IMPORTANT: You must read the following disclaimer before continuing. The following disclaimer applies to the attached prospectus (the "**Prospectus**") and you are therefore advised to read this carefully before reading, accessing or making any other use of the attached Prospectus. In accessing the Prospectus, you agree to be bound by the following terms and conditions, including any modifications to them from time to time, each time you receive any information from us as a result of such access. You acknowledge that this electronic transmission and the delivery of the attached Prospectus is confidential and intended only for you and **you agree you will not forward, reproduce or publish this electronic transmission or the attached Prospectus to any other person.**

The Prospectus and the offer when made are only addressed to and directed at persons in member states of the European Economic Area ("**EEA**") who are "qualified investors" within the meaning of Article 2(1)(e) of the Prospectus Directive (Directive 2003/71/EC) (the "**Prospectus Directive**") ("**Qualified Investors**"). In addition, in the United Kingdom ("**UK**"), this Prospectus is being distributed only to, and is directed only at, Qualified Investors (i) who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "**Order**") and Qualified Investors falling within Article 49 of the Order, and (ii) to whom it may otherwise lawfully be communicated (all such persons together being referred to as "**relevant persons**"). This Prospectus must not be acted on or relied on (i) in the UK, by persons who are not relevant persons, and (ii) in any member state of the EEA other than the UK, by persons who are not Qualified Investors. Any investment or investment activity to which this Prospectus relates is available only to (i) in the UK, relevant persons, and (ii) in any member state of the EEA other than the UK, Qualified Investors, and will be engaged in only with such persons.

THIS PROSPECTUS AND THE SECURITIES REFERENCED HEREIN MAY ONLY BE DISTRIBUTED IN "OFFSHORE TRANSACTIONS" TO PERSONS OTHER THAN UNITED STATES PERSONS AS DEFINED IN, AND AS PERMITTED BY, REGULATION S UNDER THE UNITED STATES SECURITIES ACT OF 1933 (THE "**SECURITIES ACT**") OR WITHIN THE UNITED STATES TO QUALIFIED INSTITUTIONAL BUYERS ("**QIBs**") AS DEFINED IN AND IN ACCORDANCE WITH RULE 144A UNDER THE SECURITIES ACT ("**RULE 144A**"). ANY FORWARDING, REDISTRIBUTION OR REPRODUCTION OF THIS PROSPECTUS IN WHOLE OR IN PART IS UNAUTHORISED. FAILURE TO COMPLY WITH THIS NOTICE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS.

NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES A PUBLIC OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY OTHER JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE SECURITIES HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES AND MAY NOT BE OFFERED OR SOLD IN THE UNITED STATES EXCEPT (1) IN ACCORDANCE WITH RULE 144A TO A PERSON THAT THE HOLDER AND ANY PERSON ACTING ON ITS BEHALF REASONABLY BELIEVES IS A QIB OR (2) IN AN OFFSHORE TRANSACTION TO PERSONS OTHER THAN UNITED STATES PERSONS IN ACCORDANCE WITH RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT, IN EACH CASE IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES.

Confirmation of your representation: The attached Prospectus is delivered to you at your request and on the basis that you have confirmed to Goldman Sachs International, J.P. Morgan Securities Ltd. and Merrill Lynch International (the "**Joint Lead Managers**") and JSC Georgian Railway (the "**Company**") that (i) you are either (a) located outside United States and not a U.S. person (as defined in Regulation S under the Securities Act), or (b) a QIB; (ii) if you are in the UK, you are a relevant person; and (iii) if you are in any member state of the EEA other than the UK, you are a Qualified Investor; (iv) if you are acting a financial intermediary (as that term is used in Article 3(2) of the Prospectus Directive), the securities acquired by you as a financial intermediary in the offer have not been acquired on a non-discretionary basis on behalf of, nor have they been acquired with a view to their offer or resale to, any person in circumstances which may give rise to an offer of any securities to the public other than their offer or resale in any member state of the EEA which has implemented the Prospectus Directive to Qualified Investors (as defined in the Prospectus Directive); or (v) you are outside of the UK or EEA (and the electronic mail addresses that you gave us and to which this Prospectus has been delivered are not located in such jurisdictions) or (vi) you are a person into whose possession this Prospectus may lawfully be delivered in accordance with the laws of the jurisdiction in which you are located.

This Prospectus has been made available to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently neither the Company, the Joint Lead Managers nor any of their respective affiliates accepts any liability or responsibility whatsoever in respect of any difference between the Prospectus distributed to you in electronic format and the hard copy version. By accessing the linked Prospectus, you consent to receiving it in electronic form.

A hard copy of the Prospectus will be made available to you only upon request to the Joint Lead Managers.

You are reminded that you have accessed the attached Prospectus on the basis that you are a person into whose possession this Prospectus may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not nor are you authorised to deliver this Prospectus, electronically or otherwise, to any other person.

Restriction: Nothing in this electronic transmission constitutes an offer of securities for sale to persons other than the specified qualified institutional buyers described above and to whom it is directed and access has been limited so that it shall not constitute a general solicitation. If you have gained access to this transmission contrary to the foregoing restrictions, you will be unable to purchase any of the securities described therein.

To the fullest extent permitted by law, none of the Joint Lead Managers nor any of their respective affiliates accepts any responsibility whatsoever for the contents of this Prospectus or for any other statement, made or purported to be made by any of them or on its behalf in connection with the Company or the issue and offering of the securities described herein. Each Joint Lead Manager accordingly disclaims all and any liability whether arising in tort or contract or otherwise (save as referred to above) which it might otherwise have in respect of this Prospectus or any such statement.

The Joint Lead Managers are acting exclusively for the Company and no one else in connection with the offer. They will not regard any other person (whether or not a recipient of this Prospectus) as its client in relation to the offer and will not be responsible to anyone other than the Company for providing the protections afforded to its clients nor for giving advice in relation to the offer or any transaction or arrangement referred to herein.

You are responsible for protecting against viruses and other destructive items. Your receipt of the electronic transmission is at your own risk and it is your responsibility to take precautions to ensure that it is free from viruses and other items of a destructive nature.

JSC Georgian Railway

(a joint stock company organised under the laws of Georgia)

U.S.$500,000,000 7.75 per cent. Notes due 2022

Issue Price: 99.998 per cent.

The U.S.$500,000,000 7.75 per cent. Notes due 2022 (the "**Notes**") will be issued by JSC Georgian Railway (the "**Company**"). The Notes will mature on 11 July 2022, subject to the earlier redemption of any Note at the option of the relevant Noteholder following a Change of Control Event (each, as defined in "*Terms and Conditions of the Notes*") at its principal amount, together (if applicable) with accrued and unpaid interest thereon. The Notes will be unsecured and unsubordinated obligations of the Company and will rank equally in right of payment with the Company's existing and future unsecured and unsubordinated obligations (subject as described in Condition 3(a) (Negative Pledge) of the Notes).

Interest will accrue on the outstanding principal amount of the Notes at the rate of 7.75 per cent. per annum from and including 5 July 2012 (the "**Issue Date**") and will be payable semi-annually in arrear on 11 January and 11 July in each year, except that the first payment of interest will be made on 11 January 2013 in respect of the period from and including the Issue Date to but excluding 11 January 2013.

SEE "RISK FACTORS" FOR A DISCUSSION OF CERTAIN FACTORS TO BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE NOTES.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended (the "Securities Act"), or with any securities regulatory authority of any state or other jurisdiction of the United States, and may not be offered or sold within the United States, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The Notes will be offered and sold outside the United States in reliance on Regulation S under the Securities Act ("Regulation S") and within the United States only to "qualified institutional buyers" (as defined in Rule 144A under the Securities Act ("Rule 144A"), "QIBs" and, each, a "QIB"), in reliance on Rule 144A. Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. There will be no public offering of the Notes.

The Notes will be offered and sold in registered form in denominations of U.S.$200,000 or any amount in excess thereof, which is an integral multiple of U.S.$1,000. Notes, which are offered and sold in reliance on Regulation S (the "**Unrestricted Notes**"), will be represented, upon issuance, by beneficial interests in a global note (the "**Unrestricted Global Note**"), in registered form, without interest coupons attached, which will be registered in the name of a nominee for, and will be deposited on or about the Issue Date with a common depositary for, and in respect of interests held through, Euroclear Bank S.A./N.V. ("**Euroclear**") and Clearstream Banking, *société anonyme* ("**Clearstream, Luxembourg**"). Notes, which are offered and sold in reliance on Rule 144A (the "**Restricted Notes**"), will be represented, on issuance, by beneficial interests in a global Note (the "**Restricted Global Note**" and, together with the Unrestricted Global Note, the "**Global Notes**"), in registered form, without interest coupons attached, which will be deposited on or about the Issue Date with a custodian (the "**Custodian**") for, and registered in the name of Cede & Co. as nominee for, The Depository Trust Company ("**DTC**"). Interests in the Restricted Global Note will be subject to certain restrictions on transfer. Beneficial interests in the Global Notes will be shown on, and transfers thereof will be effected only through, records maintained by DTC, Euroclear, Clearstream, Luxembourg and their respective participants. Except in the limited circumstances set out in "*Provisions Relating to the Notes whilst in Global Form*", certificates will not be issued in exchange for beneficial interests in the Global Notes.

The Notes are expected to be rated BB- (outlook: stable) by Fitch Ratings Ltd. ("**Fitch**") and BB- (outlook: stable) by Standard and Poor's Credit Market Services Europe Limited ("**S&P**"). A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation. Any change in the rating of the Notes could adversely affect the price that a purchaser would be willing to pay for the Notes. As at the date of this Prospectus, both S&P and Fitch are established in the European Union and registered under Regulation (EU) No 1060/2009 on credit rating agencies, as amended (the "**CRA Regulation**").

Application has been made to the Financial Services Authority (the "**FSA**") in its capacity as competent authority under the Financial Services and Markets Act 2000 (the "**UK Listing Authority**") for the Notes to be admitted to the official list of the UK Listing Authority (the "**Official List**") and to the London Stock Exchange plc (the "**London Stock Exchange**") for the Notes to be admitted to trading on the London Stock Exchange's Regulated Market (the "**Market**"). References in this Prospectus to the Notes being "**listed**" (and all related references) shall mean that the Notes have been admitted to the Official List and have been admitted to trading on the Market. The Market is a regulated market for the purposes of the Markets in Financial Instruments Directive 2004/39/EC. There is no assurance that a trading market in the Notes will develop or be maintained.

Joint Lead Managers

BofA Merrill Lynch | **Goldman Sachs International**

J.P. Morgan

Prospectus dated 27 June 2012

This Prospectus comprises a prospectus for the purposes of Directive 2003/71/EC (the "**Prospectus Directive**") and for the purpose of giving information with regard to the Company, the Company and its consolidated subsidiaries taken as a whole and the Notes, which, according to the particular nature of the Company and the Notes, is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the Company, as well as the rights attaching to the Notes. The Company accepts responsibility for the information contained in this Prospectus. To the best of the knowledge of the Company (having taken all reasonable care to ensure that such is the case), the information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

No person has been authorised to give any information or to make any representation other than as contained in this Prospectus in connection with the offering of the Notes and, if given or made, such information or representation must not be relied upon as having been authorised by the Company or the Joint Lead Managers (as defined in "*Subscription and Sale*"). Neither the delivery of this Prospectus nor any offer or sale of the Notes made hereunder shall, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Company since the date hereof. The Joint Lead Managers expressly do not undertake to review the financial condition or affairs of the Company during the life of the Notes or to advise any investor in Notes of any information coming to their attention. This Prospectus may only be used for the purpose for which it has been published.

This Prospectus does not constitute an offer to sell or an offer to buy in any jurisdiction to any person to whom it is unlawful to make the offer or solicitation in such jurisdiction, nor does this Prospectus constitute an offer of, or an invitation to subscribe for, or purchase, any Notes and it should not be considered as a recommendation by the Company or any Joint Lead Manager that any recipient of this Prospectus should subscribe for or purchase any Notes. The Notes are subject to restrictions on transferability and resale and may not be transferred or resold except as permitted under the Securities Act and applicable state securities laws pursuant to registration thereunder or exemption therefrom. For a more complete description of restrictions on offers, sales and transfers, see "*Subscription and Sale*" and "*Transfer Restrictions*". The distribution of this Prospectus and the offering, sale and delivery of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Company and the Joint Lead Managers to inform themselves about and to observe any such restrictions. None of the Company and the Joint Lead Managers makes any representation to any recipient of this Prospectus regarding the legality of an investment in the Notes by such recipient under applicable investment or similar laws. Each investor should consult with its own advisers as to the legal, tax, business, financial and related aspects of its purchase of Notes. For a description of certain restrictions on offers, sales and deliveries of Notes, see "*Subscription and Sale*" and "*Provisions Relating to the Notes whilst in Global Form—The Global Notes*".

