuzbass Power Plant to 98.0% during the period from May to December 2007 by purchasing shares from third parties pursuant to mandatory offer. On different dates from January to March 2008 we

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further increased our stake in Shouthern Kuzbass Power Plant to 98.3% for consideration of \$658 thousand paid in cash.

*Kuzbass Power Sales Company*. Kuzbass Power Sales Company is a power distribution company in Siberia, located in the city of Kemerovo. We acquired 49% of Kuzbass Power Sales Company from UES in June 2007 at auction for a purchase price of \$46.4 million, which increased our stake to 50.2%. In October and November 2007, we acquired a further 21.83% in the company from third parties for \$40.9 million. During 2008, we acquired insignificant amount of shares from minority shareholders, increasing our total stake in the company to 72.1%.

*Port Temryuk*. Port Temyruk is a seaport located at the Taman shore of the Sea of Azov, an inlet of the Black Sea, and primarily utilized for small tonnage river-sea type vessels in southern Russia. The port specializes mainly in coal transshipment. We purchased 100% of Port Temryuk-Sotra from third parties for \$6.3 million in July 2007.

*Bratsk Ferroalloy Plant*. Bratsk Ferroalloy Plant is the largest enterprise in Eastern Siberia producing high-grade ferrosilicon, according to Metall-Expert, a private Russian analytical agency focusing on the metals business ( Metall-Expert ). We acquired 100% of Bratsk Ferroalloy Plant from third parties in August 2007 for \$186.9 million.

*Yakutugol*. Yakutugol, located in the Sakha Republic in eastern Siberia, extracts predominantly coking coal, as well as steam coal, in open pit and underground mines. Yakutugol consists of the Nerungrinsk open pit mine and owns through subsidiaries the Kangalassk open pit mine and the Dzhebariki-Khaya underground mine. Most of Yakutugol's high-grade coking coal output is exported to customers in Japan, South Korea and Taiwan. We acquired a blocking minority stake of 25% plus one share for \$411.2 million in January 2005, and increased this stake by purchasing at auction from the government of the Sakha Republic in October 2007 the remaining 75% less one share of Yakutugol and 68.86% of the shares of Elgaugol for a total consideration of \$2.3 billion. In 2008, Yakutugol produced 8.1 million tonnes of coking coal, which represented 53.2% of our total production of coking coal for all of 2008.

*Elgaugol*. Elgaugol's principal asset was its license to mine coal at the Elga coalfield, a deposit of high-grade coal that has been explored and studied in detail for the past several decades. As noted above, we acquired 68.86% of Elgaugol from a company owned by the government of the Sakha Republic in conjunction with our acquisition of the remaining outstanding shares of Yakutugol for a total consideration of \$2.3 billion in October 2007. Prior to this acquisition, Yakutugol owned 2.35% of Elgaugol, which we then acquired through our acquisition of Yakutugol, giving us a current total stake in Elgaugol of 71.21%. The mining license to the Elga coal deposit was transferred to Yakutugol at the end of the first quarter of 2008.

*Ductil Steel*. Ductil Steel S.A. ( Ductil Steel ), a Romanian steelmaker, owns a plant in Buzau which produces carbon steel and low-alloyed steel rolled and wire products, as well as the Otelu Rosu plant, which specializes in steel and billets for rolling. We purchased 100% of Ductil Steel from third parties in April 2008 for \$224.0 million.

*Oriel Resources plc*. Oriel Resources is comprised of the Voskhod chrome project and the Shevchenko nickel project in Kazakhstan, and the Tikhvin Ferroalloy Plant in Russia, near the city of St. Petersburg. Mining operations commenced at the Voskhod chrome deposit in December 2008. We acquired a 99.3% stake in Oriel Resources in April 2008 pursuant to a public tender offer and subsequently increased our stake to 100%, for a total cost of approximately \$1.5 billion.

*HBL Holding GmbH*. The assets of HBL Holding include twelve service and trading companies in Germany. We acquired a 100% stake in HBL Holding in September 2008 for approximately \$55.9 million.

*BCG companies*. In May 2009, we acquired 100% of the shares and interests of U.S. entities Bluestone Industries, Inc., a West Virginia corporation, Dynamic Energy, Inc., a West Virginia corporation, JCJ Coal Group, LLC, a

Delaware limited liability company and some of its West Virginia affiliates (together the BCG companies ), which are privately-held West Virginia-based coal businesses engaged in the mining, processing and sale of premium quality hard coking coal. The aggregate consideration was \$436.4 million paid in cash, approximately 83.3 million of our preferred shares, plus the assumption of approximately \$132.0 million of net debt. See note 27 to our consolidated financial statements in Item 18. Financial Statements.

**Table of Contents*****Discontinued Operations***

In August 2004, we terminated production at Mechel Zeljezara, a Croatian steel mill that produced pipes. Mechel Zeljezara's assets were acquired out of bankruptcy proceedings in March 2003. We started accounting for Mechel Zeljezara as discontinued operations in September 2004. Voluntary bankruptcy proceedings in respect of Mechel Zeljezara were concluded in October 2007 and the company was removed from the Croatian trade register in February 2008. The results of operations of Mechel Zeljezara were previously included in our consolidated financial statements from its date of acquisition in March 2003. For the years ended December 31, 2008, 2007 and 2006 these results were reflected in our consolidated financial statements as discontinued operations.

**Factors Affecting Our Results of Operations and Financial Condition*****Cyclical nature of business and impact of macroeconomic factors***

Our mining and ferroalloys business sells significant amounts of coal, iron ore and ferroalloys to third parties and our revenues depend significantly on these sales. Cyclical and other changes in world market prices of these products affect the results of our mining and ferroalloy operations. The changes in these prices result from factors, such as market supply and demand, which are beyond our control. The global coal, iron ore and ferroalloys supply and demand balance is strongly influenced by interdependent global economic and industrial demand cycles, as well as supply chain-related constraints such as shipping capacity, availability of rolling stock, terrestrial transportation congestion, production disruptions and natural disasters. Prices of the products of our mining and ferroalloys business have varied significantly in the past and could vary significantly in the future. See [Price trends for products](#) below. Also see [Item 3. Key Information Risk Factors Risks Relating to Our Business and Industry](#) We operate in cyclical industries, and any local or global downturn, whether or not primarily affecting the mining and/or steel industries, may have an adverse effect on our results of operations and financial condition.

The steel industry is highly cyclical in nature because the industries in which steel customers operate are cyclical and sensitive to changes in general economic conditions. The demand for steel products thus generally correlates to macroeconomic fluctuations in the economies in which we sell our products, as well as in the global economy. The prices of our steel products are influenced by many factors, including demand, worldwide production capacity, capacity utilization rates, raw material costs, exchange rates, trade barriers and improvements in steel-making processes. Steel prices also typically follow trends in raw material prices and increases in market prices for steel may lag behind increases in production costs, including raw materials.

Demand for steel, particularly long steel products in which we are the most competitive in the Russian market, is closely tied to the construction industry in the markets in which we sell our products. The construction business in Russia, the principal market for our products, has been severely impacted by the global financial crisis and the sharp economic slowdown in Russia. Because of the critical role of steel in infrastructural and overall economic development, the steel industry tends to track macroeconomic factors such as gross domestic product ( GDP ) and industrial output.

The global financial crisis and sharp economic slowdown which started in the second half of 2008 resulted in modest 2.3% growth in global real GDP, according to CRU. According to Rosstat, Russia recorded real GDP growth of 6.0% in 2008 and 9.5% contraction in GDP and 14.9% contraction in industrial production in January through April of 2009. This slow down in economic growth and severe constraints in capital spending, both globally and in Russia, led to poor demand for our products and a substantial decrease in the prices for our products in the fourth quarter of 2008. The first quarter of 2009 saw further deterioration in our markets. See [Price trends for products](#).

Following the onset of the global financial crisis, our net income of \$1,637.4 million achieved in the nine months ended September 30, 2008 was partially offset by the net loss of \$496.9 million we incurred in the fourth quarter of 2008. Our steel and ferroalloys segments realized a net loss for the fourth quarter of 2008 \$404.1 million and \$270.1 million, respectively mainly due to foreign currency exchange losses due to revaluation of U.S. dollar denominated liabilities and significant inventories of raw material and unfinished products purchased and produced at pre-crisis prices.

**Table of Contents*****Trade and competition***

Mining products and many types of steel products are considered commodities and treated as fungible in the world markets. As such, we compete with steel producers and mining companies with operations in different countries. The main competitive advantages that steel producers can secure are based on quality and cost. Generally, steel producers in economically developed regions compete primarily based on quality of steel, while we and other steel producers in developing countries compete in the international market based primarily on lower production costs. With respect to our mining products, such as iron ore, nickel and coal, quality, production costs and transportation capabilities are key areas where companies seek a competitive advantage.

Because the production and consumption of steel are closely linked to economic development and industrial capacity in general, many countries enact measures to protect their domestic steel industries from international competition, particularly from countries with a lower average cost of production. Several key steel importing countries currently have import restrictions in place on steel products or intend to introduce them in the future. See **Risk Factors – Risks Relating to Our Business and Industry** We face numerous protective trade restrictions in the export of our steel products and ferroalloys, and we may face export duties in the future.

The E.U. has a quota system in place with respect to Russian steel imports, which affected our exports to ten countries in Central and Eastern Europe in 2008. Our sales into the E.U. constituted approximately 24% of our steel segment revenues and 37% of our steel segment export revenues in 2008. Excluding steel segment revenues from our Romanian entities and HBL Holding's sales, which are not subject to these import duties, our sales into the E.U. which were subject to such duties constituted approximately 3% of our steel segment revenues and 12% of our steel segment export revenues in 2008. In addition, the E.U. has imposed antidumping duties on certain of our exports. In February 2008, an antidumping duty in the amount of 17.8% was imposed on exports to the E.U. of ferrosilicon produced by our Bratsk Ferroalloy Plant for a period of five years. As we are seeking to expand our exports into the E.U., it is likely that our share of exports into the E.U. that will be subject to these trade restrictions will increase in future periods; however, we expect that increasing sales by our operations in Romania, further enhanced by our acquisition of Ductil Steel in April 2008, will help to mitigate the effect of E.U. trade restrictions on our steel products in the future.

At the same time, we are protected from competition from steel imports in Russia due to import tariffs that Russia has in place with respect to certain imported steel products. These tariffs generally amount to 5-15% of value. Almost all of our sales of steel products in Russia in 2008 were protected by these import tariffs. In January 2009, the Russian Government increased import duties on certain types of steel products (corrosion-resistant steel and some other steel products) from 5% to 15%. See **Risk Factors – Risks Relating to Our Business and Industry** We benefit from Russia's tariffs and duties on imported steel, which may be eliminated in the future.

***Consolidation trends in the steel and mining industries***

The steel industry has experienced a consolidation trend in recent years, which continued throughout 2006 to 2008. Key consolidations during this period included the acquisition by Mittal Steel Company N.V. ( **Mittal Steel** ) of Arcelor S.A. ( **Arcelor** ) in 2006 and the merger of Tata Steel Ltd ( **Tata Steel** ) and Corus Group plc ( **Corus** ) in 2007 (which was itself the result of a merger between British Steel Plc and Koninklijke Hoogovens N.V. in 2002).