The Notes have not been registered with, recommended by or approved or disapproved by the United States Securities and Exchange Commission (the "**SEC**") or any other federal or state securities commission in the United States, nor has the SEC or any other federal or state securities commission confirmed the accuracy or determined the adequacy of this Prospectus. Any representation to the contrary is a criminal offence in the United States.

To the fullest extent permitted by law, the Joint Lead Managers accept no responsibility whatsoever for the contents of this Prospectus or for any other statement, made or purported to be made by a Joint Lead Manager or on its behalf in connection with the Company or the issue and offering of the Notes. Each Joint Lead Manager accordingly disclaims all and any liability whether arising in tort or contract or otherwise (save as referred to above) which it might otherwise have in respect of this Prospectus or any such statement.

Each recipient of this Prospectus shall be taken to have made its own investigation and appraisal of the condition (financial or otherwise) and status of the Company.

In connection with the issue of the Notes, Goldman Sachs International (the "**Stabilising Manager**") (or any person acting for the Stabilising Manager) may over-allot notes or effect transactions with a view to supporting the market price of the Notes at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the initial allotment of the

Notes. Any stabilisation action or over-allotment must be conducted by the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) in accordance with all applicable laws and rules.

This Prospectus has been prepared by the Company for use in connection with the offer and sale of the Notes outside the United States, the resale of the Notes in the United States in reliance on Rule 144A under the Securities Act and the admission of the Notes for listing on the London Stock Exchange. The Company and the Joint Lead Managers reserve the right to reject any offer to purchase the Notes, in whole or in part, for any reason. This Prospectus does not constitute an offer to any person in the United States other than any QIB to whom an offer has been made directly by a Joint Lead Manager or its United States broker-dealer affiliate. Distribution of this Prospectus to any person within the United States, other than any QIB and those persons, if any, retained to advise such QIB with respect thereto, is unauthorised and any disclosure without the prior written consent of the Company of any of its contents to any such person within the United States, other than any QIB and those persons, if any, retained to advise such QIB, is prohibited.

Prospective investors must determine the suitability of an investment in Notes in the light of their own respective circumstances. In particular, each prospective investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the Notes and the merits and risks of investing in Notes;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in Notes and the impact the Notes will have on their overall investment portfolios;
- have sufficient financial resources and liquidity to bear all of the risks of an investment in Notes;
- understand thoroughly the terms of the Notes and be familiar with the behaviour of any relevant financial markets; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for currency, economic, interest rate and other factors that may affect their investments and ability to bear the applicable risks.

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each prospective investor should consult its legal advisers to determine whether and to what extent: (i) the Notes are legal investments for it; (ii) the Notes can be used as collateral for various types of borrowing; and (iii) other restrictions apply to its purchase or pledge of the Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Notes under any applicable risk-based capital or similar rules.

ADDITIONAL INFORMATION

The Company has agreed that, so long as any Notes are ‘‘restricted securities’’ within the meaning of Rule 144(a)(3) of the Securities Act, the Company will, during any period in which it is neither subject to Section 13 or 15(d) of the United States Securities Exchange Act of 1934 (the "**Exchange Act**") nor exempt from reporting thereunder pursuant to Rule 12g3-2(b) under the Exchange Act, provide to any holder or beneficial owner of any such ‘‘restricted security’’, or to any prospective purchaser of such restricted security designated by such holder or beneficial owner, the information specified in, and meeting the requirements of, Rule 144A(d)(4) of the Securities Act upon the request of such holder or beneficial owner.

This Prospectus is being furnished by the Company in connection with an offering exempt from the registration requirements of the Securities Act solely for the purpose of enabling a prospective investor to consider the acquisition of Notes described herein. The information contained in this Prospectus has been provided by the Company and other sources identified herein.

NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES ("RSA") WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

ENFORCEABILITY OF JUDGMENTS

The Company is a joint stock company incorporated under the laws of Georgia. All of the Company's directors and executive officers reside outside the United Kingdom and the United States and all of the assets of the Company and its subsidiaries and of such persons are located outside of the United States and the United Kingdom. The Company has appointed an agent for service of process in England; however, it may not be possible for investors to effect service of process within the United States or the United Kingdom on the directors and executive officers of the Company or enforce judgments against such persons or the Company.

In addition, on the basis of certain precedents established by foreign judiciaries, it may not be possible to effect service of process against the Company in courts outside Georgia or in a jurisdiction to which the Company has not explicitly submitted. Pursuant to Article 68.2 of the *Law of Georgia on Private International Law*, foreign court judgments against the Company will not be recognised and enforceable in Georgian courts if:

(i) the matter is within the exclusive competence of Georgia;

(ii) there is a violation in the service of process or other procedures under the law of the country of the court which rendered the judgment;

(iii) a dispute involving the same subject matter between the same parties has already been decided by a Georgian court or by a foreign court, judgment of which has been recognised in Georgia;

(iv) the court rendering the judgment is not considered competent to adjudicate the dispute under Georgian legislation;

(v) the country whose court has rendered the judgment does not recognise judgments of Georgian courts;

(vi) a dispute involving the same subject matter between the same parties is already being heard in a Georgian court; or

(vii) the judgment of the foreign court contradicts fundamental principles of Georgian law.

Pursuant to Article 45.1 of the *Law of Georgia on Arbitration*, arbitral awards against the Company may not be recognised and enforceable in Georgia if:

(i) the party against whom the award is made proves before Georgian courts that:

   (a) a party to the arbitration lacked legal capacity;

   (b) the arbitration agreement is void or set aside pursuant to the law specified by the parties in the arbitration agreement or, in the absence of such, based on the laws of the place where the award was made;

   (c) a party was not duly informed about the appointment of an arbitrator or the arbitration proceedings, or was not able to participate in the proceedings for other valid reasons;

   (d) the arbitral tribunal issued the award on a subject matter beyond the scope of the arbitration agreement;

   (e) the composition of the arbitral tribunal or the procedure of the arbitration was not in accordance with the arbitration agreement, or, in the absence of such agreement, the arbitration was conducted in violation of the laws of the place of arbitration; or

   (f) the arbitral award has not yet become binding or has been set aside or suspended by the courts of the state in which, or under the laws of which, the award was made; or

(ii) the court establishes that:

(a) the subject matter of the dispute is not subject to arbitration under Georgian law; or

(b) the award is contrary to public policy.

No treaty exists between Georgia and many Western jurisdictions, including many EU jurisdictions, for the reciprocal enforcement of foreign court judgments.

In addition, the Terms and Conditions of the Notes are governed by English law and provide that disputes arising from or in connection with the Notes may be settled by arbitration. Georgia is a party to the United Nations (New York) Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (the "**New York Convention**"). Therefore, an arbitration award obtained in a country, which is also a party to the New York Convention, such as the United Kingdom, would be enforceable in Georgia, subject to the terms of the New York Convention and compliance with Georgian civil procedure regulations, the Law of Georgia on Arbitration and other procedures and requirements established by Georgian legislation. It may be difficult, however, to enforce arbitral awards in Georgia due to a number of factors, including the lack of experience of Georgian courts in international commercial transactions, certain procedural ambiguities and Georgian courts' inability to enforce such orders, all of which could introduce delay and unpredictability into the process of enforcing any foreign arbitral award in Georgia.

Furthermore, the choice of English law as the governing law of the Terms and Conditions of the Notes and the transaction documents may not be given effect, and the recognition or enforcement of foreign court judgments and arbitral awards may be limited, by application of the Georgian law principle requiring compliance with mandatory provisions of the law of the country most closely connected to the transaction, including mandatory provisions of Georgian law. The nature and scope of such mandatory provisions are subject to a considerable degree of discretionary authority of the court in which recognition or enforcement of the judgment or arbitral award is being sought.

THIRD-PARTY INFORMATION REGARDING THE COMPANY'S MARKET AND INDUSTRY

Statistical data appearing in "*Risk Factors*" and elsewhere in this Prospectus have, unless otherwise stated, been obtained from the National Bank of Georgia (the "**NBG**") and the National Statistics Office of Georgia ("**Geostat**"). Statistics are maintained by these sources in Lari (the national currency of Georgia) or U.S. Dollars, as applicable. Certain statistics recorded in currencies other than Lari have been converted into Lari at the exchange rates indicated in this Prospectus. Similar statistics may be obtained from other sources, although the underlying assumptions and methodology, and consequently the resulting data, may vary from source to source. Although every effort has been made to include in this Prospectus the most reliable and the most consistently presented data, no assurance can be given that such data was compiled or prepared on a basis consistent with international standards.

The information that the Company has obtained from the NBG, Geostat or other third party sources has been accurately reproduced in this Prospectus and, as far as the Company is aware and is able to ascertain from the information published by such sources, no facts have been omitted which would render the reproduced information inaccurate or misleading. Where third-party information has been used in this Prospectus, the source of such information has been identified.

FORWARD-LOOKING STATEMENTS

This Prospectus contains certain forward-looking statements with respect to the business, financial condition and results of operations of the Company and its consolidated subsidiaries and certain of the plans, intentions, expectations, assumptions, goals and beliefs of the Company regarding such items. These statements include all matters that are not historical fact and generally, but not always, may be identified by the use of words such as "believes", "expects", "are expected to", "anticipates", "intends", "estimates", "should", "will", "will continue", "may", "is likely to", "plans" or similar expressions, including variations and the negatives thereof or comparable terminology and include statements regarding:

- strategies, outlook and growth prospects;
- future plans, expectations and projections;
- expected future revenues and performance;
- expected future liquidity, capital resources and capital expenditures;
- expected future growth in demand for services;
- economic outlook and industry trends;
- market developments;
- the impact of regulatory initiatives;
- plans or intentions relating to acquisitions; and
- competitive strengths and weaknesses.

The forward-looking statements in this Prospectus 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 the Company's records and other data available from third parties. Although the Company believes 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 which are beyond its control, and the Company 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 the Company's view, could cause actual results to differ materially from those discussed in the forward-looking statements include, but are not limited to:

- overall economic and political conditions globally, in the Caucasus region and within Georgia and the continuing effects of the global financial crisis, the duration and magnitude of which cannot be ascertained;
- the Company's ability to overcome competition from oil pipelines and other alternative transit routes and providers of other methods of transport;
- the Company's ability to continue setting tariffs without regulation by the Government of Georgia (the "**Government**") or otherwise freely react to market forces;
- operational limitations, including equipment failures and maintenance and rehabilitation issues related to the age of its assets;
- the Company's ability to implement the Modernisation Project (as defined below);
- exchange rate, interest rate and inflation fluctuations;

- unplanned events or accidents affecting the Company's infrastructure;
- the Company's ability to achieve and maintain profitability in its Passenger SBU (as defined below);
- changes in laws, regulations, taxation or accounting standards or practices in Georgia; and
- the Company's success at managing the risks associated with the aforementioned factors.

The foregoing list is not exhaustive. When relying on forward-looking statements, potential investors should carefully consider the foregoing factors and other uncertainties and events, especially in light of the political, economic, social and legal environment in which the Company operates. Such forward-looking statements speak only as at the date on which they are made. Except to the extent required by law, including as required by the Listing Rules, Disclosure and Transparency Rules and Prospectus Rules published by the FSA, neither the Company nor any of its agents, employees or advisers intend or have any duty or obligation to supplement, amend, update or revise any of the forward-looking statements contained in this Prospectus.

The sections of this Prospectus entitled "*Risk Factors*", "*Management's Discussion and Analysis of Results of Operations and Financial Performance*" and "*Description of the Company's Business*" contain a more complete discussion of the factors that could affect the Company's future performance and the industry in which it operates. In light of these risks, uncertainties and assumptions, the forward-looking events described in this Prospectus may not occur.