The level of acquisition activity among steel companies fell in 2008 compared with the previous two years, but it was still a notable feature of the Chinese steel industry. Tangshan Iron and Steel Group merged with Handan Iron and Steel Group and formed the second largest Chinese steelmaker – Hebei Iron and Steel Group.

Spiralling raw materials prices in the first half of 2008 led to acquisitions of raw materials companies by steel producers. Nucor, the largest electric-arc furnace producer in the world, acquired five scrap recycling companies in 2008. Severstal acquired PBS Coal Company in 2008, which is expected to supply Severstal's North American steelmaking facilities with coking coal.

Recent and future consolidation in the steel industry should enable steel producers to maintain more consistent performance through cycles in the steel industry by achieving greater efficiency and economies of scale.

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We, along with other Russian steel producers, tend to focus on vertical integration rather than consolidation, which ensures access to a stable supply of raw materials, particularly coking coal and iron ore. Our vertical integration means that we are not as affected by tightening in the supply of raw materials and also provides us with the potential for upside gains on third-party sales by our mining business.

The mining industry has also experienced consolidation in recent years. Though BHP Billiton has abandoned its plans to acquire Rio Tinto, the world's three leading iron ore suppliers (BHP Billiton, Rio Tinto and Vale) are still looking for acquisition opportunities. In the third quarter of 2008, Teck Cominco acquired Fording Canadian Coal Trust and all of its assets. Teck now owns 100% of Elk Valley Coal, which has been renamed Teck Coal. This acquisition has resulted in the formation of the world's second largest metallurgical coal exporter. Consolidation among suppliers in the mining industry has led to a stronger bargaining position among mining companies vis-a-vis steel producers. As we are vertically integrated in both the upstream and downstream sides of the mining and steel businesses, we are not as affected by consolidation among suppliers.

Consolidation in the ferroalloys industry is primarily driven by the largest diversified mining companies, such as BHP Billiton, Rio Tinto, Vale and Xstrata, and large-scale international traders, such as Glencore. These companies are steadily looking to increase their resource base and find new growth opportunities.

***Price trends for products******Coking coal and steam coal***

The Japanese financial year ( JFY ) 2008/2009 contract prices for standard hard coking coal were settled at \$289 per tonne ( Free On Board (FOB) delivery terms from Australia) in April 2008, up from \$89-107 per tonne in 2006-2007. Substantial steel demand and production growth in the first half of 2008 coupled with coal supply shortage pushed hard coking coal spot prices to unprecedented level of around \$400 per tonne in the third quarter of 2008. The situation sharply changed by the end of third quarter 2008, when the financial crisis and uncertain economic outlook led to a decrease in coal demand, and spot hard coking coal prices fell to around \$100 per tonne by the end of 2008. The JFY 2009/2010 contract price for standard hard coking coal was settled at \$120 per tonne (FOB Australia), representing a 58% decrease from \$289 per tonne (FOB Australia) for the prior year.

Prices for steam coal generally increased during the 2006-2008 period under review, reaching a high of \$209 per tonne (CIF Amsterdam/Rotterdam/Antwerp) in July 2008 from a low of \$55 per tonne in January 2006. As the global financial crisis began in September 2008, demand for steam coal was suddenly reduced and spot prices fell to \$80 per tonne by the end of 2008. Steam coal price decreased further in the first quarter of 2009, when the price fell to \$60 per tonne (CIF Amsterdam/Rotterdam/Antwerp).

***Iron ore***

Iron ore prices increased by 82% during the 2006-2008 period under review, reaching a high price of \$89 per tonne (63% elemental iron, Carajas fines, FOB Brazil) in JFY 2008/2009 from a price of \$49 per tonne in JFY 2006/2007, according to industry publications. Prices increased generally due to buoyant demand and limited supply. Spot iron ore prices decreased substantially in the second half of 2008 due to the decline in global economic activity and reduced demand. The iron ore contract price for JFY 2009/2010 settled at \$61 per tonne, representing a 31% decrease from \$89 per tonne (63% elemental iron, Carajas fines, FOB Brazil).

***Nickel***

Nickel prices generally decreased during the 2006-2008 period under review. On the London Metal Exchange ( LME ) the cash nickel price decreased by 33% in December 2008 compared with January 2006. The cash price of nickel reached a high of \$54,150 per tonne in May 2007 and a low of \$9,050 per tonne in December 2008, according to the LME. The increase in 2006-2007 was due primarily to a nickel deficit in the world market caused by speculative trading on the LME and a decrease in world nickel inventories. The situation changed in the second half of 2007, when demand for nickel fell. Later on in 2008 the nickel price slipped further, driven by deterioration in the global economic environment. Nickel prices were volatile in the first quarter of 2009, varying in the range of \$9,405 to \$13,420 per tonne.

**Table of Contents***Ferrochrome*

Ferrochrome prices increased by 230% during the 2006-2008 period under review, reaching a high price of \$6,280 per tonne of chrome content (high carbon ferrochrome price in Europe, Delivered Duty Paid (DDP) delivery terms) in May 2008, according to MetalBulletin Research. Prices increased generally due to buoyant demand from stainless steel producers and limited supply. Ferrochrome prices decreased to \$2,810 per tonne of chrome content in the second half of 2008 due to reduced demand. Prices decreased further in the first quarter of 2009, falling to \$1,760 per tonne of chrome content.

*Ferrosilicon*

Ferrosilicon prices increased 2.1 times during the 2006-2008 period under review, reaching a high price of \$2,620 per tonne (ferrosilicon with 75% silicon content in Europe, DDP) in August 2008, according to MetalBulletin Research. Prices increased generally due to buoyant demand for steel, since ferrosilicon is an essential ingredient in the manufacture of all types of steel. Ferrosilicon prices decreased to \$1,615 per tonne by the end of 2008 due to reduced steel demand. Ferrosilicon prices decreased further to \$1,290 per tonne in the first quarter of 2009.

*Steel*

During the 2006-2008 period under review, steel prices were generally increasing, with the regular seasonal volatility. The price of rebar increased by 300% from January 2006 through July 2008, reaching a high price of \$1,305 per tonne (rebar, Russia domestic market, ex-warehouse), and then fell to a low price of \$410 per tonne in December 2008, according to Metal-Courier. The price increase during this period was due to a strong global demand and raw materials costs increase, particularly in the first half of 2008. The domestic price for rebar improved to \$425 per tonne in the first quarter of 2009, driven by a slight uptick in activity by traders replenishing inventories on an expectation of demand recovery during the summer construction season.

*Freight costs*

In recent years, ocean freight charges have been volatile and generally increased prior to the global financial crisis due to worldwide capacity issues and localized logistical bottlenecks. During 2008, freight rates peaked at \$80 per tonne (Queensland to Rotterdam, Capesize vessels) in June 2008 and fell to a low of \$12 per tonne in December 2008 and January 2009, according to industry publications.

Freight costs are a significant concern for Russian steel producers and mining companies, as distances in Russia are vast and major steel producing and mining areas tend to be located far from developed year-round port facilities. In addition to geographical challenges, domestic Russian rail freight shipments are carried out by Russian Railways, a government-controlled monopoly, such that there is no downward pressure on rail freight rates due to market competition, unlike in countries where there are multiple freight carriers that compete based on price.

*Exchange rates*

The escalation in the value of the U.S. dollar versus many other currencies, a trend which started in the fourth quarter of 2008, has resulted in decreased prices in U.S. dollar terms of coking and steam coal, iron ore, nickel and steel products that we price in other currencies. The U.S. dollar continued to grow against currencies of the jurisdictions in which we have operations, including the Russian ruble, the Romanian lei, the Lithuanian litas, the Bulgarian lev and the Kazakhstan tenge. In the first quarter of 2009, the U.S. dollar's value has decreased but remained significantly higher than in 2007 and the first half of 2008.

Our products are typically priced in rubles for Russian and CIS sales and in U.S. dollars or euros for international sales. Our direct costs, including raw materials, labor and transportation costs, are largely incurred in rubles, while other costs, such as interest expense, are incurred in rubles, euros and U.S. dollars. The mix of our revenues and costs is such that depreciation in real terms of the ruble against the U.S. dollar tends to result in a decrease in our costs relative to our revenues, while appreciation of the ruble against the U.S. dollar in real terms tends to result in an increase in our costs relative to our revenues.

**Table of Contents****Results of Operations**

The following table sets forth our consolidated statement of income data for the years ended December 31, 2008, 2007 and 2006.

Revenues	Year Ended December 31,					
	2008		2007		2006	
	Amount	% of Revenues (In thousands of U.S. dollars, except for percentages)	Amount	% of Revenues	Amount	% of Revenues
Revenue, net	9,950,705	100.0%	6,683,842	100.0%	4,397,811	100.0%
Cost of goods sold	(5,260,108)	(52.9)%	(4,166,864)	(62.3)%	(2,860,224)	(65.0)%
Gross profit	4,690,597	47.1%	2,516,978	37.7%	1,537,587	35.0%
Selling, distribution and operating expenses	(2,134,328)	(21.4)%	(1,119,385)	(16.7)%	(811,889)	(18.5)%
Operating income	2,556,269	25.7%	1,397,593	20.9%	725,698	16.5%
Other (expense) income, net	(1,208,001)	(12.1)%	(12,146)	(0.2)%	139,135	3.2%
Income before income tax, minority interest and discontinued operations	1,348,268	13.5%	1,385,447	20.7%	864,833	19.7%
Income tax expense	(118,887)	(1.2)%	(356,320)	(5.3)%	(230,599)	(5.2)%
Minority interest in income of subsidiaries	(88,837)	(0.9)%	(116,234)	(1.7)%	(31,528)	(0.7)%
Income from continuing operations	1,140,544	11.5%	912,893	13.7%	602,706	13.7%
Income from discontinued operations, net of tax		0.0%	158	0.0%	543	0.0%
Net income	1,140,544	11.5%	913,051	13.7%	603,249	13.7%

***Year ended December 31, 2008 compared to year ended December 31, 2007****Net revenues*

Consolidated net revenues increased by \$3,266.9 million, or 48.9%, to \$9,950.7 million in the year ended December 31, 2008, from \$6,683.8 million in the year ended December 31, 2007.

Across our segments, our acquisitions in 2008 and 2007 led to higher consolidated net revenues due to higher production and sales volumes arising primarily from the consolidation of the results of operations of acquired companies. Approximately 48.4%, or \$1,580.8 million, of the increase in our consolidated net revenues in the year ended December 31, 2008 compared to the year ended December 31, 2007 was due to the consolidation of companies

acquired during the year, including \$1,277.1 million in respect of Yakutugol, \$68.2 million in respect of chrome sales of Tikhvin Ferroalloy Plant, \$203.0 million in respect of steel products of Ductil Steel and \$32.5 million in respect of steel products of the HBL Holding companies. The remainder of our increase in revenues was due to organic growth, which was driven largely by price increases and changes in the product mix towards higher value-added products.

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The following table sets forth our net revenues by segment:

	<b>Year Ended December 31,</b>	
	<b>2008</b>	<b>2007</b>
	<b>(In thousands of U.S. dollars, except percentages)</b>	
<b>Mining segment</b>		
To third parties	3,333,406	1,372,508
To ferroalloys segment	11,271	12,051
To power segment	27,695	11,272
To steel segment	659,595	575,138
Total	4,031,967	1,970,969
<b>Steel segment</b>		
To third parties	5,495,139	4,306,875
To ferroalloys segment	96,752	79,135
To power segment	174,814	22,509
To mining segment	7,014	5,973
Total	5,773,719	4,414,492
<b>Ferroalloys segment</b>		
To third parties	434,017	501,143
To steel segment	150,614	135,513
Total	584,631	636,656
<b>Power segment</b>		
To third parties	688,143	503,316
To steel segment	257,368	38,587
To ferroalloys segment	29,468	26,225
To mining segment	53,131	30,387
Total	1,028,110	598,515
Eliminations	1,467,722	936,790
Consolidated revenues	9,950,705	6,683,842
% from mining segment	33.5%	20.5%
% from steel segment	55.2%	64.4%
% from ferroalloys segment	4.4%	7.5%
% from power segment	6.9%	7.5%

***Mining segment***

Our total mining segment sales increased by \$2,061.0 million, or 104.6%, to \$4,032.0 million in the year ended December 31, 2008 from \$1,971.0 million in the year ended December 31, 2007.

Coking coal concentrate sales to third parties increased by \$1,238.0 million, or 198.7%, to \$1,860.9 million in the year ended December 31, 2008 from \$622.9 million in the year ended December 31, 2007 as a result of a sales price increase of \$995.6 million and a sales volume increase of \$242.4 million. The sales price increase is explained by the sharp increase in international coking coal prices through the second quarter of 2008, when the premium hard coking coal price rose more than 300% to \$300 per tonne. The volume of coking coal concentrate sold to third parties increased by 2,342 thousand tonnes, or 38.9%, to 8,360 thousand tonnes in the year ended December 31, 2008 from 6,018 thousand tonnes in the year ended December 31, 2007. The increase in sales volumes during the period was principally due to the fact that the results of operations of Yakutugol were reflected in our consolidated results of operations in the year ended December 31, 2008 for the full year, while in the year ended December 31, 2007 these results were included since October 2007 only. If Yakutugol's results of operations are excluded, our

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coking coal volumes sold in the year ended December 31, 2008 would have decreased by 9.7% due to Southern Kuzbass Coal Company's decrease in production volumes. Pursuant to a directive from the FAS dated August 14, 2008, we entered into long-term coking coal supply contracts with some of our major domestic customers. These new contracts provide for the supply of coking coal concentrate under a fixed price based on the price of premium hard coking coal under one-year contracts under FOB terms from Australian ports, excluding the costs of transshipment and rail transportation with the application of a coefficient representing the quality of the coal concentrate. See Item 4. Information on the Company Mining Business Marketing and distribution Domestic sales. Previously, the delivery terms for most of our major domestic customers provided for sale at spot market prices.

Coking coal concentrate supplied to our steel segment increased by \$87.9 million, or 21.6%, to \$495.8 million in the year ended December 31, 2008 from \$407.9 million in the year ended December 31, 2007. Of this increase, \$219.7 million was due to an increase in sales prices that was partially offset by a decrease in sales volumes of \$131.8 million. The decrease in sales volumes is explained by the shift of purchases of coking coal by Mechel-Coke and Moscow Coke and Gas Plant towards external suppliers (because we focused on exports of coking coal due favorable market conditions in the first three quarters of 2008, resulting in approximately 45.3% of our coking coal sales volume coming from exports) and a decrease in coke and pig iron production in the fourth quarter of 2008 due to reduced demand for steel products caused by the global financial crisis.

Steam coal and steam coal concentrate sales to third parties increased by \$488.7 million, or 112.0%, to \$925.0 million in the year ended December 31, 2008 from \$436.3 million in the year ended December 31, 2007, where \$409.4 million of the increase was due to an increase in sales prices and \$79.3 million was due to an increase in sales volume. The increase in sales volumes during the period was principally due to the fact that the results of operations of Yakutugol were reflected in our consolidated results from the fourth quarter of 2007. If Yakutugol's results of operations are excluded, our steam coal volumes sold in 2008 would have decreased by 17.5%, the net effect of an increase in the volume of steam coal supplied to the power segment and a decrease in export demand in the fourth quarter of 2008. Export prices for steam coal and steam coal concentrate rose sharply in the second quarter of 2008 as a result of increasing demand, especially in Asia, and limited supply growth from major exporting countries. Domestic prices increased due to growing production costs and global steam coal price increases.

Sales of steam coal supplied to the power and ferroalloys segments increased by \$31.3 million, or 169.0%, to \$49.9 million in the year ended December 31, 2008 from \$18.5 million in the year ended December 31, 2007, as a result of sales price increases amounting to \$9.3 million and sales volume increases amounting to \$22.1 million. The increase in sales volumes is explained by the fact that Southern Kuzbass Power Plant was consolidated in our financial statements from April 2007, as well as by the increase in electricity sales by Mechel-Energo, to which co-generation units from Chelyabinsk Metallurgical Plant and Southern Kuzbass Coal Company were transferred in the first quarter of 2008.

Sales of iron ore to third parties increased by \$125.8 million, or 58.9%, to \$339.4 million in the year ended December 31, 2008 from \$213.6 million in the year ended December 31, 2007 as a result of a sales price increase of \$93.7 million and a sales volume increase of \$32.2 million. The sales price increase is explained by stable iron ore demand growth and limited supply in the first half of 2008, especially in Asia. The sales volume increase is explained by our increased iron ore export deliveries to China.

Supplies of iron ore by our mining segment to our steel segment decreased by \$4.2 million, or 2.7%, to \$148.9 million in the year ended December 31, 2008 from \$153.1 million in the year ended December 31, 2007 as a result of a sales volume decrease amounting to \$22.8 million partially offset by sales price increases amounting to \$18.6 million. The decrease in sales volumes is explained by the shift of purchases of iron ore by Chelyabinsk Metallurgical Plant towards external suppliers (because we focused on exports of iron ore due the favorable market conditions in the first three quarters of 2008) and the decrease in pig iron production in the fourth quarter of 2008 due to reduced demand

for steel products caused by the global financial crisis.

Excluding intersegment sales, export sales were 60.6% of mining segment sales in the year ended December 31, 2008, compared to 40.2% in the year ended December 31, 2007. The increase in the proportion of our export sales was due to the higher export volumes of coking coal, steam coal and iron ore due to higher sales prices on export markets. Average steam coal sales export prices on Free Carrier (FCA) delivery terms in 2008 were

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\$102.7 per tonne in comparison with \$43.9 per tonne for average domestic sales prices on FCA basis. Average coking coal sales export prices on FCA basis in 2008 were \$221.2 per tonne in comparison with \$179.4 per tonne for average domestic sales prices on FCA basis. Average iron ore sales export prices on FCA basis in 2008 were \$108.6 per tonne in comparison with \$86.6 per tonne for average domestic sales prices on FCA basis.

***Steel segment***

Our steel segment revenues increased by \$1,359.2 million, or 30.8%, to \$5,773.7 million in the year ended December 31, 2008 from \$4,414.5 million in the year ended December 31, 2007. The increase in steel segment revenues was primarily due to the following increases:

Coke sales increased by \$128.7 million, or 51.7%, to \$377.5 million in the year ended December 31, 2008 from \$248.8 million in the year ended December 31, 2007 as a result of sales price increases amounting to \$172.6 million partially offset by sales volume decreases amounting to \$43.9 million. The increase in sales prices was driven by the increase in coking coal prices which is the key raw material in the production of coke. The sales volume decrease is explained by the decrease in production volumes of Moscow Coke and Gas Plant and Mechel-Coke in response to weakened demand due to the global financial crisis.

Rebar sales increased by \$615.7 million, or 60.5%, to \$1,632.8 million in the year ended December 31, 2008 from \$1,017.1 million in the year ended December 31, 2007 as a result of sales price increases amounting to \$475.6 million and sales volume increases amounting to \$140.1 million. The increase in sales prices was driven by a sharp increase in steelmaking raw materials prices and were supported by strong demand in first nine months of 2009. The increase in sales volumes is explained by the acquisition of Ductil Steel in April 2008.

Wire-rod sales increased by \$50.2 million, or 26.4%, to \$240.3 million in the year ended December 31, 2008 from \$190.1 million in the year ended December 31, 2007 as a result of sales price increases amounting to \$61.8 million offset by sales volume decreases amounting to \$11.6 million. The increase in sales prices was driven by the increase in the prices of raw materials used in steelmaking. The decrease in sales volumes is explained by an increase in the share of high value-added products produced from wire-rod in our product portfolio.

Low alloyed engineering steel sales increased by \$171.9 million, or 40.3%, to \$598.3 million in the year ended December 31, 2008 from \$426.3 million in the year ended December 31, 2007, as a result of sales price increases amounting to \$167.5 and sales volume increases amounting to \$4.4 million. The increase in sales prices was driven by a sharp increase in the prices of raw materials used in steelmaking. The increase in sales volumes is explained by demand growth in the first three quarters of 2008.

Carbon and low-alloyed forgings sales increased by \$20.3 million, or 23.3%, to \$107.2 million in the year ended December 31, 2008 from \$86.9 million in the year ended December 31, 2007, as a result of sales price increases amounting to \$13.7 million and sales volume increases amounting to \$6.6 million. The increase in sales prices was driven by the substantial increase in the prices of raw materials used in steelmaking. The increase in sales volumes is explained by the increased demand in export markets in the first half of 2008.

Stampings sales increased by \$34.6 million, or 17.2%, to \$236.1 million in the year ended December 31, 2008 from \$201.4 million in the year ended December 31, 2007 as a result of sales price increases amounting to \$56.1 million partially offset by sales volume decreases amounting to \$21.5 million. The increase in sales prices was driven by the increase in the prices of raw materials used in steelmaking. The decrease in sales volumes is explained by the demand slump in the fourth quarter of 2008.

Wire sales increased by \$225.7 million, or 54.4%, to \$640.2 million in the year ended December 31, 2008 from \$414.5 million in the year ended December 31, 2007 as a result of sales price increases amounting to \$190.7 million and sales volume increases amounting to \$35.0 million. The increase in sales prices was driven by the increase in the prices of raw materials used in steelmaking. The increase in sales volumes is explained in part by our acquisition of Ductil Steel in April 2008, and in part by an increase in the share of high value-added products in our portfolio.

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Excluding intersegment sales, export sales comprised 25.4% of steel segment sales in the year ended December 31, 2008, compared to 31.5% in the year ended December 31, 2007. The decrease in the proportion of our export sales was largely due to favorable domestic pricing and robust domestic steel consumption growth which exceeded the Russian steel industry's increase in production volumes.

***Ferroalloys segment***

Nickel sales to third parties decreased by \$187.6 million, or 40.0%, to \$281.3 million in the year ended December 31, 2008 from \$468.9 million in the year ended December 31, 2007, mainly as a result of sales price decreases amounting to \$183.6 million. Average sales prices decreased by \$14,126.9 from \$35,775.2 per tonne in 2007 to \$21,648.3 per tonne in 2008.

Nickel supplies to the steel segment decreased by \$36.6 million, or 29.1%, to \$89.2 million in the year ended December 31, 2008 from \$125.8 million in the year ended December 31, 2007, mostly due to a decrease in sales prices. There were no significant changes in intersegment sales volumes.

Ferrosilicon sales to third parties increased by \$50.3 million, or 173.4%, to \$79.3 million in the year ended December 31, 2008 from \$29.0 million in the year ended December 31, 2007, mainly as a result of sales price increases of \$22.5 million as well as sales volume increases amounting to \$27.7 million. The increase in sales volume is explained by the fact that Bratsk Ferroalloy Plant was consolidated in our financial statements only since August 2007. The increase in sales prices is explained by the sharp increase in international ferrosilicon prices in the first half of 2008.