Prospective investors should be aware that forward-looking statements are not guarantees of future performance and that the Company's actual business, financial condition and results of operations and prospects, as well as the development of the industry in which it operates, may differ significantly from those made in, or suggested by, the forward-looking statements contained in this Prospectus. In addition, even if the Company's business, financial condition and results of operations and prospects, as well as the development of the industry in which it operates, are consistent with the forward-looking statements contained in this Prospectus, those results or developments may not be indicative of results or developments in subsequent periods.

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

Financial Information

The Company's audited consolidated financial statements included in this Prospectus, together with the notes thereto, were prepared in accordance with International Financial Reporting Standards ("**IFRS**") as issued by the International Accounting Standards Board.

The Company's audited consolidated financial statements include:

- the Company's audited annual consolidated financial statements as at and for the year ended 31 December 2011, which include comparative financial information as at and for the year ended 31 December 2010 (the "**2011 Audited Consolidated Financial Statements**"); and

- the Company's audited annual consolidated financial statements as at and for the year ended 31 December 2010, which include comparative financial information as at and for the year ended 31 December 2009 (the "**2010 Audited Consolidated Financial Statements**" and, together with the 2011 Audited Consolidated Financial Statements, the "**Audited Consolidated Financial Statements**").

The 2010 Audited Consolidated Financial Statements and the 2011 Audited Consolidated Financial Statements in this Prospectus are those of Georgian Railway LLC, the predecessor company to the Company. On 12 April 2012, Georgian Railway LLC changed its corporate form from a limited liability company to a joint stock company and was re-registered under the name "JSC Georgian Railway" in accordance with the *Law on Entrepreneurs*.

The Audited Consolidated Financial Statements of the Company's predecessor, Georgian Railway LLC, are included in this Prospectus and have been audited and the Company's unaudited condensed consolidated interim financial statements as at and for the three-month periods ended 31 March 2012 and 2011 (the "**First Quarter Condensed Consolidated Financial Statements**") have been reviewed by the Tbilisi branch of KPMG CIS Limited ("**KPMG**") of 4 Besiki Street Tbilisi, 0108 Georgia, as stated in their reports appearing herein. The First Quarter Condensed Consolidated Financial Statements, together with the notes thereto, were prepared in accordance with IAS 34 (*Interim Financial Reporting*).

The review report of the Tbilisi branch of KPMG CIS Limited in respect of the First Quarter Condensed Consolidated Financial Statements contains an "emphasis of matter", which draws attention to the fact that the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011, excluding the adjustments described in Note 18 to the First Quarter Condensed Consolidated Financial Statements, were based on the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011 that were approved for issuance by the Company on 15 May 2011. Such statements were neither audited nor reviewed. As part of preparing the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2012, management adjusted the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011. The Tbilisi branch of KPMG CIS Limited has reviewed the adjustments made and has stated in its review report that nothing has come to its attention that causes it to believe that such adjustments have not been properly applied.

The Audited Consolidated Financial Statements and the First Quarter Condensed Consolidated Financial Statements (together, the "**Consolidated Financial Statements**"), together with the respective notes thereto, are included in this Prospectus beginning on page F-2.

As the offered securities have not been and will not be registered under the Securities Act, KPMG has not filed a consent under the Securities Act.

Other Financial Information

This Prospectus includes non-IFRS measures and ratios, including EBITDA, EBITDA margin, adjusted EBITDA and adjusted EBITDA margin. EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses. EBITDA margin is EBITDA divided by revenue. Adjusted EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses, certain items included in other expenses (write-off of non-current assets, inventory write-downs due to obsolescence, guarantee provisions and other provisions) and certain items included in other income (gain on sale of subsidiaries and associates, and other). Adjusted EBITDA margin is adjusted EBITDA divided by revenue. EBITDA, EBITDA margin, adjusted EBITDA, adjusted EBITDA margin and other non-IFRS measures should not be considered in isolation or as an alternative to results from operating activities, cash flow from operating activities or other financial measures of the

Company's results of operations or liquidity derived in accordance with IFRS. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a reconciliation of EBITDA and adjusted EBITDA to profit and total comprehensive income for the period. The Company includes EBITDA, EBITDA margin, adjusted EBITDA and adjusted EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. These non-IFRS measures are not audited.

Currencies

In this Prospectus: all references to "**Lari**" or "**GEL**" are to the lawful currency of Georgia; all references to "**U.S. Dollars**" or "**U.S.$**" are to the lawful currency of the United States of America; all references to "**Euro**" or "**€**" are to the single currency of the participating member states of the European and Monetary Union of the Treaty Establishing the European Community, as amended from time to time; and all references to "**CHF**" or "**Swiss Francs**" are to the lawful currency of Switzerland.

This Prospectus contains translations of certain Lari amounts into U.S. Dollars or Swiss Francs and certain of Swiss Franc amounts into Lari, at specified rates solely for the convenience of the reader. These translations should not be construed as representations that the Lari or Swiss Franc amounts actually represent such equivalent U.S. Dollar, Swiss Franc or Lari amounts, as the case may be, or could be or could have been converted into U.S. Dollars or Swiss Francs at the rate indicated as at the dates mentioned herein or at all.

Unless otherwise indicated, such U.S. Dollar amounts have been translated from Lari at an exchange rate of GEL 1.6600 = U.S.$1.00, being the rate as set by the NBG for 31 March 2012 or 1.6703 = U.S.$1.00, being the rate as set by the NBG for 31 December 2011. The U.S. Dollar exchange rate at 14 June 2012 was GEL 1.6341 = U.S.$1.00. Unless otherwise indicated, such Swiss Franc amounts have been translated from Lari at an exchange rate of GEL 1.7780 = CHF 1.00, being the rate as set by the NBG for 31 December 2011. The Swiss Franc exchange rate at 14 June 2012 was GEL 1.7061 = CHF 1.00. Unless otherwise indicated, such Lari amounts have been translated from Swiss Francs at an exchange rate of CHF 0.5624 = GEL 1.00, being the rate as set by the NBG for 31 December 2011. The Lari exchange rate at 14 June 2012 was CHF 0.5861 = GEL 1.00. See "*Exchange Rate Information*".

Rounding

Certain numerical figures set out in this Prospectus, including financial data presented in thousands and millions and percentages, have been subject to rounding adjustments and, as a result, the totals of the data in this Prospectus may vary slightly from the actual arithmetic totals of such information. Percentages and amounts reflecting changes over time periods relating to financial and other data set out in "*Management's Discussion and Analysis of Results of Operations and Financial Condition*" are calculated using the numerical data in the Consolidated Financial Statements or the tabular presentation of other data (subject to rounding) contained in this Prospectus, as applicable, and not using the numerical data in the narrative description thereof. Accordingly, in certain instances the sum of the numbers in a column or a row in tables contained in this Prospectus may not conform exactly to the total figure given for that column or row. Some percentages in tables in this Prospectus have also been rounded and accordingly the totals in these tables may not add up to 100 per cent.

Definitions

Unless otherwise noted, references to "management" are to the members of the Company's supervisory board (the "**Supervisory Board**") and management board (the "**Board of Directors**"), and statements as to the Company's or the Company's beliefs, expectations, estimates and opinions are to those of the Company's management.

Industry and Market Data

Market data used in this Prospectus have been extracted from official and industry sources and other sources the Company believes to be reliable, including from the NBG and other public sources in Georgia, as well as the Company's knowledge of its volumes and markets and assessments made by management. Certain statistics are maintained by these sources in Lari, U.S. Dollars or Swiss Francs, as applicable. Similar statistics may be obtained from other sources, although the underlying assumptions and methodology, and consequently the resulting data, may vary from source to source. Although every effort has been made to include in this Prospectus the most reliable and the most consistently presented data, no assurance can be given that such data were compiled or prepared on a basis consistent with international standards. While the Company has compiled, extracted and reproduced market or other industry data from external sources, including third parties or industry or general publications, neither the Company nor the Joint Lead Managers have independently verified that data. In addition, industry publications generally state that their information is obtained from sources they believe to be reliable, but that the accuracy and completeness of such information is not guaranteed and that the projections they contain are based on a number of significant assumptions.

The Company has relied on the accuracy of such data and statements without carrying out an independent verification thereof, and therefore cannot guarantee their accuracy and completeness. Furthermore, management believes that its estimates and assessments are accurate and reliable, however, they have not been verified by independent external professionals.

The information described above has been accurately reproduced and, as far as the Company is aware and is able to ascertain from the information published by such sources, no facts have been omitted which would render the reproduced information inaccurate or misleading. Information in this Prospectus that has been sourced from a third party is identified as such together with the name of the third party source.

General Information

Neither the contents of the Company's website, or any of the Company's subsidiaries' websites (or any other website), nor the content of any website accessible from hyperlinks on the Company's or any of its subsidiaries' websites (or any other website), is incorporated into, or forms part of, this Prospectus.

EXCHANGE RATE INFORMATION

The following table sets forth, at the dates and for the periods indicated, the period-end, average and high and low official rates set by the NBG, in each case for the purchase of Lari, all expressed in Lari per U.S. Dollar. The Federal Reserve Bank of New York does not report a noon buying rate for Lari.

	Lari per U.S.$1.00			
	High	**Low**	**Average**(1)	**Period end**
Year				
2009	1.70	1.64	1.67	1.69
2010	1.89	1.69	1.78	1.77
2011	1.81	1.64	1.69	1.67
Month				
January 2012	1.67	1.67	1.67	1.67
February 2012	1.67	1.62	1.66	1.66
March 2012	1.68	1.64	1.65	1.66
April 2012	1.66	1.63	1.64	1.63
May 2012	1.63	1.62	1.63	1.63

(1) The average exchange rate for the year is the average of the daily exchange rates for the year. The average exchange rate for the month is the average of the daily exchange rates for each month.

The Lari/U.S. Dollar exchange rate set by the NBG reported on 14 June 2012 was GEL 1.6341 to U.S.$1.00.

The following table sets forth, for the periods indicated, the period-end, average and high and low official rates set by the NBG, in each case for the purchase of Lari, expressed in Lari per Swiss Franc:

	Lari per CHF 1.00			
	High	**Low**	**Average**(1)	**Period end**
Year				
2009	1.68	1.41	1.54	1.63
2010	1.89	1.53	1.71	1.89
2011	2.28	1.75	1.91	1.78
Month				
January 2012	1.82	1.75	1.78	1.80
February 2012	1.85	1.77	1.82	1.85
March 2012	1.86	1.78	1.81	1.84
April 2012	1.84	1.78	1.79	1.79
May 2012	1.80	1.68	1.74	1.68

(1) The average exchange rate for the year is the average of the daily exchange rates for the year. The average exchange rate for the month is the average of the daily exchange rates for each month.

The Lari/Swiss Franc exchange rate set by the NBG reported on 14 June 2012 was GEL 1.7061 to CHF 1.00.

The rates set out above may differ from the actual rates used in the preparation of the Company's Consolidated Financial Statements and other financial information appearing in this Prospectus.

Fluctuations in the exchange rates between the Lari and the U.S. Dollar or the Lari and the Swiss Franc in the past are not necessarily indicative of fluctuations that may occur in the future. No representation is made that Lari amounts referred to in this Prospectus could have been or could be converted into U.S. Dollars or Swiss Francs at the above exchange rates or at any other rate at all.

OVERVIEW OF THE COMPANY

This section contains an overview of the detailed information and financial information included elsewhere in this Prospectus. This overview may not contain all of the information that may be material to prospective investors and, therefore, should be read in conjunction with this entire Prospectus, including the more detailed information regarding the Company's business and financial information and related notes included elsewhere in this Prospectus. Prospective investors should also carefully consider the information set forth under the heading "Risk Factors".

Overview

JSC Georgian Railway is, by statute, Georgia's only railway operator. It principally provides freight services, transhipping a variety of cargo, including oil, oil products, ores and grains, originating principally in the east from the Caspian Sea and Central Asia to the Black Sea. The Company also provides passenger services. It has a vertically integrated business model, owning and operating the tracks, stations, other infrastructure and rolling stock comprising Georgia's entire national railway system, as well as the land adjoining the tracks. The Company sets its own tariffs without the need to obtain governmental approval.