Ferrosilicon supplies to our steel segment increased by \$29.8 million, or 308.1%, to \$39.5 million in the year ended December 31, 2008 from \$9.7 million in the year ended December 31, 2007, as a result of sales price increases amounting to \$11.1 million and sales volume increases amounting to \$18.7 million. The increase in sales volumes is explained by the fact that Bratsk Ferroalloy Plant was consolidated in our financial statements only since August 2007.

Chrome sales to third parties were \$68.2 million in the year ended December 31, 2008 compared to none in the year ended December 31, 2007, as a result of our acquisition of Tikhvin Ferroalloy Plant in April 2008.

Chrome supplies to the steel segment were \$21.9 million in the year ended December 31, 2008 compared to none in the year ended December 31, 2007, as a result of our acquisition of Tikhvin Ferroalloy Plant in April 2008.

Excluding intersegment sales, export sales were 76.8% of ferroalloys segment sales in the year ended December 31, 2008, compared to 93.7% in the year ended December 31, 2007. The decrease in the proportion of our export sales was due to the inclusion of Bratsk Ferroalloy Plant in the reporting segment beginning with August 2007, because Bratsk Ferroalloy Plant's export sales are a small proportion of its overall sales, with domestic sales representing 92.0% of its overall sales in the year ended December 31, 2008.

***Power segment***

Our power segment revenues increased by \$429.6 million, or 71.8%, to \$1,028.1 million in the year ended December 31, 2008 from \$598.5 million in the year ended December 31, 2007. The increase in energy segment revenues is mostly explained by the fact that Southern Kuzbass Power Plant and Kuzbass Power Sales Company are included in our financial results since the second quarter of 2007.

Prior to our acquisition of Southern Kuzbass Power Plant and Kuzbass Power Sales Company in the second quarter of 2007, our power segment consisted of intersegment and third-party sales of electricity produced by co-generation units burning blast furnace gas and coal gas produced as a byproduct of industrial processes at our Chelyabinsk Metallurgical Plant, Moscow Coke and Gas Plant, Southern Kuzbass Coal Company and Mechel-Coke.

Southern Kuzbass Power Plant contributed \$18.2 million to the power segment revenues through power generation capacity sales to third parties in the year ended December 31, 2008.

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Power supplies to the steel segment increased by \$218.8 million, or 567.0%, to \$257.4 million in the year ended December 31, 2008 from \$38.6 million in the year ended December 31, 2007, as a result of an increase in electricity sales by Mechel-Energo, to which co-generation units from Chelyabinsk Metallurgical Plant were transferred in the first quarter of 2008.

*Cost of goods sold and gross profit*

Consolidated cost of goods sold was 52.9% of consolidated revenues in the year ended December 31, 2008, as compared to 62.3% of consolidated revenues in the year ended December 31, 2007, resulting in an increase in consolidated gross margin to 47.1% in the year ended December 31, 2008 from 37.7% for the year ended December 31, 2007. Cost of goods sold primarily consists of costs relating to raw materials (including products purchased for resale), direct payroll, depreciation and energy. The table below sets forth cost of goods sold and gross margin by segment for the years ended December 31, 2008 and 2007, including as a percentage of segment revenues.

<b>Cost of Goods Sold and Gross Margin by Segment</b>	<b>Year Ended December 31, 2008</b>		<b>Year Ended December 31, 2007</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Mining segment</b>				
Cost of goods sold	1,229,631	30.5%	1,008,485	51.2%
Gross margin	2,802,336	69.5%	962,484	48.8%
<b>Steel segment</b>				
Cost of goods sold	4,219,344	73.1%	3,374,420	76.4%
Gross margin	1,554,375	26.9%	1,040,072	23.6%
<b>Ferroalloys segment</b>				
Cost of goods sold	571,162	97.7%	253,725	39.9%
Gross margin	13,469	2.3%	382,931	60.1%
<b>Power segment</b>				
Cost of goods sold	714,094	69.5%	393,153	65.7%
Gross margin	314,016	30.5%	205,362	34.3%

*Mining segment*

Mining segment cost of goods sold increased by \$221.1 million, or 21.9%, to \$1,229.6 million in the year ended December 31, 2008 from \$1,008.5 million in the year ended December 31, 2007. Mining segment gross margin increased from 48.8% in the year ended December 31, 2007 to 69.5% in the year ended December 31, 2008.

The increase in the mining segment's gross margin percentage is explained by increases in coking coal, steam coal and iron ore sales prices both on export and domestic markets. At the same time, coking coal concentrate production cash costs per tonne at Southern Kuzbass Coal Company increased by 42.5% due to an increase in the prices of spare parts and fuel, an increase in heat prices following the transfer of co-generation units from Southern Kuzbass Coal Company to Mechel-Energo and an increase in payroll expenses due to salary indexation, as well as increase in fixed costs per tonne due to a decrease in production volumes. Production cash costs of coking coal at Yakutugol decreased by 6.2% due to implementation of a cost cutting strategy following our acquisition of Yakutugol in October 2008. The production cash costs of steam coal at Southern Kuzbass Coal Company increased by 17.4% due to the same reasons

as for the increase in production cash costs of coking coal and coking coal concentrate. The production cash costs of steam coal at Yakutugol decreased by 30.4% due to the same reasons as for coking coal and coking coal concentrate. Production cash costs of iron ore increased by 9.9% due to increases in electricity prices, production personnel wages and the prices of mining supplies used in iron ore production, such as spare parts, fuel and explosives.

***Steel segment***

Steel segment cost of goods sold increased by \$844.9 million, or 25.0%, to \$4,219.3 million in the year ended December 31, 2008 from \$3,374.4 million in the year ended December 31, 2007. Steel segment cost of goods sold

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was 73.1% of the segment's revenues in the year ended December 31, 2008, as compared to 76.4% in the year ended December 31, 2007, resulting in an increase in gross margin from 23.6% to 26.9%. Such increase is attributable to the increase in sales prices, as well as the decrease in the price of nickel, a major raw material in stainless steel production.

***Ferroalloys segment***

Ferroalloys segment cost of goods sold increased by \$317.4 million, or 125.1%, to \$571.2 million in the year ended December 31, 2008 from \$253.7 million in the year ended December 31, 2007. Ferroalloys segment cost of goods sold was 97.7% of the segment's revenues in the year ended December 31, 2008, as compared to 39.9% in the year ended December 31, 2007, resulting in a decrease in gross margin from 60.1% to 2.3%. Such decrease is attributable to the sharp decrease in nickel and chrome sales prices on the back of growing coke prices (coke is one of the major raw materials in nickel and chrome production) as well as the effect of write-down of inventory to the market value and provision for obsolete stock of \$94.7 million.

***Power segment***

Power segment cost of goods sold increased by \$320.9 million, or 81.6%, to \$714.1 million in the year ended December 31, 2008 from \$393.2 million in the year ended December 31, 2007. Power segment gross margin decreased from 34.3% in the year ended December 31, 2007 to 30.5% in the year ended December 31, 2008. Such decrease is explained by an increase in steam coal sales prices (steam coal is the major raw material in electricity production) that exceeded the growth of electricity sales prices.

***Selling, distribution and operating expenses***

Selling, distribution and operating expenses increased by \$1,014.9 million, or 90.7%, to \$2,134.3 million in the year ended December 31, 2008 from \$1,119.4 million in the year ended December 31, 2007 mainly due to an increase in transportation expenses in the steel and mining segments, general and administrative expenses in the mining segment and bad debt allowance expenses in the steel segment, as explained below. As a percentage of consolidated revenues, selling, distribution and operating expenses increased to 21.4% in the year ended December 31, 2008, as compared to 16.7% in the year ended December 31, 2007. Our selling, distribution and operating expenses consist primarily of selling and distribution expenses, taxes other than income tax, loss on write-offs of property, plant and equipment, allowance for doubtful accounts and general, administrative and other operating expenses. The table below sets forth these costs by segment for the years ended December 31, 2008 and 2007, including as a percentage of segment revenues.

<b>Selling, Distribution and Operating Expenses by Segment</b>	<b>Year Ended December 31, 2008</b>		<b>Year Ended December 31, 2007</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Mining segment</b>				
Selling and distribution expenses	678,070	16.8%	241,090	12.2%
Taxes other than income tax	60,450	1.5%	3,815	0.2%
Allowance for doubtful accounts	13,564	0.3%	(1,441)	(0.1)%

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Accretion expense	2,530	0.1%	1,071	0.1%
Loss on write-off property, plant and equipment	796	0.0%		
General, administrative and other operating expenses	246,386	6.1%	146,480	7.4%
Total	1,001,796	24.8%	391,015	19.8%

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<b>Selling, Distribution and Operating Expenses by Segment</b>	<b>Year Ended December 31, 2008</b>		<b>Year Ended December 31, 2007</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Steel segment</b>				
Selling and distribution expenses	406,687	7.0%	194,855	4.4%
Taxes other than income tax	49,421	0.9%	71,243	1.6%
Loss on write off of property, plant and equipment	3,527	0.0%		0.0%
Accretion expense	2,792	0.0%	1,708	0.0%
Allowance for doubtful accounts	78,031	1.4%	3,602	0.1%
General, administrative and other operating expenses	243,478	4.2%	231,403	5.2%
<b>Total</b>	<b>783,936</b>	<b>13.6%</b>	<b>502,811</b>	<b>11.4%</b>
<b>Ferroalloys segment</b>				
Selling and distribution expenses	10,185	1.7%	3,400	0.5%
Taxes other than income tax	3,437	0.6%	7,528	1.2%
Allowance for doubtful accounts	2,232	0.4%	2	0.0%
Accretion expense	591	0.1%	322	0.1%
General, administrative and other operating expenses	47,541	8.1%	21,572	3.4%
<b>Total</b>	<b>63,986</b>	<b>10.9%</b>	<b>32,824</b>	<b>5.2%</b>
<b>Power segment</b>				
Selling and distribution expenses	254,047	24.7%	182,466	30.5%
Taxes other than income tax	3,282	0.3%	1,408	0.2%
Allowance for doubtful accounts	9,805	1.0%	(752)	(0.1)%
Accretion expense	165	0.0%		0.0%
General, administrative and other operating expenses	17,311	1.7%	9,613	1.6%
<b>Total</b>	<b>284,610</b>	<b>27.7%</b>	<b>192,735</b>	<b>32.2%</b>

**Mining segment**

Selling and distribution expenses consisted almost entirely of transportation expenses related to our selling activities, and increased by \$437.0 million in line with sales volume increases in 2008. As a percentage of mining segment revenues, selling and distribution expenses increased from 12.2% to 16.8% due to an increase in the share of sales on delivery terms where transportation expenses are included in the final sales prices and therefore are incurred by the seller.