The Company's mainline rail network, together with that of CJSC Azerbaijan Railway ("**Azerbaijan Railway**"), forms the Caucasus railway corridor, a key segment of the Transport Corridor Europe Caucasus Asia ("**TRACECA**") corridor. The Company's mainline rail network is thus a link in the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. As a key link in the transportation chain between Europe and Central Asia, the Company believes that it is uniquely positioned to capitalise on trade between Europe and the Caspian Region and Central Asia. Three of the Company's lines terminate at the Black Sea, at the Georgian port cities of Batumi, Kulevi and Poti. Access to these ports allows easy on-shipment of transit cargo to the Mediterranean basin and Europe.

The Company operates the national railway system through three strategic business units, or SBUs: the Freight SBU, which provides freight traffic (transportation and handling) and freight car rental services; the Passenger SBU, which primarily transports passengers within Georgia; and the Infrastructure SBU, which operates, maintains and manages the Company's principal infrastructure assets. The Infrastructure SBU provides services only to the Freight SBU and the Passenger SBU and does not conduct business with third-party customers. For the year ended 31 December 2011, the Company transported 20.12 million tonnes of freight and carried 3.3 million passengers.

The Freight SBU accounted for over 90 per cent. of the Company's total revenue in the first quarter of 2012 and each of 2011, 2010 and 2009. The Company transports both liquid cargoes (crude oil and oil products) and various dry cargoes, with liquid cargoes accounting for 52.0 per cent. of the Company's total freight transportation volumes in the year ended 31 December 2011. Transport of crude oil across the Company's rail network is an alternative to oil pipelines, and the crude oil transported by the Company primarily originates in Kazakhstan and Azerbaijan. Given its strategic location, as producers seek to diversify their transportation options, the Caucasus corridor should capture a relatively stable share of the crude oil transported in the region, which management estimates should be approximately eight to ten per cent. of total Kazakhstan and Azerbaijan production.

For the year ended 31 December 2011, the Company had consolidated revenue of GEL 477.4 million, profit and total comprehensive income for the year of GEL 174.4 million and EBITDA of GEL 259.9 million, as compared to consolidated revenue of GEL 404.7 million, profit and total comprehensive income for the year of GEL 101.5 million and EBITDA of GEL 194.8 million for the year ended 31 December 2010.

Recent Developments

Since 31 March 2012, the following developments have occurred that may affect the Company's financial condition and results of operations in the future:

- In March 2012, the Company declared a dividend in the total amount of GEL 28 million in respect of the Company's 2011 profits. The Company paid GEL 10 million of this dividend in April 2012 and the balance of GEL 18 million in a second instalment in May 2012.

- In April 2012, the Company and the Government, represented by the Ministry of Finance and the Ministry of Economy and Sustainable Development (the "**MESD**"), entered into a memorandum of understanding (the "**Bypass Project Memorandum**") in respect of the Bypass Project (as defined below). The Bypass Project Memorandum creates a set-off mechanism for the Company to be reimbursed by the State of Georgia (the "**State**") for the Company's future expenses in relation to the Bypass Project out of dividends that would otherwise be payable to the State in respect of its shares in the Company and in exchange for the transfer, by the Company to the State, of land plots in central Tbilisi freed up as a result of the Bypass Project (the "**Existing Railway Land**"). The amount to be reimbursed to the Company does not cover an instalment of CHF 36.1 million due to be paid by the Company to its contractor in 2012 and is subject to an aggregate cap of CHF 138.0 million. In May 2012 and to date in June 2012, the Company paid to its contractor approximately GEL 20.4 million (CHF 11.9 million) and GEL 5.0 million (CHF 2.9 million), respectively, of the CHF 36.1 million not covered by the reimbursement obligation, with the balance to be paid by the Company out of its existing cash flows upon the completion of the corresponding work by the contractor. The Existing Railway Land will be transferred to the State upon completion of the Bypass Project or, if later, upon the full reimbursement of reimbursable expenses by the Government. If the dividends payable to the State are insufficient to cover the reimbursable expenses in full, the Company has the right to retain a *pro rata* ownership interest in the Existing Railway Land.

- On 18 June 2012, the Company invited certain holders of the U.S.$250,000,000 9.875 per cent. Notes due 2015 issued by the Company on 22 July 2010 (the "**2010 Notes**") to tender any and all such notes for purchase by the Company for cash (the "**2010 Notes Tender**") at a price of U.S.$1,112.50 for each U.S.$1,000 in principal amount, together with accrued and unpaid interest to the relevant settlement date for tender, subject to certain terms and conditions and restrictions, as set out in a Tender Offer Memorandum dated 18 June 2012 relating to such invitation. On 26 June 2012, the Company announced that, subject to its receipt of sufficient proceeds from the issue of the Notes to provide financing for the payment of the amounts payable under the 2010 Notes Tender, it will accept for purchase U.S.$222,480,000 in aggregate principal amount of 2010 Notes pursuant to the 2010 Notes Tender. Subject as described above, the 2010 Notes Tender is expected to be completed on or about 5 July 2012.

Credit Ratings

As at the date of this Prospectus, the Company is rated by two rating agencies: Fitch and S&P. The Company has been assigned a long-term issuer default rating of BB- by Fitch and a long-term corporate credit rating of BB- by S&P, in each case with a stable outlook. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

Each of S&P and Fitch is established in the EU and registered under the CRA Regulation. As such, each of S&P and Fitch is included on the list of credit agencies published by the European Securities and Markets Authority on its website in accordance with the CRA Regulation as of the date of this Prospectus.

Competitive Strengths

The Company believes that it has a number of key competitive strengths that will enable it to capitalise on its leading position in the Georgian and Caucasus transportation markets in the future. These include:

- A unique strategic location with highly attractive market fundamentals
- A well invested asset base
- A favourable regulatory framework and strong Government support
- A track record of resilient and profitable growth with further upside
- A high quality customer portfolio
- An experienced management team with proven track record of delivery

Strategy

The Company's strategic objective is to consistently achieve profitability levels above the industry average. The key elements of its strategy are to:

- Continue to grow its freight service business, while increasing geographic diversification
- Focus on core business activities

- Maintain competitiveness of the Caucasus corridor and attract and retain customers through a flexible tariff policy

- Maintain a lean and efficient cost structure to continue increasing profitability

- Develop and modernise its infrastructure

Strategic Projects

The Company is undertaking two major strategic projects:

- The "**Modernisation Project**", whose key objectives include optimising traffic, rolling stock and infrastructure; reducing operational expenses; improving safety; and increasing train speeds. The Company expects to complete the Modernisation Project by 2016.

- The "**Bypass Project**", whose objective is to relocate certain railway infrastructure components from the centre of Tbilisi to the northern part of the city. Management is working with contractors to determine a projected completion date for the Bypass Project.

SUMMARY HISTORICAL FINANCIAL AND OPERATING INFORMATION

This section should be read together with the information contained in "Presentation of Financial and Other Information", "Use of Proceeds", "Capitalisation", "Selected Historical Financial and Operating Information", "Management's Discussion and Analysis of Results of Operations and Financial Condition", the Consolidated Financial Statements and the respective notes thereto included elsewhere in this Prospectus.

The following summary of consolidated historical financial information as at and for the three-month periods ended 31 March 2012 and 2011 and for the years ended 31 December 2011, 2010 and 2009 has been extracted from the Consolidated Financial Statements, included elsewhere in this Prospectus, other than non-IFRS measures and to the extent such financial information has been translated into U.S. Dollars.

Summary Statement of Comprehensive Income Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[1]	*(GEL millions)*	
Revenue	63.7	105.8	103.4
Other income	3.4	5.7	4.0
Employee benefits expense	(14.3)	(23.8)	(26.3)
Depreciation and amortisation expense	(14.9)	(24.8)	(23.0)
Electricity and materials used	(7.4)	(12.3)	(12.7)
Other expenses	(8.9)	(14.7)	(20.5)
Results from operating activities	**21.6**	**35.9**	**24.9**
Finance income	6.3	10.4	10.9
Finance costs	(4.0)	(6.6)	(1.5)
Net finance income	**2.3**	**3.9**	**9.4**
Profit before income tax	**23.9**	**39.7**	**34.3**
Income tax expenses	(4.0)	(6.6)	(5.7)
Profit and total comprehensive income for the period	**19.9**	**33.1**	**28.5**

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions)[(1)]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
Revenue	283.2	477.4	404.7	318.8
Other income	7.1	12.0	17.8	10.7
Payroll expenses	(64.4)	(108.5)	(111.3)	(106.1)
Depreciation and amortisation expenses	(54.6)	(92.1)	(98.7)	(96.1)
Raw materials and consumables used	(28.4)	(47.8)	(44.6)	(40.3)
Other expenses	(43.4)	(73.2)	(71.8)	(64.1)
Results from operating activities	**99.5**	**167.8**	**96.1**	**22.8**
Finance income	16.0	27.0	45.4	0.6
Finance costs	(6.2)	(10.5)	(17.7)	(4.8)
Net finance income/(costs)	**9.8**	**16.5**	**27.7**	**(4.2)**
Profit before income tax	**109.3**	**184.3**	**123.8**	**18.7**
Income tax expense	(5.9)	(9.9)	(22.3)	(2.9)
Profit and total comprehensive income for the year	**103.4**	**174.4**	**101.5**	**15.8**

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Summary Statement of Financial Position Data

	As at 31 March		As at 31 December			
	2012		2011		2010	2009
	(U.S.$ millions)[1]	*(GEL millions)*	*(U.S.$ millions)*[2]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
ASSETS						
Non-current assets						
Property, plant and equipment	1,192.5	1,979.5	1,145.4	1,913.2	1,725.6	1,699.9
Investment property	—	—	4.1	6.8	9.9	9.9
Other non-current assets	137.2	227.8	165.2	276.0	136.4	12.8
Total non-current assets	**1,329.7**	**2,207.3**	**1,314.8**	**2,196.1**	**1,871.9**	**1,722.7**
Current assets						
Non-current assets held for distribution	19.9	33.0	—	—	—	—
Inventories	13.9	23.1	14.2	23.7	18.0	23.7
Current tax assets	—	—	0.3	0.5	—	4.6
Trade and other receivables	19.2	31.8	16.4	27.4	26.9	22.2
Prepayments and other current assets	34.6	57.4	16.6	27.7	42.7	35.1
Cash and cash equivalents	25.4	42.1	38.6	64.5	335.9	1.4
Bank deposits	52.5	87.2	45.7	76.4	38.0	—
Total current assets	**165.4**	**274.6**	**131.9**	**220.3**	**461.4**	**87.0**
Total assets	**1,495.1**	**2,481.9**	**1,446.7**	**2,416.4**	**2,333.4**	**1,809.6**
EQUITY AND LIABILITIES						
Equity						
Charter capital	596.7	990.6	599.0	1,000.5	985.4	967.2
Non-cash owner contribution reserve	22.9	38.0	22.8	38.0	35.4	25.3
Retained earnings	463.0	768.6	457.1	763.5	612.3	556.2
Total equity	**1,082.7**	**1,797.2**	**1,078.8**	**1,802.0**	**1,633.0**	**1,548.7**
Non-current liabilities						
Loans and borrowings	248.1	411.8	247.9	414.1	438.4	24.9
Trade and other payables	0.0	0.0	0.0	0.05	0.05	28.9
Deferred tax liabilities	36.1	60.0	36.5	60.9	66.5	74.8
Total non-current liabilities	**284.2**	**471.7**	**284.4**	**475.0**	**504.9**	**128.6**
Current liabilities						
Loans and borrowings	5.0	8.3	11.1	18.6	19.3	3.9
Trade and other payables	48.9	81.2	27.5	46.0	61.9	66.0
Liabilities to the owner	13.4	22.3	7.9	13.2	29.2	26.6
Provisions	11.9	19.8	12.2	20.3	21.6	6.1
Other taxes payable	20.1	33.4	16.1	26.9	27.2	21.8
Dividends payable	7.8	12.9	—	—	—	—
Other current liabilities	16.9	28.0	8.6	14.4	15.0	8.0
Current tax liabilities	4.5	7.5	0.0	—	21.2	—
Total current liabilities	**128.6**	**213.4**	**83.4**	**139.3**	**195.4**	**132.4**
Total liabilities	**412.5**	**684.7**	**367.8**	**614.3**	**700.3**	**261.0**
Total equity and liabilities	**1,495.1**	**2,481.9**	**1,446.7**	**2,416.4**	**2,333.4**	**1,809.6**

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(1) For convenience, these figures have been translated into U.S.$ at the period-end GEL/U.S.$ exchange rate published by the NBG for 31 March 2012, which was GEL 1.6600 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) For convenience, these figures have been translated into U.S.$ at the period-end GEL/U.S.$ exchange rate published by the NBG for 31 December 2011, which was GEL 1.6703 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Summary Cash Flow Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)(1)	*(GEL millions)*	
Net cash from operating activities	30.5	50.7	49.1
Net cash used in investing activities	(33.5)	(55.7)	(91.7)
Net cash used in financing activities	(12.3)	(20.5)	(22.3)
Net decrease in cash and cash equivalents	(15.4)	(25.5)	(64.9)
Cash and cash equivalents at 1 January	37.1	61.6	323.9
Effect of exchange rate fluctuations on cash and cash equivalents	1.8	3.0	(6.7)
Cash and cash equivalents at 31 March	23.5	39.0	252.3

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions)(1)	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
Net cash from operating activities	134.0	225.9	231.5	116.7
Net cash used in investing activities	(270.2)	(455.6)	(322.0)	(89.4)
Net cash from/(used in) financing activities	(14.2)	(23.9)	390.1	(29.2)
Net increase/(decrease) in cash and cash equivalents	(150.4)	(253.6)	299.6	(1.9)
Cash and cash equivalents at 1 January	192.1	323.9	1.4	3.2
Effect of exchange rate fluctuations on cash and cash equivalents	(5.2)	(8.8)	23.0	0.1
Cash and cash equivalents at 31 December	36.5	61.6	323.9	1.4

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Other Financial and Operating Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[1]	*(GEL millions)*	
Other Financial Data			
EBITDA[2]	36.5	60.6	47.9
EBITDA Margin[2] (*per cent.*)	—	57.3	46.4
Adjusted EBITDA[3]	35.7	59.3	50.1
Adjusted EBITDA Margin[3] (*per cent.*)	—	56.0	48.4
Selected Operating Data			
Freight volume (*million tonnes*)	—	4.5	4.6
Number of passengers (*millions*)	—	0.7	0.7
Number of working freight cars	—	8,269	8,002
Number of employees	—	12,698	13,997

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses. EBITDA margin is EBITDA divided by revenue. EBITDA and EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to results from operating activities or cash flows from operating activities or as a measure of liquidity or as an indicator of the Company's operating performance or any other measure of performance derived in accordance with IFRS. The Company includes EBITDA, EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(3) Adjusted EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses, certain items included in other expenses (write-off of non-current assets, inventory write-downs due to obsolescence, guarantee provisions and other provisions) and certain items included in other income (gain on sale of subsidiaries and associates, and other). Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Adjusted EBITDA and adjusted EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to cash flows from operating activities or as measures of liquidity or an indicator of the Company's operating performance or any other measures of performance derived in accordance with IFRS. The Company includes adjusted EBITDA, adjusted EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(4) Debt is comprised of current loans and borrowings and non-current loans and borrowings.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions, except as noted)[1]	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*
Other Financial Data				
EBITDA[2]	154.2	259.9	194.8	118.9
EBITDA Margin[2](*per cent.*)	—	54.4	48.1	37.3
Adjusted EBITDA[3]	154.6	260.6	204.4	124.1
Adjusted EBITDA Margin[3] (*per cent.*)	—	54.6	50.5	38.9
Selected Ratios				
Net cash from operations to debt[4]	—	0.5	0.5	4.1
Debt[4] to Adjusted EBITDA[3]	—	1.7	2.2	0.2
Debt[4] to total equity	—	0.24	0.28	0.02
Selected Operating Data				
Freight volume (*million tonnes*)	—	20.1	19.9	17.1
Number of passengers (*millions*)	—	3.3	3.2	3.1
Number of working freight cars	—	8,122	7,659	7,910
Number of employees	—	13,227	14,335	15,100

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses. EBITDA margin is EBITDA divided by revenue. EBITDA and EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to results from operating activities or cash flows from operating activities or as a measure of liquidity or as an indicator of the Company's operating performance or any other measure of performance derived in accordance with IFRS. The Company includes EBITDA, EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(3) Adjusted EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses, certain items included in other expenses (write-off of non-current assets, inventory write-downs due to obsolescence, guarantee provisions and other provisions) and certain items included in other income (gain on sale of subsidiaries and associates, and other). Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Adjusted EBITDA and adjusted EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to cash flows from operating activities or as measures of liquidity or an indicator of the Company's operating performance or any other measures of performance derived in accordance with IFRS. The Company includes adjusted EBITDA, adjusted EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(4) Debt is comprised of current loans and borrowings and non-current loans and borrowings. See Note 19 to the 2011 Audited Consolidated Financial Statements.

OVERVIEW OF THE OFFERING

The following is an overview of the terms of the Notes. This overview is derived from, and should be read in conjunction with, the full text of the Terms and Conditions of the Notes, which prevail to the extent of any inconsistency with the terms set out in this overview. Capitalised terms used herein and not otherwise defined have the respective meanings given to such terms in the relevant Terms and Conditions of the Notes.

Company	JSC Georgian Railway
Issue	U.S.$500,000,000 7.75 per cent. Notes due 2022
Issue Price	99.998 per cent. of the principal amount of the Notes.
Interest	The Notes will bear interest at the rate of 7.75 per cent. per annum from and including 5 July 2012 (the Issue Date) to but excluding 11 July 2022 (subject to early redemption). Interest on the Notes will be payable semi-annually in arrear on 11 January and 11 July in each year, except that the first payment of interest will be made on 11 January 2013 in respect of the period from and including the Issue Date to but excluding 11 January 2013.
Maturity Date..	11 July 2022
Use of Proceeds	The Company intends to use the net proceeds of the issue of the Notes for general corporate and liquidity management purposes, which may include (i) financing of such amounts (if any) as may become payable in connection with the 2010 Notes Tender and (ii) the payment of dividends in respect of cumulative profits for 2011 and prior years to the extent such dividends may be recommended by the Company and approved by its shareholders. See "*Use of Proceeds*".
Joint Lead Managers.................................	Goldman Sachs International, J.P. Morgan Securities Ltd. and Merrill Lynch International
Fiscal Agent and Principal Paying and Transfer Agent..	Citibank, N.A., London Branch
Registrar and Paying and Transfer Agent	Citigroup Global Markets Deutschland AG
Negative Pledge; Restriction on Certain Corporate Reorganisations; Financial Reporting Obligations; Limitation on Incurrence of Financial Indebtedness; Limitation on Restricted Payments..........	The Terms and Conditions of the Notes will contain a negative pledge provision, a restriction on certain corporate reorganisations, financial reporting obligations, a covenant restricting the incurrence of Financial Indebtedness (as defined in Condition 3) by reference to a Net Financial Indebtedness (as defined in Condition 3) to EBITDA ratio and a covenant limiting Restricted Payments (as defined in Condition 3). See "*Terms and Conditions of the Notes—Covenants*".
Redemption by Noteholder	If, at any time, Georgia ceases to own, directly or indirectly, more than 50 per cent. of the Company's issued share capital or otherwise ceases to control, directly or indirectly, the Company, the Company shall, at the option of any Noteholder, upon such Noteholder giving notice at any time during the relevant period, redeem the Notes held by such Noteholder on the relevant date at the principal amount thereof, together (if applicable) with accrued and unpaid interest thereon to but excluding the date fixed for redemption, as further described in "*Terms and Conditions of the Notes—Redemption and Purchase*".

Cross-acceleration	The Terms and Conditions of the Notes will contain a cross acceleration provision. See "*Terms and Conditions of the Notes—Events of Default*".
Form and Denomination	The Notes will be offered and sold in registered form, in denominations of U.S.$200,000 and integral multiples of U.S.$1,000 in excess thereof. The Notes will initially be issued in the form of an Unrestricted Global Note and a Restricted Global Note, each in registered form and without interest coupons. The Unrestricted Global Note will be deposited with, and registered in the name of, a nominee for a common depositary for Euroclear and Clearstream, Luxembourg. The Restricted Global Note will be deposited with a custodian for, and registered in the name of Cede & Co., as nominee for, DTC. Ownership interests in the Unrestricted Global Note and the Restricted Global Note will be shown on, and transfers thereof will be effected only through, records maintained by DTC, Euroclear, Clearstream, Luxembourg and their respective participants. Notes in definitive form will be issued only in very limited circumstances.
Taxation	All payments of principal and interest by or on behalf of the Company in respect of the Notes shall be made free and clear of, and without withholding or deduction for, any taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or within Georgia or any political subdivision thereof or any authority therein or thereof having power to tax, in accordance with "*Terms and Conditions of the Notes—Taxation*", unless such withholding is required by law, in which event, the Company shall, save in certain circumstances provided in "*Terms and Conditions of the Notes—Taxation*", pay such additional amounts as will result in receipt by the Noteholders of such amounts as would have been received by them had no such withholding or deduction been required.
Listing and Trading	Application has been made to the UK Listing Authority for the Notes to be admitted to the Official List and to the London Stock Exchange for the Notes to be admitted to trading on the Market.
Selling Restrictions	There are restrictions on the offer, sale and transfer of the Notes in the United States, the United Kingdom and Georgia. See "*Subscription and Sale*".
Governing Law	The Notes will be governed by, and shall be construed in accordance with, English law.
Ratings	The Notes are expected to be rated BB- (outlook: stable) by Fitch and BB- (outlook: stable) by S&P. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation. Any change in the rating of the Notes could adversely affect the price that a purchaser would be willing to pay for the Notes. As at the date of this Prospectus, both Fitch and S&P are established in the European Union and registered under the CRA Regulation.
Risk Factors	Prospective purchasers of the Notes should consider carefully all of the information set forth in this Prospectus and, in particular, the information set forth under "*Risk Factors*" below before making an investment in the Notes.

Security Codes..	**Unrestricted Notes:**		
	ISIN:	XS0800346362	
	Common Code:	080034636	
	Restricted Notes:		
	ISIN:	US37363BAA61	
	Common Code:	080082215	
	CUSIP:	37363B AA6	

RISK FACTORS

An investment in the Notes involves a high degree of risk. Prospective investors should carefully consider the risks described below and the other information contained in this Prospectus before making a decision to invest in the Notes. Any of the following risks, individually or together, could adversely affect the Company's business, results of operations, financial condition and prospects, in which case the trading price of the Notes could decline and investors could lose all or part of their investment.

The Company has described the risks and uncertainties that the Company believes are material, but these risks and uncertainties may not be the only ones the Company faces. Additional risks and uncertainties of which the Company is currently not aware or which the Company currently deems immaterial may also have a material adverse effect on the Company's business, results of operations, financial condition and prospects. Prospective investors should be aware that the value of the Notes may go down as well as up and that investors may not be able to realise their initial investment.

Risks Related to the Company's Business

The Company's results of operations and financial condition are affected by economic and political conditions globally, in the Caucasus region and in Georgia

The Company's railway network comprises a key segment of the TRACECA corridor, the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. A significant portion of the Company's freight operations (which accounted for 95.3 per cent. of the Company's total revenue in the year ended 31 December 2011 and 93.4 per cent. in the year ended 31 December 2010) are derived from the transport of goods through Georgia from or to neighbouring countries whose rail networks, together with Georgia's, comprise the TRACECA corridor. The Company's financial condition and results of operations are, therefore, significantly influenced by the overall economic and political conditions affecting both Georgia and neighbouring countries. The Company is also affected by economic and political conditions in other countries to or from which goods that transit through the TRACECA corridor are ultimately shipped. The Company's transportation of liquid cargoes (crude oil and oil products) accounted for 52.0 per cent. and 57.8 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively. Transit of crude oil across the Company's rail network is an alternative to oil pipelines, and the Company's liquid cargo transit shipments accounted for 45.5 per cent. and 51.4 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively. Crude oil transported by the Company principally originates in Kazakhstan and Azerbaijan, while a significant percentage of oil products (approximately 66.5 per cent. for the year ended 31 December 2011) originate in Azerbaijan and Turkmenistan. The Company also tranships goods from west to east across its network for onward delivery to support military operations in Afghanistan.