Taxes other than income tax include property and land taxes, as well as other taxes. Taxes other than income tax increased by \$56.6 million, or 1,484.4%, to \$60.4 million in the year ended December 31, 2008 from \$3.8 million in the year ended December 31, 2007. The increase was mainly due to the recognition of \$34.0 million in tax penalties

and fines imposed by FAS under antimonopoly legislation on Mechel Trading House, Southern Kuzbass Coal Company and Yakutugol. In addition, prior period taxes were lower due to the reversal of a \$25.7 million tax liability related to Korshunov Mining Plant in 2007 in respect of mineral extraction taxes and social taxes for prior periods. On December 18, 2007, the Supreme Arbitration Court of the Russian Federation issued an order in our favor that clarified an aspect of tax law that was previously uncertain, resulting in a reduction in our mineral extraction tax liability for the years 2003-2007.

Allowance for doubtful accounts increased by \$15.0 million, to a \$13.6 million expense in the year ended December 31, 2008 from income of \$1.4 million in the year ended December 31, 2007, due to the increased exposure to losses on our accounts receivable because of the global financial crisis. In accordance with our

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accounting policy we provision for bad debts by applying specific rates to overdue accounts receivable of our companies depending on the history of cash collections and future expectations of conditions that might impact the collectability of accounts of each our companies. As in the fourth quarter of 2008 the overdue balances increased, the allowance increased as well.

Loss on write-off of property, plant and equipment was \$0.8 million compared to none in the year ended December 31, 2007. This is due to the write-off of the construction-in-progress objects that are not planned for further use in production process at Southern Kuzbass Coal Company.

General, administrative and other expenses which consist of payroll and payroll taxes, depreciation, rent and maintenance, legal and consulting expenses, office overhead and other expenses, increased by \$99.9 million, or 68.2%, to \$246.4 million in the year ended December 31, 2008 from \$146.5 million in the year ended December 31, 2007. The overall increase in general, administrative and other expenses can be explained by the inclusion of Yakutugol in the mining segment since October 2007. Salaries and related social taxes increased by \$56.8 million, or 74.0%, to \$133.6 million in the year ended December 31, 2008 from \$76.7 million in the year ended December 31, 2007, mainly due to indexation of salary rates to inflation at our production companies and due to the Yakutugol acquisition in the amount of \$38.0 million. Legal and consulting fees and insurance services increased by \$4.5 million, or 42.9%, to \$15.0 million in the year ended December 31, 2008 from \$10.5 million in the year ended December 31, 2007, due to increases in consulting fees. Rent and maintenance, business travel expenses, bank charges and office expenses increased by \$19.8 million, or 123.4%, to \$35.9 million in the year ended December 31, 2008 from \$16.1 million in the year ended December 31, 2007, and depreciation increased by \$5.7 million, or 119.8%, to \$10.5 million in the year ended December 31, 2008 from \$4.8 million in the year ended December 31, 2007, mainly due to the Yakutugol acquisition effect. Social expenses decreased by \$3.1 million, or 12.3%, to \$22.3 million in the year ended December 31, 2008 from \$25.4 million in the year ended December 31, 2007, mainly due to the effect of the ruble depreciation. Other administrative and operating expenses increased by \$16.2 million due to the Yakutugol acquisition.

***Steel segment***

Selling and distribution expenses for our steel segment consisted almost entirely of transportation expenses related to our selling activities. Such expenses increased by \$211.8 million, or 108.7%, to \$406.7 million in the year ended December 31, 2008 from \$194.9 million in the year ended December 31, 2007 and increased as a percentage of steel segment revenues from 4.4% in the year ended December 31, 2007 to 7.0% in the year ended December 31, 2008. The increase is mainly explained by an increase of the share of sales on delivery terms where transport expenses are included in the final sales prices and therefore are incurred by the seller.

Taxes other than income tax decreased by \$21.8 million, or 30.6%, to \$49.4 million in the year ended December 31, 2008 from \$71.2 million in the year ended December 31, 2007. As a percentage of segment revenues, these taxes decreased from 1.6% to 0.9%. Property and land taxes increased by \$2.7 million, or 6.0%, to \$47.5 million in the year ended December 31, 2008 from \$44.8 million in the year ended December 31, 2007, due to an increase in the property tax base (as a result of putting new fixed assets into operation). At the same time, in the year ended December 31, 2007, we incurred \$10.1 million in tax penalties and fines as a result of prior period tax audits at our Chelyabinsk Metallurgical Plant. The remaining part of the decrease of \$14.5 million is attributed mainly to a decrease in non-reimbursable VAT expenses at Chelyabinsk Metallurgical Plant and tax expense accrued at Mechel Campia Turzii and Mechel Trading House.

Allowance for doubtful accounts increased by \$74.4 million, or 2,066.2%, to \$78.0 million in the year ended December 31, 2008 from \$3.6 million in the year ended December 31, 2007, due to increased exposure to losses on our accounts receivable because of the global financial crisis. A substantial portion of such increase is attributable to

several customers experiencing liquidity problems, the most significant of which were GAZ Group, Metalltrade OOO, Stupinsk Metallurgical Company OAO.

Loss on write-off of property, plant and equipment was \$3.3 million compared to none in the year ended December 31, 2007. All of this amount relates to the write-off of the construction-in-progress objects that are not planned for further use in the production process at Chelyabinsk Metallurgical Plant.

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General, administrative and other expenses, increased by \$12.1 million, or 5.2%, to \$243.5 million in the year ended December 31, 2008 from \$231.4 million in the year ended December 31, 2007, and decreased as a percentage of segment revenues from 5.2% in the year ended December 31, 2007, to 4.2% in the year ended December 31, 2008. Payroll and related social taxes decreased by \$2.2 million, or 2.0%, to \$109.0 million in the year ended December 31, 2008 from \$111.2 million in the year ended December 31, 2007 due to the reduction of the duration of the working day at our companies in the last quarter of 2008. Social expenses (including pension obligations) decreased by \$1.0 million, or 4.5%, to \$22.2 million in the year ended December 31, 2008 from \$23.3 million in the year ended December 31, 2007, mainly due to ruble depreciation. Rent and maintenance, business travel expenses, bank charges and office expenses decreased by \$0.9 million, or 2.6%, to \$35.0 million in the year ended December 31, 2008 from \$35.9 million in the year ended December 31, 2007, primarily due to the effect of cost cutting measures implemented at our companies. Professional expenses, which include auditing, accounting, legal and engineering fees, and insurance services decreased by \$1.3 million, or 6.9%, to \$17.2 million in the year ended December 31, 2008 from \$18.4 million in the year ended December 31, 2007, primarily due to an decrease in insurance expenses as a result of cost-cutting measures implemented at our companies. Other administrative and operating expenses increased by \$17.5 million, or 41.1%, to \$60.2 million in the year ended December 31, 2008 from \$42.7 million in the year ended December 31, 2007, mainly due to acquisition, and an overall increase of segment activities in the first half of 2008.

***Ferroalloys segment***

Selling and distribution expenses, consisting almost entirely of transportation expenses related to our selling activities, increased by \$6.8 million, or 199.6%, to \$10.2 million in the year ended December 31, 2008 from \$3.4 million in the year ended December 31, 2007, and increased as a percentage of segment revenues from 0.5% in the year ended December 31, 2007, to 1.7% in the year ended December 31, 2008.

Taxes other than income tax decreased by \$4.1 million, or 54.3%, to \$3.4 million in the year ended December 31, 2008 from \$7.5 million in the year ended December 31, 2007, and decreased as a percentage of segment revenues from 1.2% in the year ended December 31, 2007 to 0.6% in the year ended December 31, 2008. The decrease in tax expenses is primarily due to the \$2.1 million reduction in income tax accruals for 2005, 2006 and 2007 by Southern Urals Nickel Plant because gains from forgiveness of tax fines and penalties can be excluded from taxable profit. Property and land taxes amounted to \$4.8 million in the year ended December 31, 2008, representing an increase of \$1.8 million, or 63.3%, from \$2.9 million in the year ended December 31, 2007, and were due to the Oriel Resources acquisition in April 2008 and the inclusion of Bratsk Ferroalloy Plant in August 2007.

Allowance for doubtful accounts increased to \$2.2 million in the year ended December 31, 2008 from \$1.9 thousand in the year ended December 31, 2007, due to the increased exposure to losses on our accounts receivable because of customers liquidity problems caused by the global financial crisis.

General, administrative and other expenses increased by \$26.0 million, or 120.4%, to \$47.5 million in the year ended December 31, 2008 from \$21.6 million in the year ended December 31, 2007, and increased as a percentage of segment revenues from 3.4% in the year ended December 31, 2007, to 8.1% in the year ended December 31, 2008. The overall increase of general, administrative and other expenses in this segment was due to acquisitions.

***Power segment***

Selling and distribution expenses consisted almost entirely of electricity transmission costs incurred by our Kuzbass Power Sales Company for usage of the power grid, over which electricity is distributed to end consumers. These costs are incurred by all power distribution companies under agreements between such companies and the grid operator. These expenses increased by \$71.6 million, or 39.2%, to \$254.0 million in the year ended December 31, 2008 from \$182.5 million in the year ended December 31, 2007 due to the inclusion of Kuzbass Power Sales Company in the

power segment since June 2007. These costs decreased as a percentage of segment revenues because of an increase in electricity prices in 2008 in comparison with 2007 due to the ongoing liberalization of the Russian electricity market.

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Taxes other than income tax increased by \$1.9 million, or 133.0%, to \$3.3 million in the year ended December 31, 2008 from \$1.4 million in the year ended December 31, 2007. As a percentage of segment revenues, these taxes increased from 0.2% to 0.3%.

Allowance for doubtful accounts increased by \$10.6 million, to a \$9.8 million expense in the year ended December 31, 2008 from \$0.8 million income in the year ended December 31, 2007, due to the increased exposure to losses on our accounts receivable because of the global financial crisis.

General, administrative and other expenses increased by \$7.7 million, or 80.1%, to \$17.3 million in the year ended December 31, 2008 from \$9.6 million in the year ended December 31, 2007, and increased as a percentage of segment revenues from 1.6% in the year ended December 31, 2007 to 1.7% in the year ended December 31, 2008. The overall increase in general, administrative and other expenses in this segment was due to acquisitions.

*Operating income*

Operating income increased by \$1,158.7 million, or 82.9%, to \$2,556.3 million in the year ended December 31, 2008 from \$1,397.6 million in the year ended December 31, 2007. Operating income as a percentage of consolidated revenues increased to 25.7% in the year ended December 31, 2008 from 20.9% in the year ended December 31, 2007, mainly due to the increase in gross margin on the back of sales prices increases in the steel and mining segments in the first half of 2008. However, this effect was partially offset by the losses incurred by our steel and ferroalloys segments in the fourth quarter of 2008 due to the financial crisis.

The table below sets out operating income by segment, including as a percentage of segment revenues.

Operating Income by Segment	Year Ended December 31, 2008		Year Ended December 31, 2007	
	Amount	% of Segment Revenues	Amount	% of Segment Revenues
	(In thousands of U.S. dollars, except for percentages)			
Mining segment	1,800,540	44.7%	571,469	29.0%
Steel segment	770,439	13.3%	537,261	12.2%
Ferroalloys segment	(50,517)	(0.9)%	350,107	55.0%
Power segment	29,406	2.9%	12,627	2.1%
Elimination of intersegment unrealized profit	6,401		(73,871)	
Consolidated operating income	2,556,269		1,397,593	

*Mining segment*

Mining segment operating income increased by \$1,229.1 million, or 215.1%, to \$1,800.5 million in the year ended December 31, 2008 from \$571.5 million in the year ended December 31, 2007. Operating margin percentage increased to 44.7% in the year ended December 31, 2008 from 29.0% in the year ended December 31, 2007, mainly due to the effect of inclusion of Yakutugol in the mining segment since October 2007 as well as an increase in coking coal, steam coal and iron ore sales prices in the first half of 2008.

***Steel segment***

Steel segment operating income increased by \$233.2 million, or 43.4%, to \$770.4 million in the year ended December 31, 2008 from \$537.3 million in the year ended December 31, 2007. Operating margin percentage increased to 13.3% in the year ended December 31, 2008 from 12.2% in the year ended December 31, 2007 due to the increase in gross profit following on an increase in sales prices in the first half of 2008.

***Ferroalloys segment***

Ferroalloys segment operating income decreased by \$400.6 million, or 114.4%, to a \$50.5 million loss in the year ended December 31, 2008 from \$350.1 million income in the year ended December 31, 2007. Operating

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margin percentage decreased to negative 0.9% from 55.0%, mainly due to a decrease in nickel sales prices with a simultaneous increase in the price of raw materials (primarily coke).

**Power segment**

Power segment operating income increased by \$16.8 million, or 132.9%, to \$29.4 million in the year ended December 31, 2008 from \$12.6 million in the year ended December 31, 2007. Operating margin percentage increased to 2.9% from 2.1% due to the decrease in the share of selling and distribution expenses primarily consisting from electricity transmission costs incurred by Kuzbass Power Sales Company.

**Other income and expense, net**

Other income and expense, net consists of income (loss) of equity investees, interest income, interest expense, gain on revaluation of trading securities, other income and foreign exchange gain. The table below sets forth these costs for the years ended December 31, 2008 and 2007, including as a percentage of revenues.

	Year Ended December 31, 2008		Year Ended December 31, 2007	
	Amount	% of Revenues	Amount	% of Revenues
<b>Other Income and Expense, Net</b>				
	<b>(In thousands of U.S. dollars, except for percentages)</b>			
Income (loss) from equity investees	717	0.0%	8	0.0%
Interest income	11,614	0.1%	12,278	0.2%
Interest expense	(324,083)	(3.3)%	(98,976)	(1.5)%
Other income, net	(18,821)	(0.2)%	19,844	0.3%
Foreign exchange gain (loss)	(877,428)	(8.8)%	54,700	0.8%
Total	(1,208,001)	(12.1)%	(12,146)	(0.2)%

Income from equity investees was \$0.7 million compared to \$8.5 thousand in the year ended December 31, 2007 and consists of our share of income of our equity investments such as Toplofikatsia Rousse and Southern Kuzbass Coal Company offset by losses at equity investments such as Mechel Energy AG.

Interest income decreased by \$0.7 million, or 5.4%, to \$11.6 million in the year ended December 31, 2008 from \$12.3 million in the year ended December 31, 2007. The decrease was due to a reduction in income from deposits held by our Russian and foreign subsidiaries in various banks following a decrease in such deposits.

Interest expense increased by \$225.1 million, or 227.4%, to \$324.1 million in the year ended December 31, 2008 from \$99.0 million in the year ended December 31, 2007. The increase was associated with the overall increase of average loan balances in 2008, especially by the interest incurred on the syndicated loan related to the Yakutugol acquisition and the loan for the Oriol Resources acquisition. See Liquidity and Capital Resources Description of Certain Indebtedness.

Other income decreased by \$38.7 million, or 194.8%, from \$19.8 million income in the year ended December 31, 2007 to a \$18.8 million loss in the year ended December 31, 2008. The decrease is explained by equity contributions to pension fund Penfosib made by a number of our companies in 2008 which do not meet the definition of an asset,

totaling \$17.5 million. Also in the year ended December 31, 2007, we recorded other income from gain due to the release of an accounting provision in respect of a \$10.7 million tax liability relating to our Korshunov Mining Plant, as well as income from release of prior-period tax provisions for Mechel International Holdings AG of \$9.3 million.

Foreign exchange loss increased by \$932.1 million, or 1,704.1%, to a \$877.4 million loss in the year ended December 31, 2008 from a \$54.7 million gain in the year ended December 31, 2007. This foreign exchange loss was primarily attributable to losses from revaluation of the U.S. dollar-denominated syndicated loan related to acquisition of Yakutugol and the loan for the acquisition of Oriel Resources.

**Table of Contents***Income tax expense*

Income tax expense decreased by \$237.4 million, or 66.6%, to \$118.9 million in the year ended December 31, 2008 from \$356.3 million in the year ended December 31, 2007, and our effective tax rate decreased to 8.8% from 25.7%. The decrease in income tax expenses is attributable to the decrease in taxable income and the decrease in the Russian statutory income tax rate from 24% to 20% effective January 1, 2009. In addition, in December 2008, the tax legislation of Kazakhstan was amended to decrease the statutory income tax rate from 30% in 2008 to 20% in 2009. The effect of both decreases was recorded as the decrease of deferred tax liabilities in both our Russian and Kazakh subsidiaries. As of December 31, 2008, the effect of these changes in the total amount of \$341.1 million was recognized as a reduction in the income tax expense for the year then ended.

*Minority interest*

Minority interest in income of subsidiaries decreased by \$27.4 million, or 23.6%, to \$88.8 million in the year ended December 31, 2008 from \$116.2 million in the year ended December 31, 2007. The minority interest in the income of our subsidiaries in 2008 consisted of the share of minority shareholders in the net income of Southern Kuzbass Coal Company of \$25.1 million, of Korshunov Mining Plant of \$26.6 million, of Tomusinsk Open Pit Mine of \$12.9 million, of Chelyabinsk Metallurgical Plant of \$7.3 million, of Beloretsk Metallurgical Plant of \$3.0 million, of Mechel Targoviste of \$3.7 million, of Ural Stampings Plant of \$2.5 million, of ferroalloys segment companies of \$2.3 million and of power segment companies of \$2.2 million.

*Income from continuing operations*

Income from continuing operations increased by \$227.7 million, or 24.9%, to \$1,140.5 million in the year ended December 31, 2008 from \$913.0 million in the year ended December 31, 2007, mainly as a result of an increase in operating income, mainly due to the increase in gross margin on the back of sales prices increases in the steel and mining segments in the first half of 2008. However, this effect was partially offset by the losses incurred by our steel and ferroalloys segments in the fourth quarter of 2008 due to the global financial crisis.

*Loss from discontinued operations*

Income from discontinued operations was none in the year ended December 31, 2008 compared to \$0.2 million in the year ended December 31, 2007. The income in 2007 resulted from a write-off of Mechel Zeljezara's accounts payables due to this company's bankruptcy. In February 2008, Mechel Zeljezara was finally liquidated. Mechel Zeljezara engaged in business until August 2004, when we decided to terminate production.

*Net income*

For the reasons set forth above, our net income increased by \$227.5 million, or 24.9%, to \$1,140.5 million in the year ended December 31, 2008 from \$913.0 million in the year ended December 31, 2007.

***Year ended December 31, 2007 compared to year ended December 31, 2006****Net revenues*

Consolidated net revenues increased by \$2,286.0 million, or 52.0%, to \$6,683.8 million in the year ended December 31, 2007, from \$4,397.8 million in the year ended December 31, 2006.

Across our segments, our acquisitions in 2006 and 2007 led to higher consolidated net revenues due to higher production and sales volumes arising primarily from the consolidation of the results of operations of acquired companies. Approximately 27%, or \$611.0 million, of the increase in our consolidated net revenues in the year ended December 31, 2007 compared to the year ended December 31, 2006 was due to the consolidation of companies acquired during the year. The remainder of our increase in revenues was due to organic growth, which was driven largely by price increases and changes in the product mix towards higher value-added products. In addition, the steady decrease in real terms in the value of the dollar, in which most of our products are priced, against the ruble, in which most of our production costs are incurred, put exchange rate-based pressure on profit margins.

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This was more than offset by increases in the weighted average prices of products sold by our mining and steel segments.

The following table sets forth our net revenues by segment:

	<b>Year Ended December 31,</b>	
	<b>2007</b>	<b>2006</b>
	<b>(In thousands of U.S. dollars, except percentages)</b>	
<b>Mining segment</b>		
To third parties	1,372,508	1,045,696
To power segment	11,272	399
To ferroalloys segment	12,051	11,512
To steel segment	575,138	296,678
Total	1,970,969	1,354,285
<b>Steel segment</b>		
To third parties	4,306,875	3,042,795
To power segment	22,509	17,195
To ferroalloys segment	79,135	20,358
To mining segment	5,973	3,306
Total	4,414,492	3,083,654
<b>Ferroalloys segment</b>		
To third parties	501,143	259,857
To steel segment	135,513	79,891
Total	636,656	339,748
<b>Power segment</b>		
To third parties	503,316	49,463
To steel segment	38,587	41,087
To ferroalloys segment	26,225	8,487
To mining segment	30,387	24,285
Total	598,515	123,322
Eliminations	936,790	503,198
Consolidated revenues	6,683,842	4,397,811
% from mining segment	20.5%	23.8%
% from steel segment	64.4%	69.2%
% from ferroalloys segment	7.5%	5.9%
% from power segment	7.5%	1.1%

***Mining segment***

Our total mining segment sales increased by \$616.7 million, or 45.5%, to \$1,971.0 million in the year ended December 31, 2007 from \$1,354.3 million in the year ended December 31, 2006.

Coking coal concentrate sales to third parties increased by \$104.6 million, or 20.2%, to \$622.9 million in the year ended December 31, 2007 from \$518.3 million in the year ended December 31, 2006, where a decrease in sales volumes offset a \$150.4 million sales price increase by \$45.9 million. The price increases occurred on both export and domestic markets, resulting from increasing coking coal demand and tight supply both in domestic and export markets due to accidents in several Russian coal mines which caused mine closures, as well as cargo seaport

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capacity problems in Australia. The volume of coking coal concentrate sold to third parties decreased by 584 thousand tonnes, or 8.8%, to 6,018 thousand tonnes in the year ended December 31, 2007 from 6,603 thousand tonnes in the year ended December 31, 2006, primarily due to an increase in intersegment sales volumes as described below.

Coking coal concentrate supplied to the steel segment increased by \$220.3 million, or 117.5%, to \$407.9 million in the year ended December 31, 2007 from \$187.6 million in the year ended December 31, 2006, where \$123.7 million of the increase was due to an increase in sales prices and \$96.6 million was due to an increase in sales volumes. The increase in volumes was principally due to shipments from Southern Kuzbass Coal Company to Moscow Coke and Gas Plant of 981 thousand tonnes that were insignificant in 2006 before our acquisition of Moscow Coke and Gas Plant, as we acquired Moscow Coke and Gas Plant in the fourth quarter of 2006, and shipments from Yakutugol to Mechel-Coke and Moscow Coke and Gas Plant in the fourth quarter of 2007 totaling 58 thousand tonnes.

Steam coal and steam coal concentrate sales to third parties increased by \$125.2 million, or 40.2%, to \$436.3 million in the year ended December 31, 2007 from \$311.1 million in the year ended December 31, 2006, where \$102.0 million of the increase was due to an increase in sales prices and \$23.2 million was due to an increase in sales volume. The increase of sales volumes during the period was principally due to the fact that the results of operations of Yakutugol were reflected in our consolidated statement of income from the fourth quarter of 2007. If Yakutugol's results of operations are excluded, our steam coal volumes sold in 2007 would have decreased by 3%, in part due to the increase in the volume of steam coal supplied to the power segment and in part due to a shortage, as compared to the prior period, of working, empty rail freight cars from Russian Railways in the Southern Kuzbass region where our other coal operations are based. Export prices for steam coal and steam coal concentrate rose during the period as a result of increasing demand, especially in Asia, and limited supply growth from major exporting countries. Domestic prices rose on the back of growing production costs and global steam coal price increases.