The worldwide economic downturn, which began in mid-2008, adversely affected the Company's operations in 2008 and 2009. Many of the goods originating in the Caucasus region and Central Asia and transhipped through the TRACECA corridor, such as oil, ores and various oil products, are important raw materials for industry. As a result, the Company's railway freight transportation volumes are sensitive to changes in GDP and industrial production of TRACECA countries and their end markets. According to data compiled by Eurostat, GDP in the EU (an important market for goods shipped through the TRACECA corridor) decreased by 1.9 per cent. between the fourth quarter of 2008 and the fourth quarter of 2009, while industrial production decreased by 3.6 per cent. in 2009, as compared to 2008. The Georgian economy was also affected by the global economic crisis, with real GDP and industrial production in Georgia decreasing by 3.8 per cent. and 0.6 per cent., respectively in 2009, as compared to 2008, according to the Geostat. See "*—Risks Related to Georgia—Emerging markets such as Georgia are generally subject to greater risks than more developed markets*" and "*—Risks Related to Georgia—Fluctuations in exchange rates and inflation could have a material adverse effect on the Company's business*".

As a consequence of the crisis, the Company's freight transportation volumes and passenger numbers decreased by 19.3 per cent. and 8.8 per cent., respectively, in 2009, as compared to 2008. The Company's revenue and operating profit also decreased in 2009, as compared to 2008, as a result of the crisis. The Company might not be able to maintain the return to growth in freight transportation volumes, passenger numbers and revenue that began in 2010. During the second half of the year 2011 and to date in 2012, news reports have indicated that a number of countries, particularly in Europe, were experiencing slower than expected growth and that there were and are worries that certain of these countries may experience "double-dip" or prolonged recessions. Furthermore, during 2011 and 2012, there has been turmoil in the European banking system and a deterioration of sovereign credit among governments in Greece, Ireland, Italy, Spain, Portugal and a number of other European economies. Adverse economic developments in Georgia, the surrounding region or globally could reduce demand for the Company's services. Moreover, a number of countries in the region have in the recent past experienced, or, in the case of Afghanistan, are currently experiencing, political, social and economic instability, terrorist acts or war. Such economic, social and political unrest could reduce transportation volumes along parts of the TRACECA corridor, in turn potentially reducing demand for the Company's services. Conversely, any changes in the political and military situation in Afghanistan could reduce the demand for the Company's services on this route. Reduced demand for the Company's services could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company faces competition from oil pipelines

The Company faces competition from oil pipelines in transporting crude oil. Transport of crude oil accounted for 26.8 per cent. and 31.7 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively. Transport of crude oil across the Company's rail network is an alternative to oil pipelines. Pipelines often have lower transport and operational costs, particularly for large oil producers that participate in their construction, and are more efficient than rail in transporting large volumes of crude oil. Pipelines in the region, such as the Caspian Pipeline Consortium pipeline (the "**CPC Pipeline**"), the Baku-Tbilisi-Ceyhan pipeline (the "**BTC Pipeline**"), the Baku-Novorossiysk pipeline and the Baku-Supsa pipeline, compete with the Company directly. In particular, part of the decrease in the Company's liquid cargo volumes in 2009, as compared to 2008, resulted from the opening of the BTC Pipeline. This competition also limits the tariffs the Company is able to charge in its liquid cargo transportation business. To help offset competition from pipelines, the Company must attract the business of smaller oil producers, particularly those who either do not benefit from costs savings in using the pipelines or produce grades of crude oil that cannot be transported through the pipelines. To the extent that the Company cannot attract this business, competition from pipelines may adversely affect its business. In addition, the BTC Pipeline has unused capacity. Plans to increase the capacity of the BTC Pipeline and the CPC Pipeline were postponed due to the economic crisis. However, it is currently expected that capacity increases for the CPC Pipeline will be completed in 2015 or 2016, and plans to expand capacity for the BTC Pipeline could also be reinitiated in the future. There can be no assurance that intense competition from oil pipelines will not have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Description of the Company's Business—Business Operations—Freight SBU—Freight Competition—Competition from pipelines*".

The Company faces competition from alternative rail transit routes and providers of other methods of transportation

The Company faces competition from alternative rail transit routes and providers of other methods of transportation, and such competition may increase in the future. The Company's competitors may have more resources and better access to customers than the Company does. In particular, the existence of alternative railway routes through Russia and Iran, including routes providing access or onward transportation to or from Aktau port in Kazakhstan, Turkmenbashi port in Turkmenistan, Makhachkala and Novorossiysk ports in Russia, Bandar Anzali port in Iran and the Sea of Azov port in Ukraine, could pose competition to the Company's Freight SBU. If, in the future, rail operators of these routes significantly increase the number of railcars that they operate throughout the year or significantly reduce the tariffs they apply, the Company may be unable to successfully compete with them. In addition, any improvement in political relations between Iran and western jurisdictions could result in an increase of freight traffic using routes through Iran rather than Georgia. See "*Description of the Company's Business—Business Operations—Freight SBU—Freight Competition—Competition from alternative rail routes*".

The Freight SBU also faces competition from other methods of transport for its freight transportation services, including transport by truck and oil pipelines. The Company's Passenger SBU faces competition in passenger transportation services from other forms of domestic transport, such as buses, mini-buses, passenger automobiles and airplanes. Intense competition from alternative transit routes and other methods of transportation may have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*—The Company faces competition from oil pipelines*", "*Description of the Company's Business—Business Operations—Freight SBU—Freight Competition—Competition from other modes of transport*" and "*Description of the Company's Business—Business Operations—Freight SBU—Freight Competition—Competition from pipelines*" and "*Description of the Company's Business—Business Operations—Passenger SBU—Freight Competition—Passenger Competition*".

The Company provides its freight services to a limited number of customers

The Company has well-established ties with a number of large customers for its freight services, including Georgia Transit, BSI Trans, PACE Georgia and subsidiaries of Heidelberg Cement. The Company has historically earned, and expects to continue to earn, a significant portion of its revenues from a relatively small pool of large customers. A single customer of the Freight SBU accounted for approximately 30 per cent. of the Company's total revenue in each of the years ended 31 December 2011 and 2010.

A number of factors, including pricing and market demand for the Company's services, could cause the loss of a customer. Some of these factors may be unforeseeable. Moreover, in its liquid cargo transportation services in particular, the Company largely works with freight forwarders, who aggregate volumes for the Company to transport. The Company does not have long-term contracts with the ultimate owners whose cargo the freight forwarders aggregate. As a result, there can be no assurance that cargo owners will continue to use the services of the freight forwarders with which the Company has relations. In addition, the crude oil the Company transports originates primarily from a limited number of oil fields in Kazakhstan and Azerbaijan. Any disruption in oil production from such fields, whether planned or as a result of accidents, decreased demand or other unforeseen factors, or the loss of end-customers producing in such fields could decrease the volumes of liquid cargo transported by the Company.

The Company may be unable to retain its customers in the future. If the Company loses customers, it may be unable to replace the lost business with that of other customers on comparable terms and at comparable volume levels or at all. Future decisions by these customers not to use the Company's services or to use them to a lesser degree could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company's infrastructure is ageing and requires continual maintenance and improvements and may require replacement in the future

A substantial portion of the infrastructure owned and operated by the Company, including its track network and the related engineering technology (including signalling and rolling stock maintenance depots), dates back to the Soviet era. Although the condition of this infrastructure is sufficient to carry out the Company's current and planned railway operations without significant disruptions, the Company continues to carry out extensive maintenance and improvement works on much of its network. The Company has already made, and intends to continue making, substantial investments to modernise its infrastructure, including the Modernisation Project and the Bypass Project. See "*Description of the Company's Business—Modernisation Project*", "*Description of the Company's Business—Bypass Project*" and "*—Current and future projects designed to improve the Company's infrastructure, including the Modernisation Project and the Bypass Project, are still in the early stages of implementation and may be subject to delays or, in relation to the Modernisation Project and the Bypass Project, higher than anticipated costs*". The Company had capital expenditures and other additions to non-current assets related to its infrastructure and headquarters of GEL 355.6 million and GEL 231.1 million in the years ended 31 December 2011 and 2010, respectively. There can be no assurance that portions of the Company's network and other infrastructure assets are not now or will not become outdated or require significant further improvements or replacement, which would require additional capital expenditure. Any failure of the Company's infrastructure to operate properly, or accidents attributable to poor conditions of the rail infrastructure, could lead to material disruptions in the Company's business, increase the Company's operating expenses or require significant additional capital expenditures, which could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as the trading price of the Notes.

The Company's rolling stock and related assets require continual maintenance and improvements and may require replacement in the future

The Company owns and operates various freight and passenger transportation assets, including locomotives, railcars, EMUs and other equipment. Although the condition of the Company's rolling stock and related assets is sufficient to carry out the Company's railway operations without significant disruptions, the Company continues to carry out refurbishment works and, to the extent such rolling stock and related assets reach the end of their useful operating life (as extended by any capital repairs), they will require replacement in the future. The Company's Freight SBU and Passenger SBU had combined capital expenditures and other additions to non-current assets of GEL 62.7 million and GEL 41.7 million in the years ended 31 December 2011 and 2010, respectively, principally for capital repairs to locomotives and acquisition of railcars. Any failure of the Company's rolling stock to operate properly could lead to material disruptions in the Company's business, increase the Company's operating expenses or require significant capital expenditures. Moreover, in the event that any of the Company's rolling stock needs to be replaced, there can be no assurance that the Company will continue to be able to source sufficient supplies of suitable new rolling stock on commercially acceptable terms, or at all. Any requirement to replace or repair a significant portion of the Company's railway assets, such as rolling stock and related assets, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as the trading price of the Notes.

Insufficient supply of, or increases in the price of, rolling stock may limit the operations of the Company

There is a relatively limited number of quality rolling stock manufacturers in Georgia and the CIS and their output is limited. In addition, the adaptability of these manufacturers' production facilities from one type of railcar to another is limited. A significant part of the rolling stock fleet operated by the Company is ageing and may require replacement. Although the Company has recently entered into an agreement to lease up to 1,000 tank cars until 1 April 2015, the Company has historically, from time to time, including in the first quarter of 2012, experienced shortages of rolling stock and there can be no assurance that the Company will continue to be able to source sufficient supplies of new rolling stock for its fleet on commercially acceptable terms, or at all. Failure by the Company to procure the requisite amount of rolling stock could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Current and future projects designed to improve the Company's infrastructure, including the Modernisation Project and the Bypass Project, are still in the early stages of implementation and may be subject to delays or higher than anticipated costs

The Company is in the early stages of implementing the Modernisation Project, which it currently expects to complete by 2016. Implementation of projects such as the Modernisation Project involve many potential risks and uncertainties. These include work stoppages and interruptions resulting from inclement weather (particularly in the winter), unforeseen engineering difficulties and geological problems. Any of these developments could cause delays or may result in the Company's desired or anticipated results not being achieved. These developments, as well as unanticipated cost increases, could also cause cost overruns in relation to the Modernisation Project. Any material deviations from the Company's expectations and assumptions for the Modernisation Project, including delays in completion of the project or higher than expected costs, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Description of the Company's Business—Modernisation Project*".

In addition, the Company is engaging in the Bypass Project, in connection with which the Government, acting through the Ministry of Finance and the MESD, and the Company have entered into the Bypass Project Memorandum. The Bypass Project Memorandum creates a set-off mechanism for the Company to be reimbursed by the State for the Company's future expenses in relation to the Bypass Project out of dividends that would otherwise be payable to the State in respect of its shares in the Company and in exchange for the transfer, by the Company to the State, of the Existing Railway Land. The amount to be reimbursed to the Company does not cover an instalment of CHF 36.1 million due to be paid by the Company to its contractor in 2012 and is subject to an aggregate cap of CHF 138.0 million. In May 2012 and to date in June 2012, the Company paid to its contractor approximately GEL 20.4 million (CHF 11.9 million) and GEL 5.0 million (CHF 2.9 million), respectively, of the CHF 36.1 million not covered by the reimbursement obligations and the balance shall be paid by the Company out of its existing cash flows upon the completion of the corresponding work by the contractor. The Existing Railway Land will be transferred to the State upon completion of the Bypass Project or, if later, upon the full reimbursement of reimbursable expenses by the Government. If the dividends payable to the State are insufficient to cover the reimbursable expenses in full, the Company has the right to retain a pro rata ownership interest in the Existing Railway Land. Separately, the relocation of certain rail infrastructure to a different part of the city in connection with the Bypass Project could result in complaints from nearby residents, whether due to noise, environmental or other reasons. Any material deviations from the Company's expectations and assumptions for the Bypass Project, including any failure of the set-off mechanism set out in the Bypass Project Memorandum or in the incurrence of expenses in relation to the project in excess of the cap of CHF 138.0 million, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Description of the Company's Business—Bypass Project*".