Sales of steam coal supplied to the power segment increased by \$9.8 million, or 100%, to \$9.8 million in the year ended December 31, 2007 from none in the year ended December 31, 2006, due to the acquisition of Southern Kuzbass Power Plant.

Sales of iron ore to third parties increased by \$45.4 million, or 27.0%, to \$213.6 million in the year ended December 31, 2007 from \$168.2 million in the year ended December 31, 2006, where a decrease in sales volumes offset a \$76.1 million sales price increase by \$30.7 million. Price increases were driven principally by increasing iron ore demand in Russia and elsewhere, especially in China; limited iron ore production capacity increases which typically lag behind rising demand; and significant increases in freight costs. The decrease in sales volumes is primarily attributable to a temporary decrease in the second half of 2007 in orders from Zapadno-Sibirsky Metallurgical Works OAO ( ZapSib ), one of our primary customers, which sourced its iron ore from a different supplier during part of 2007.

Supplies to the steel segment increased by \$57.6 million, or 60.3%, to \$153.1 million in the year ended December 31, 2007 from \$95.5 million in the year ended December 31, 2006, primarily due to a sales price increase, as there was no significant increase in volumes.

Excluding intersegment sales, export sales were 40.2% of mining segment sales in the year ended December 31, 2007, compared to 36.9% in the year ended December 31, 2006. The increase in the proportion of our export sales was due to the higher export volumes of steam coal and iron ore due to higher sales prices on export markets. The average steam coal export price on FCA basis in 2007 was \$44.4 per tonne in comparison with \$32.3 per tonne for the average domestic price on FCA basis in 2006; the average iron ore export sales price on FCA basis in 2007 was \$84.9 per tonne in comparison with \$73.5 per tonne for the average domestic price on FCA basis in 2006.



**Table of Contents*****Steel segment***

Our steel segment revenues increased by \$1,330.8 million, or 43.2%, to \$4,414.5 million in the year ended December 31, 2007 from \$3,083.7 million in the year ended December 31, 2006. The increase in steel segment revenues was primarily due to the following increases:

Coke and coking products sales increased by \$235.8 million, or 542.8%, to \$284.8 million in the year ended December 31, 2007 from \$49.0 million in the year ended December 31, 2006, where \$61.2 million of the increase was due to an increase in sales prices and \$174.6 million of the increase was due to an increase in sales volumes. The sales volume increase was a result of consolidating Moscow Coke and Gas Plant results for the full year 2007; in 2006, the results for the plant were consolidated for the fourth quarter only. The sales price increase was due to strong market demand for coke and coking products.

Semi-finished steel products sales increased by \$157.6 million, or 39.6%, to \$555.1 million in the year ended December 31, 2007 from \$397.5 million in the year ended December 31, 2006, where \$115.0 million of the increase was due to an increase in sales prices and \$42.6 million of the increase was due to an increase in sales volumes. Increases in both sales prices and sales volumes were primarily driven by increased demand and a shortage of supply from China.

Alloyed long products sales increased by \$20.8 million, or 15.8%, to \$151.9 million in the year ended December 31, 2007 from \$131.1 million in the year ended December 31, 2006, where a decrease in sales volumes of \$20.1 million offset a \$40.9 million sales price increase. The sales price increase was primarily driven by a significant increase in the price of alloy materials used in production. The sales volume decrease was caused by a decrease in market demand for alloyed long products following an increase in market prices for such products.

Rebar sales increased by \$264.1 million, or 35.1%, to \$1,017.1 million in the year ended December 31, 2007 from \$753.0 million in the year ended December 31, 2006, where \$228.4 million of the increase was due to an increase in sales prices and \$35.7 million of the increase was due to an increase in sales volumes. The increases in both sales prices and sales volumes are attributable to the high level of activity in the construction industry in Russia.

Low alloyed engineering steel sales increased by \$111.6 million, or 35.5%, to \$426.3 million in the year ended December 31, 2007 from \$314.7 million in the year ended December 31, 2006, where \$97.8 million of the increase was due to an increase in sales prices and \$13.8 million of the increase was due to an increase in sales volumes. The increases in both sales prices and sales volumes were driven by strong demand on both export and domestic markets.

Flat steel products sales increased by \$117.7 million, or 38.7%, to \$421.8 million in the year ended December 31, 2007 from \$304.2 million in the year ended December 31, 2006, where \$112.8 million of the increase was due to an increase in sales prices and \$4.8 million of the increase was due to an increase in sales volumes. The increase in sales prices was in both domestic and export markets, and was mainly due to a stainless flat steel price increase driven by an increase in nickel prices in 2007. The other reasons were a general increase in production costs and strong domestic demand.

Forgings and stampings sales increased by \$133.1 million, or 57.2%, to \$366.1 million in the year ended December 31, 2007 from \$232.9 million in the year ended December 31, 2006, mainly due to a \$126.1 million sales price increase. The increase in the sales price was primarily due to rapid increases in the market prices for nickel and other alloy materials and a shift in product mix to more value-added items.

Hardware sales increased by \$145.4 million, or 31.7%, to \$603.4 million in the year ended December 31, 2007 from \$458.0 million in the year ended December 31, 2006, where \$78.6 million of the increase was due to an increase in sales prices and \$66.8 million of the increase was due to an increase in sales volumes. The volume increase was due to the installation of several new production lines at the Beloretsk Metallurgical Plant, including two spring wire drawing mills and a stabilized high-tensile wire production complex. The price increase was due to an increase in demand on the Russian domestic market and in the CIS from the construction industry, machine-building and other industries.

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Excluding intersegment sales, export sales comprised 31.4% of steel segment sales in the year ended December 31, 2007, compared to 32.5% in the year ended December 31, 2006. The decrease in the proportion of our export sales was largely due to favorable domestic pricing and robust domestic steel consumption growth which exceeded the Russian steel industry's increase in production volumes.

***Ferrous alloys segment***

Our total ferrous alloys segment sales increased by \$296.9 million, or 87.4%, to \$636.7 million in the year ended December 31, 2007 from \$339.7 million in the year ended December 31, 2006.

Nickel sales to third parties increased by \$210.2 million, or 81.3%, to \$468.9 million in the year ended December 31, 2007 from \$258.7 million in the year ended December 31, 2006, where \$189.6 million of the increase was due to an increase in sales prices and \$20.6 million of the increase was due to an increase in sales volumes. Average sales prices increased by \$14,468 to \$35,775 per tonne during 2007. LME prices increased to record levels in the first half of 2007. The highest daily spot price reached \$54,200 per tonne on May 16, 2007. Sales volumes increased by 8% to 13 thousand tonnes in the year ended December 31, 2007 from 12 thousand tonnes in the year ended December 31, 2006 due to the overall increase of production volumes at Southern Urals Nickel Plant.

Nickel supplies to the steel segment increased by \$46.5 million, or 58.6%, to \$125.8 million in the year ended December 31, 2007 from \$79.3 million in the year ended December 31, 2006, due to an increase in sales prices. There were no significant changes in intersegment sales volumes.

Ferrosilicon sales were \$29.0 million in the year ended December 31, 2007 compared to none in the year ended December 31, 2006, due to the acquisition of Bratsk Ferroalloy Plant in August 2007.

Excluding intersegment sales, export sales were 93.7% of ferrous alloys segment sales in the year ended December 31, 2007 compared to 99.5% in the year ended December 31, 2006. The decrease in the proportion of our export sales was due to the acquisition in August 2007 of Bratsk Ferroalloy Plant, whose domestic sales in the period from August 2007 to December 2007 constituted 89.6% of its total sales.

***Power segment***

Our power segment revenues increased almost four-fold by \$475.2 million to \$598.5 million in the year ended December 31, 2007 from \$123.3 million in the year ended December 31, 2006. The increase in power segment revenues was principally due to the acquisition of Southern Kuzbass Power Plant and Kuzbass Power Sales Company in the second quarter of 2007, which resulted in an almost four-fold increase in segment revenues from sales to third parties of \$446.7 million.

Prior to our acquisition of Southern Kuzbass Power Plant and Kuzbass Power Sales Company in the second quarter of 2007, our power segment consisted of intersegment and third-party sales of electricity produced by co-generation units burning blast furnace gas and coal gas produced as a byproduct of industrial processes at our Chelyabinsk Metallurgical Plant, Moscow Coke and Gas Plant, Southern Kuzbass Coal Company and Mechel-Coke.

Southern Kuzbass Power Plant contributed \$1.8 million to the power segment revenues through power generation capacity sales to third parties in the second half of 2007.

**Table of Contents***Cost of goods sold and gross profit*

Consolidated cost of goods sold was 62.3% of consolidated revenues in the year ended December 31, 2007, as compared to 65.0% of consolidated revenues in the year ended December 31, 2006, resulting in an increase in consolidated gross margin to 37.7% in the year ended December 31, 2007 from 35.0% for the year ended December 31, 2006. Cost of goods sold primarily consists of costs relating to raw materials (including products purchased for resale), direct payroll, depreciation and energy. The table below sets forth cost of goods sold and gross margin by segment for the years ended December 31, 2007 and 2006, including as a percentage of segment revenues.

<b>Cost of Goods Sold and Gross Margin by Segment</b>	<b>Year Ended December 31, 2007</b>		<b>Year Ended December 31, 2006</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Mining segment</b>				
Cost of goods sold	1,008,485	51.2%	830,632	61.3%
Gross margin	962,484	48.8%	523,653	38.7%
<b>Steel segment</b>				
Cost of goods sold	3,374,420	76.4%	2,240,001	72.6%
Gross margin	1,040,072	23.6%	843,653	27.4%
<b>Ferroalloys segment</b>				
Cost of goods sold	253,725	39.9%	174,675	51.4%
Gross margin	382,931	60.1%	165,073	48.6%
<b>Power segment</b>				
Cost of goods sold	393,153	65.7%	110,273	89.4%
Gross margin	205,362	34.3%	13,049	10.6%

***Mining segment***

Mining segment cost of goods sold increased by \$177.9 million, or 21.4%, to \$1,008.5 million in the year ended December 31, 2007 from \$830.6 million in the year ended December 31, 2006. Mining segment gross margin increased from 38.7% in the year ended December 31, 2006 to 48.8% in the year ended December 31, 2007. The increase in the mining segment gross margin was principally due to the increase in coking coal and iron ore sales prices in both export and domestic markets, an increase in nickel and steam coal sales prices in export markets and a decrease in the production cash costs of coking coal concentrate at Southern Kuzbass Coal Company by 3.0% due to an increase in production volumes and a corresponding apportionment of fixed costs to larger production volumes. The production cash costs of steam coal and steam coal concentrate remained flat. Cash costs of production of iron ore increased by 38.9% due to an increase in electricity prices, production personnel wages and the prices of mining supplies used in coal and iron ore production, such as spare parts and equipment, fuel and explosives.