The Company's capital investment programme may not be successfully implemented on schedule, its cost may fluctuate or the Company's operating cash flows may be insufficient to finance its planned capital investments or meet other significant needs and the Company may be unable to obtain necessary alternative financing

The Company plans to continue to invest in its infrastructure and operations, including by undertaking the Modernisation Project and the Bypass Project. The Company's cash flows used in the acquisition of property, plant and equipment were GEL 436.0 million and GEL 281.7 million in the years ended 31 December 2011 and 2010, respectively. The Company began incurring expenses for the Modernisation Project and the Bypass Project in September 2010 and November 2010, respectively. These amounts are expected to increase substantially going forward. The Company's currently budgeted capital expenditures between 2012 and 2014 are approximately CHF 482.0 million (GEL 880.1 million), including approximately CHF 153.1 million (GEL 272.2 million) for the Modernisation Project and approximately CHF 151.0 million (GEL 268.5 million) for the Bypass Project (out of total incurred and budgeted expenses for the Bypass Project, approximately CHF 36.1 million is to be paid by the Company independently from its dividends in 2012 and the remaining expenses of up to CHF 138.0 million are to be reimbursed by the State from the

Company's dividends pursuant to the Bypass Project Memorandum). Such factors as changes in economic conditions in Georgia or the region, higher capital costs than expected, slower than anticipated revenue growth, regulatory developments, delays in project completion, cost overruns and defects in design or construction could impair the Company's ability to implement its capital investment programme on time and within budget. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Liquidity and Capital Resources—Capital expenditures*".

Save as described above in relation to the reimbursement of certain expenses for the Bypass Project, the Company's capital investment programme is expected to be funded from internally-generated cash flows, as well as from existing external financings and new external financings, such as the proceeds of the Notes. In the past, the Company has experienced negative free cash flow as a result of both the level of the Company's capital investment programme and the payment of dividends in respect of the Company's share capital and there can be no assurance that the Company will not experience negative free cash flow in the future for the same or other reasons. In particular, the use by the Company of cash generated by operations for the payment of dividends (to the extent permitted by the Terms and Conditions of the Notes) may mean that the Company may again experience negative free cash flow in future periods and, accordingly, cash generated by operations may be insufficient to finance the Company's capital investment programme. If the Company is unable to finance its planned capital investments as anticipated, it may need to seek further financing from the capital markets, through bilateral or syndicated loans or from the State, through further capital contributions or otherwise. There can be no assurance that such financing can be arranged on terms acceptable to the Company in an amount sufficient to finance any balance of capital expenditures not otherwise provided for. An inability to finance planned capital investments, to finance such investments at an acceptable cost or to implement its capital investment programme for any other reason could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Overview of the Company—Strategic Projects*". Moreover, if the Company were to experience persistent negative free cash flow following necessary funding of its capital investment programme and the payment of dividends or for other reasons, this could adversely affect the Company's ability to repay principal of, and make payments of interest on, the Notes, as well as having a material adverse effect on the trading price of the Notes.

The Modernisation Project and Bypass Project may put a strain on the Company's management resources

Each of the Modernisation Project and the Bypass Project is a multi-year, discretionary, complex project in the early stages of implementation. These two projects will require the Company's management to devote time to monitoring their respective progress and development, in addition to their current tasks. To the extent that there are any problems, delays or unanticipated complexities with the Modernisation Project or the Bypass Project, further management time or resources may need to be devoted to these projects, which could put further strain on the Company's management and management systems and could divert management's attention from effectively overseeing the day-to-day operations of the Company's business. Any failure by the Company to deploy and maintain adequate management resources to support the Modernisation Project and Bypass Project could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Overview of the Company—Strategic Projects*".

The Company is exposed to foreign currency exchange risk

The Company's reporting currency is the Lari. To a material extent, the Company enters into transactions denominated in Swiss Francs and U.S. Dollars, and carries a portion of its liabilities and assets in these currencies and the remainder in Lari. Therefore, variations between the rate of exchange among the Swiss Franc, the U.S. Dollar and the Lari have had and will continue to have some effect on the Company's results of operations. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Swiss Franc Exchange Rates*" and "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Exchange Rates*".

For all periods under review in this Prospectus, the Company has quoted its freight tariffs in Swiss Francs only, except for tariffs for freight services, which, since 1 February 2012, the Company quotes in U.S. Dollars due to the volatility of the exchange rates between the Swiss Franc, the Lari and other currencies and also to better align costs and revenues for its customers and suppliers which mainly trade in U.S. Dollars or Lari. In addition, a significant part of the Company's capital expenditures and of its operating expenses, including the Company's rental charges for using the railcars of other national railway operators, have been and continue to be denominated in Swiss Francs.

During the periods discussed herein, the Swiss Franc has experienced average year-on-year appreciation relative to the Lari. Such appreciation was a significant contributor to the revenue growth in the year ended 31 December 2011, as compared to the year ended 31 December 2010, and in the year ended 31 December 2010, as compared to the year ended 31 December 2009. The appreciation of the Swiss Franc during the periods under the review, however, has also had the effect of contributing to increases in capital expenditures and costs of materials used for repair and maintenance. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends— Change in freight tariffs and volume-based discounts*".

In addition, as at 31 December 2011, the Company's outstanding loans and borrowings, which were GEL 432.7 million, were denominated in U.S. Dollars. The Company also incurs a portion of its trade payables in U.S. Dollars. In the period from 1 January 2009 to 31 December 2010, the U.S. Dollar experienced average year-on-year appreciation relative to the Lari. Such appreciation had a tendency to increase operating expenses and finance costs. In the year ended 31 December 2011, the U.S. Dollar depreciated relative to the Lari.

Historically, the Company has not utilised forward exchange contracts, currency swaps or other hedging arrangements in respect of its foreign currency risk. In April 2012, the Company engaged a consultant with a view to evaluating its options in respect of hedging, including in respect of the Company's exposure to fluctuations in the value of the Swiss Franc and the U.S. Dollar and, as at the date of this Prospectus, the Company is in the process of negotiating appropriate hedging agreements under the guidance of this consultant. There can be no assurance that this or other strategies will be implemented or, if implemented, that the Company will be fully or partially able to offset negative effects arising from the currency fluctuations to which it is exposed. Therefore, fluctuations in the values of these currencies could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as the trading price of the Notes. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Exchange Rates"* and "*—The Company's operations may be restricted by its loan covenants*", and "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Exchange rates*".

The Company may not be able to offset the impact of a decline in freight volumes by increasing tariffs

The Freight SBU accounted for over 90 per cent. of the Company's total revenue in the first quarter of 2012 and each of the three years ended 31 December 2011. While freight traffic volumes increased by 16.4 per cent. in 2010, as compared to 2009, and then increased by a further 1.0 per cent. in 2011, as compared to 2010, historically, volumes transported by the Freight SBU have fluctuated. In the first quarter of 2012, total volumes transported by the Company decreased by 0.9 per cent., as compared to the same period of 2011. As the Company is not currently subject to any mandatory statutory or regulatory tariff restrictions, the Company may increase the tariffs it sets in respect of its freight operations in order to offset any declines in freight volumes, as it did in 2009. However, such tariff increases may not be sufficient to compensate fully for decreased freight volumes. Although the Company has further increased its freight tariffs by two per cent., except on discounted tariffs for liquid cargo, with effect from 1 January 2012, the Company's ability to offset decreased volumes by increasing prices is limited by the Company's need to remain competitive with alternative transit routes, including oil pipelines. There can be no assurance the Company will be able to return to the growth in freight volumes that began in 2010 or, if volumes continue to decrease, that the Company will be able to increase its freight tariffs to offset any such decreased volumes. Decreases in volumes that cannot be offset by increased tariffs could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends— Change in freight tariffs and volume-based discounts*".

A major accident, derailment or other incident could result in loss of the Company's rolling stock, disruption to services, environmental remediation costs and damage to the Company's reputation

The Company owns and operates the tracks, stations and other infrastructure and rolling stock comprising Georgia's entire national railway. As a result, the Company's infrastructure and transportation operations may be adversely affected by many factors, including accidents, derailments, the breakdown or failure of equipment or processes, natural disasters, terrorist attacks or sabotage. A major rail accident, derailment or other incident involving the Company's railway operations could result in damage to or loss of the Company's infrastructure or rolling stock and may also disrupt the Company's services, which could give rise to potential claims by freight shippers, injured passengers and others. A major rail accident or derailment involving oil or oil products cargo could also result in substantial environmental remediation costs. In July 2011, the Company experienced three freight train derailments. Although none of these derailments caused death or injury, each involved the derailment of loaded tank cars. Oil products were spilled in two of the incidents, and there can be no assurance that subsequent investigation will confirm the Company's initial assessment that no significant environmental damage resulted from these spills. In addition, railcars not owned by the Company may be used on the Company's rail network, as parties to the tariff agreement among the Company, the railway companies of a number of CIS member states and the railway companies of certain other states (the "**Tariff**

Agreement") have the right to utilise their own railcars on freight routes throughout the rail network of the member states. Such rolling stock may not be maintained to the same standard as the Company's rolling stock and could be more prone to accidents or breakdowns. For example, following preliminary investigations, the Company believes that two of the July 2011 derailments were caused by technical problems in railcars owned by third parties. Negative publicity concerning any accident or derailment, even if caused by rolling stock not owned by the Company, could also have a material adverse effect on the Company's reputation and the attractiveness of its services in the future.

Moreover, as set out below under "—*The Company is largely self-insured*", the Company does not carry liability insurance or business interruption insurance in relation to these matters. A significant uninsured event would cause the Company to incur additional expenses and the Company may not be able to rebuild or repair its infrastructure or rolling stock or restore operations in a timely fashion. Accordingly, a major accident, derailment or other incident involving the Company's railway operations could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company is largely self-insured

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. Moreover, to the extent insurance may be available to the Company outside Georgia (if at all), the Company understands that such insurance would be prohibitively expensive and, as such, based on statistics relating to past failures on the railway, the Company does not believe it would be cost effective to purchase insurance services for its infrastructure assets. Accordingly, in common with other state-owned enterprises, the Company does not have any insurance coverage for its infrastructure and other assets, business interruption or third-party liability in respect of property or environmental damage arising from accidents on the Company's property or relating to the Company's operations. The Company also does not maintain insurance for terrorism or war risk. The Company's customers typically purchase insurance covering the cargo transported by the Company. There can be no assurance that claims or losses will not increase in the future or that insurance coverage (if any) that it may carry in the future will be sufficient to cover its exposures. The Company's failure to carry business interruption insurance also means that, if the Company suffers an interruption in its ability to operate, the Company will have reduced income available to pay its obligations. Until and unless the Company obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Disruption on the Company's mainline could affect its business

In operating its business, and particularly its freight transportation business, the Company depends on its ability to provide continuous service along the Company's railtrack. The Company's main rail line is a 527 kilometre fully-electrified mainline from the Azerbaijan and Armenian borders to the Black Sea (of which 293 kilometres are double-track line). The electricity supply along this route runs in parallel with the Company's rail track. In addition, an important section of this line is a single-track line running through a gorge in mountainous terrain. The Company's ability to provide service along this mainline could be affected by various natural disasters or other unforeseen events such as flooding, disruption of the electricity supply, fires, terrorism, sabotage and human error. The section of track running through the mountainous gorge area is also subject to the additional risk of rock falls and other geological shifts in the mountains surrounding the railtrack, which could block the track, interrupt the electricity supply or otherwise prevent the Company from running its service along this line. Any disruption or lasting damage caused to the Company's railtrack, particularly the mainline route for freight transportation running from the Azerbaijan and Armenian borders to the Black Sea, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See also "—*The Company is largely self-insured*".