***Steel segment***

Steel segment cost of goods sold increased by \$1,134.4 million, or 50.6%, to \$3,374.4 million in the year ended December 31, 2007 from \$2,240.0 million in the year ended December 31, 2006. Steel segment cost of goods sold was 76.4% of the segment's revenues in the year ended December 31, 2007, as compared to 72.6% in the year ended December 31, 2006, resulting in a decrease in gross margin from 27.4% to 23.6%. Such decrease was primarily

attributable to an increase in production costs during the period under review in this section, which was itself due to the growth in raw materials prices, particularly the prices of nickel and coking coal.

***Ferrous alloys segment***

Ferrous alloys segment cost of goods sold increased by \$79.1 million, or 45.3%, to \$253.7 million in the year ended December 31, 2007, from \$174.7 million in the year ended December 31, 2006. Ferrous alloys segment gross margin percentage increased from 48.6% in the year ended December 31, 2006 to 60.1% in the year ended

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December 31, 2007. The increase in the ferroalloys segment gross margin was principally due to increase of nickel prices on export markets. Production cash costs of nickel increased by 38.9% due to the increases in the prices of raw materials used in nickel production such as coke, pyrites and limestone.

**Power segment**

Power segment cost of goods sold increased by \$282.9 million, or 256.5%, to \$393.2 million in the year ended December 31, 2007 from \$110.3 million in the year ended December 31, 2006. Power segment gross margin increased from 10.6% in the year ended December 31, 2006, to 34.3% in the year ended December 31, 2007. The increase in the power segment gross margin principally reflected the acquisition of Southern Kuzbass Power Plant and Kuzbass Power Sales Company in the second quarter of 2007, which generated higher profits than those of previously existing co-generation assets at our production facilities. The new assets also have incurred high electricity transmission costs that are included in the selling and distribution expenses for the power segment, as set forth below.

**Selling, distribution and operating expenses**

Selling, distribution and operating expenses increased by \$307.5 million, or 37.9%, to \$1,119.4 million in the year ended December 31, 2007 from \$811.9 million in the year ended December 31, 2006. As a percentage of consolidated revenues, selling, distribution and operating expenses decreased to 16.7% in the year ended December 31, 2007, as compared to 18.5% in the year ended December 31, 2006. Our selling, distribution and operating expenses consist primarily of selling and distribution expenses, taxes other than income tax, loss on write-offs of property, plant and equipment, allowance for doubtful accounts and general, administrative and other operating expenses. The table below sets forth these costs by segment for the years ended December 31, 2007 and 2006, including as a percentage of segment revenues.

<b>Selling, Distribution and Operating Expenses by Segment</b>	<b>Year Ended December 31, 2007</b>		<b>Year Ended December 31, 2006</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Mining segment</b>				
Selling and distribution expenses	241,090	12.2%	213,511	15.8%
Taxes other than income tax	3,815	0.2%	32,913	2.4%
Accretion expense	1,071	0.1%	2,144	0.2%
Allowance for doubtful accounts	(1,441)	(0.1)%	(43)	(0.0)%
General, administrative and other operating expenses	146,480	7.4%	84,087	6.2%
<b>Total</b>	<b>391,015</b>	<b>19.8%</b>	<b>332,612</b>	<b>24.6%</b>
<b>Steel segment</b>				
Selling and distribution expenses	194,855	4.4%	202,391	6.6%
Taxes other than income tax	71,243	1.6%	44,515	1.4%
Loss on write-off of property, plant and equipment			2,418	0.1%
Accretion expense	1,708	0.0%	5,089	0.2%
Allowance for doubtful accounts	3,602	0.1%	2,853	0.1%

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General, administrative and other operating expenses	231,403	5.2%	199,834	6.5%
Total	502,811	11.4%	457,100	14.8%

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<b>Selling, Distribution and Operating Expenses by Segment</b>	<b>Year Ended December 31, 2007</b>		<b>Year Ended December 31, 2006</b>	
	<b>Amount</b>	<b>% of Segment Revenues</b>	<b>Amount</b>	<b>% of Segment Revenues</b>
<b>(In thousands of U.S. dollars, except for percentages)</b>				
<b>Ferroalloys segment</b>				
Selling and distribution expenses	3,400	0.5%	729	0.2%
Taxes other than income tax	7,528	1.2%	4,419	1.3%
Accretion expense	322	0.1%	200	0.1%
Allowance for doubtful accounts	2	0.0%	(72)	(0.0)%
General, administrative and other operating expenses	21,572	3.4%	12,501	3.7%
<b>Total</b>	<b>32,824</b>	<b>5.2%</b>	<b>17,777</b>	<b>5.2%</b>
<b>Power segment</b>				
Selling and distribution expenses	182,466	30.5%	2,270	1.8%
Taxes other than income tax	1,408	0.2%	293	0.2%
Allowance for doubtful accounts	(752)	(0.1)%	(16)	(0.0)%
General, administrative and other operating expenses	9,613	1.6%	1,853	1.5%
<b>Total</b>	<b>192,735</b>	<b>32.2%</b>	<b>4,400</b>	<b>3.6%</b>

***Mining segment***

Selling and distribution expenses consisted almost entirely of transportation expenses related to our selling activities, and increased by \$27.6 million in line with sales volume increases in 2007. As a percentage of mining segment revenues, selling and distribution expenses decreased from 15.8% to 12.2% due to an increase in the share of sales on delivery where transportation expenses are paid by the customer.

Taxes other than income tax include property and land taxes, as well as other taxes. Taxes other than income tax decreased by \$29.1 million, or 88.4%, to \$3.8 million in the year ended December 31, 2007 from \$32.9 million in the year ended December 31, 2006. The decrease was mainly due to the reversal of a \$25.7 million tax liability related to Korshunov Mining Plant in respect of mineral extraction taxes and social taxes for prior periods. On December 18, 2007, the Supreme Arbitration Court of the Russian Federation issued an order in our favor that clarified an aspect of tax law that was previously uncertain, resulting in a reduction in our mineral extraction tax liability for the years 2003-2007. In addition, on April 7, 2008, the Federal Arbitration Court in Moscow issued an order in our favor requiring the tax authorities to pay interest to us in respect of overpaid social taxes previously assessed for the period from August 2004 to February 2007.

Allowance for doubtful accounts decreased by \$1.4 million, or 3,253.5%, to \$1.4 million income in the year ended December 31, 2007 from income of \$43.0 thousand in the year ended December 31, 2006, due to an improvement in our collection of trade receivables.

General, administrative and other expenses, consisting of payroll and payroll taxes, depreciation, rent and maintenance, legal and consulting expenses, office overhead and other expenses, increased by \$62.4 million, or 74.2%, to \$146.5 million in the year ended December 31, 2007 from \$84.1 million in the year ended December 31, 2006, representing an increase as a percentage of segment revenues from 6.2% to 7.4%. Salaries and related social taxes increased by \$32.0 million, or 71.5%, to \$76.7 million in the year ended December 31, 2007 from \$44.8 million in the year ended December 31, 2006, mainly due to indexation of salary rates to inflation at our production companies, increases in management bonuses and an increase in employee headcount in connection with the Yakutugol acquisition which accounted for additional salaries and related social taxes of \$11.2 million. Legal and consulting fees and insurance services increased by \$2.0 million, or 23.3%, to \$10.5 million in the year ended December 31, 2007 from \$8.5 million in the year ended December 31, 2006, due to increases in consulting fees. Rent and maintenance, business travel expenses, bank charges and office expenses increased by \$5.9 million,

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or 57.8%, to \$16.1 million in the year ended December 31, 2007 from \$10.2 million in the year ended December 31, 2006. Depreciation increased by \$2.3 million, or 91.1%, to \$4.8 million in the year ended December 31, 2007 from \$2.5 million in the year ended December 31, 2006, due to the overall expansion of segment activities in 2007. Social expenses increased by \$14.3 million, or 128.2%, to \$25.4 million in the year ended December 31, 2007 from \$11.1 million in the year ended December 31, 2006, mainly due to expansion of our socially-oriented activities in various regions of Russia as well as social programs for our employees. Other administrative and operating expenses increased by \$6.0 million due to overall expansion of segment activities.

***Steel segment***

Selling and distribution expenses for our steel segment consisted almost entirely of transportation expenses related to our selling activities. Such expenses decreased by \$7.5 million, or 3.7%, to \$194.9 million in the year ended December 31, 2007 from \$202.4 million in the year ended December 31, 2006. The decrease is explained by an increase in the share of export sales on delivery terms where transportation expenses are paid by the customer.

Taxes other than income tax increased by \$26.7 million, or 60.0%, to \$71.2 million in the year ended December 31, 2007 from \$44.5 million in the year ended December 31, 2006. As a percentage of segment revenues, these taxes increased from 1.4% to 1.6%. Property and land taxes increased by \$9.3 million, or 26.2%, to \$44.8 million in the year ended December 31, 2007 from \$35.5 million in the year ended December 31, 2006, due to an increase in the property tax base (as a result of putting new fixed assets into operation). In the year ended December 31, 2007, we incurred \$10.1 million in tax penalties and fines assessed in prior-period tax audits at our Chelyabinsk Metallurgical Plant. The remaining increase of \$7.3 million was caused mainly by the increase of non-reimbursable VAT expenses at Chelyabinsk Metallurgical Plant. The majority of these expenses are related to non-reimbursable VAT on railway charges that increased in line with the increase in rail freight carriage prices.

Allowance for doubtful accounts increased by \$0.7 million, or 26.3%, to \$3.6 million in the year ended December 31, 2007 from \$2.9 million in the year ended December 31, 2006, due to changes in our estimate of bad debts as of the respective period end dates based on the ageing of the balances.

General, administrative and other expenses increased by \$31.6 million, or 15.8%, to \$231.4 million in the year ended December 31, 2007 from \$199.8 million in the year ended December 31, 2006, and decreased as a percentage of segment revenues from 6.5% in the year ended December 31, 2006, to 5.2% in the year ended December 31, 2007. Payroll and related social taxes increased by \$28.7 million, or 34.8%, to \$111.2 million in the year ended December 31, 2007 from \$82.5 million in the year ended December 31, 2006, mainly due to indexation of salary rates to inflation at our production companies and also due to increases in management bonuses. Social expenses (including pension obligations) increased by \$3.7 million, or 18.9%, to \$23.3 million in the year ended December 31, 2007 from \$19.6 million in the year ended December 31, 2006, due to expansion of our social activities in various regions of Russia as well as social programs for our employees. Rent and maintenance, business travel expenses, bank charges and office expenses increased by \$12.3 million, or 52.3%, to \$35.9 million in the year ended December 31, 2007 from \$23.6 million in the year ended December 31, 2006, primarily due to the overall expansion of segment activities in 2007. Professional expenses, which include auditing, accounting, legal and engineering fees, and insurance services increased by \$2.2 million, or 13.9%, to \$18.4 million in the year ended December 31, 2007 from \$16.2 million in the year ended December 31, 2006, due to increases in consulting fees. Other administrative expenses increased by \$8.6 million, or 52.3%, to \$21.5 million in the year ended December 31, 2007 from \$12.9 million in the year ended December 31, 2006, mainly due to an increase in the number of administrative departments at our Chelyabinsk Metallurgical Plant. These increases in expenses were partially offset by recognition of income from reductions in asset retirement obligations at our Chelyabinsk Metallurgical Plant of \$19.7 million based on expert consultants review of our capital improvements program for Chelyabinsk Metallurgical Plant and planned changes aimed at minimizing environmental impact.