The Company's operations may be affected by operational decisions and limitations in capacity of other regional rail operators

The Company's mainline rail network comprises a key segment of the TRACECA corridor and, together with Azerbaijan Railway, forms the Caucasus corridor. Because the rail networks of TRACECA members are interlinked, capacity or other limitations of other regional rail networks, particularly Azerbaijan Railway, can constrain the Company's operations. Transit shipments are a significant portion of the Company's transportation volumes, accounting for 62.5 per. cent and 66.3 per cent. of the Company's total transportation volumes in the years ended 31 December 2011 and 2010, respectively. Capacity or other transhipment limitations elsewhere along the TRACECA or Caucasus corridor, as a result of, for example, insufficient rolling stock or underinvestment in infrastructure that limits speed or otherwise reduces track capacity, could limit the volume of cargo reaching the Company's network and thus reduce the volume of cargo shipped by the Company.

Similarly, railcars not owned by the Company may be used on the Company's rail network, as parties to the Tariff Agreement have the right to use their own railcars on freight routes throughout the rail network of the member states. Third-party rolling stock may not be maintained to the same standard as the Company's rolling stock and could be more prone to accidents or breakdowns, which could result in damage or loss of the Company's infrastructure or rolling stock. Operational decisions of other regional rail networks that result in capacity or other limitations could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company is wholly owned by the State, which could act inconsistently with the best interests of the Noteholders

The Company is wholly owned by the State (directly and indirectly through the JSC Partnership Fund (the "**PF**"), which has the power to replace the members of the Supervisory Board and elect new members, to influence the Company's operational and financial decisions and to control the outcome of all matters to be decided by a vote of shareholders of the Company. As a consequence of its role as controlling shareholder, the State would be effectively able to overturn any decision of the Supervisory Board or its committees. The State may also influence the Company's operations in other ways. For example, the Company is required to get approval from the General Shareholders Meeting (the "**GMS**") for matters such as approval of its annual accounts, borrowings in excess of one per cent. of the Company's authorised capital and capital-related matters (such as dividend payments). The interests of the State could conflict with those of the Noteholders, potentially having a material adverse effect on the trading price of the Notes. The State may require the Company to engage in business practices that could materially affect the Company's ability to operate on a commercial basis or in a way that is inconsistent with the best interests of the holders of the Notes. See "*—The Georgian Government has the power to start establishing tariffs and could otherwise require the Company to operate on a non-commercial basis*" and "*Shareholders*".

The Georgian Government has the power to start establishing tariffs and could otherwise require the Company to operate on a non-commercial basis

The Company is not currently subject to mandatory statutory or regulatory tariffs and, under the Railway Code of Georgia, No. 1911, dated 28 December 2002 (as amended) (the "**Railway Code**"), the Company is able to set its own tariff policies. The Railway Code, however, also authorises the State to establish a Rail Transport Authority (the "**Rail Transport Authority**") that would have the power to set tariffs. Although the Company is not aware of any plans of the State to create the Rail Transport Authority, there can be no assurance that the State will not establish the Rail Transport Authority or otherwise take steps limiting the Company's ability to set its own tariffs, including through its influence as the Company's principal shareholder. In particular, as in cases of other state-owned infrastructure assets, the State could use passenger tariffs to support public policy initiatives without regard to the impact on the Company. For example, although the State does not explicitly mandate pricing, the significant social importance to the State of providing affordable passenger transportation services has constrained the Company from setting passenger transportation tariffs wholly on the basis of market forces. It has also constrained the Company from removing or reducing services on certain passenger routes. As a result, the Company has focused on decreasing passenger operating costs, while average passenger tariffs have remained relatively stable, with fares unchanged for travel in older railcars. See "*Description of the Company's Business—Business Operations—Passenger SBU—Passenger Tariffs*".

In addition, the Government has established the State Transportation Committee, an advisory body of the Government, with the objective of discussing all major transport issues within the country and to make strategic decisions concerning the development of the transportation industry, including the national railway. The Government may influence decisions of the Company's management in respect of the Passenger SBU in connection with providing affordable passenger transportation services through the policies of the State Transportation Committee, which is headed by the Prime Minister and includes the Minister of Finance, the Minister of Economy and Sustainable Development, the Minister of Infrastructural Development, the Chief Executive Officer of the Company, the Head of the Roads Department and representatives of Black Sea port operators. The Government may also suggest that the Company undertake certain actions or projects in respect of the Passenger SBU.

There can also be no assurance that the Government will not in the future implement tariff regulations in order to reflect various EU directives related to rail transportation and rail authorities. The Company is not aware of any plans to implement such regulations, although the Government is currently in discussions with the EU in relation to the potential entering into of an EU association agreement.

Any limitations on the Company's ability to control its own tariffs, or any other action of the Government that requires the Company to operate on a non-commercial basis, could hamper the Company's ability to increase tariffs in response to increases in its costs of operations or otherwise impact its ability to react to market forces. This could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*—The Company is wholly owned by the State which could act inconsistently with the best interests of the Noteholders*".

The Company's operations may be restricted by its loan covenants

The Company is obliged to comply with various covenants and restrictions contained in its financing arrangements, including the Notes and, to the extent any of the 2010 Notes remain outstanding following the 2010 Notes Tender, the 2010 Notes. Such covenants include the requirement to meet certain financial ratios, such as financial indebtedness to EBITDA, as well as restrictions on the creation of security interests. In addition, until the repayment of the Notes and, to the extent any of the 2010 Notes remain outstanding following the 2010 Notes Tender, the 2010 Notes, the Company may not incur any secured financial debt, except as permitted thereunder. To the extent that the Company's existing credit facilities, including the Notes, and the Company's internal cash flow are not sufficient for the Company's planned capital expenditure requirements, the Company may have to seek additional forms of financing. Moreover, it may become impossible or difficult to comply with, or obtain consent for deviation from, the covenants set out in the Company's financing arrangements, which could require the Company to restructure its indebtedness or refinance its existing debt. Any failure in these respects could be costly and could have a material adverse effect on the Company's business, financial condition, results of operations, and prospects, as well as on the trading price of the Notes. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Liquidity and Capital Resources—Borrowings*".

The Company may be unable to obtain refinancing for its current loans and borrowings on commercially acceptable terms, if at all

As at 31 December 2011, the Company's total outstanding loans and borrowings were GEL 432.7 million, including the 2010 Notes. The Company evaluates its options in respect of such loans and borrowings based on its actual performance in any given year and is currently intending to repay the principal and interest amounts under such loans and borrowings from its operating cash flows as and when they become due. If the Company's cash flows are insufficient to repay its loans and borrowings, the Company will need to renegotiate its loans or seek alternative financing from the capital markets. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Liquidity and Capital Resources—Borrowings*".

The Company's ability to raise alternative financing or to renegotiate loans on commercially acceptable terms, or at all, depends on, among other factors, the general condition of the international capital markets and the overall economic conditions in Georgia, as well as the financial condition of the Company. There can be no assurance that, if alternative financing becomes necessary, the Company will be able to obtain such financing on commercially acceptable terms, if at all. See also "*—The Company's operations may be restricted by its loan covenants*".

The ratings assigned to the Company, among other things, are dependent on those assigned to Georgia (for so long as the State maintains a sufficient ownership interest in the Company), as well as on the overall economic and financial conditions in Georgia. In the event that the ratings agencies downgrade Georgia's ratings, decouple the Company's rating from Georgia's rating or downgrade the Company's ratings, the Company's ability to obtain debt or equity financing may be materially adversely affected and any debt financing the Company were then able to obtain would likely bear higher interest than would have been the case had the rating not declined.

Pursuant to the 2010 Notes (to the extent any of the 2010 Notes remain outstanding following completion of the 2010 Notes Tender), failure to pay amounts due, whether principal or interest, or failure by the Company to pay other indebtedness in excess of U.S.$10 million or more in the aggregate will, among other matters, constitute an event of default. In addition, pursuant to the Notes, failure to pay amounts due, whether principal or interest, or failure by the Company to pay other indebtedness in excess of U.S.$25 million or more in the aggregate will, among other matters, constitute an Event of Default. Under the 2010 Notes and the Notes, such an event will, upon notice given by 25 per cent. of the holders of the 2010 Notes or the Notes, as the case may be, cause the 2010 Notes or the Notes (as the case may be) to become immediately due and payable without further action or formality. Such default or any failure to generate sufficient funds from operating cash flows or obtain sufficient debt financing on commercially acceptable terms to repay its loans and borrowings could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company's passenger services have historically generated net losses

One of the Company's medium-term strategic objectives is to transform the Passenger SBU into a profitable operation. Historically, however, the Company's passenger transportation services have generated net losses. The Passenger SBU had a loss before infrastructure costs, net interest costs and income tax of GEL 10.9 million and of GEL 10.8 million in the years ended 31 December 2011 and 2010, respectively. There can be no assurance that the Company's planned investment in new rolling stock to increase speed, decrease maintenance expenses and improve travel comfort will enable it to increase passenger transportation tariffs or to generate profit from its passenger rail operations. Historically, passenger tariffs have remained relatively low due to the social importance to the State of the Company's provision of affordable passenger transportation services. Moreover, given the social importance of its passenger services, the

Company may be constrained in removing or reducing services on certain passenger routes, even where such routes are not economical. Failure by the Passenger SBU to achieve profitability could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company is subject to risks relating to operations at sea ports and terminals

Three of the Company's railway lines terminate at cargo or oil terminals at the Black Sea ports of Batumi, Poti and Kulevi, through or at which the substantial majority of the freight the Company transports is received, stored or on-shipped. Accordingly, the Company's freight operations are exposed to the risk of interruption at the ports or terminals, which may prevent the Company from delivering or receiving cargo to be transported at the ports or stored at the terminals. Any sustained disruption at the port or terminal facilities, including with respect to the transportation of cargo to and from the Company's operations to the ships or terminal facilities, for example, due to strikes or inclement weather (particularly in the winter, as happened in 2012), could impede the Company's ability to provide its freight services on time, or at a reasonable cost, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company's energy costs could increase

Costs related to energy, and particularly electricity, constitute a significant portion of the Company's operating expenses, making its operating expenses sensitive to changes in energy prices. Electricity costs include principally the costs of the electricity used to move the Company's locomotives and vehicles and the electricity used in the Company's buildings. Approximately 94.0 per cent. of the Company's railway network is electrified. The Company also uses diesel-powered locomotives. Significant increases in the cost of electricity or diesel fuel, including as a consequence of increased regulation or taxation of greenhouse gases, could adversely affect the Company's operating expenses and results. Following tariff increases, the Company's average electricity tariffs increased by 14.8 per cent. in the year ended 31 December 2011, as compared to 2010, and by 3.3 per cent. in the year ended 31 December 2010, as compared to 2009. In September 2011, the Company entered into an agreement for the purchase and sale of electricity with JSC EnergoPro Georgia ("**EnergoPro Georgia**"), which fixes tariffs for electricity for five years (the "**Electricity Agreement**"). After the initial five year period, the agreement provides that the tariff will be fixed again for a further five year period. The tariff may be adjusted upwards in the limited circumstances provided for in the agreement. Management estimates that electricity delivered under this contract will satisfy almost 90 per cent. of the Company's total electricity requirements. However, future increases in electricity tariffs payable to EnergoPro Georgia after the initial five year contract period, continued increases in electricity tariffs in respect of the electricity not supplied by EnergoPro Georgia or increases in other energy prices could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Cost of electricity and materials*".

Failure to comply with applicable environmental and health and safety laws and regulations may give rise to significant liabilities

The Company is subject to various environmental protection and occupational health and safety laws and regulations relating to protection of the environment and protection of human health and safety in Georgia. These laws and regulations set various standards regulating certain aspects of health, safety, security and environmental quality and they provide for civil and criminal penalties and other liabilities for the violation of such standards and may in certain circumstances impose obligations to remediate current and former facilities and locations where operations are or were carried out. The cost of environmental and health and safety compliance in the future and potential liability due to any environmental damage that may be caused by the Company or that may already exist on land owned by the Company or any health and safety violations committed by the Company could be material. Moreover, the Company could be adversely affected by future actions and fines imposed on the Company by environmental authorities. To the extent that any provision in the Company's financial statements relating to remediation costs for environmental or health and safety liabilities proves to be insufficient, this could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company cannot guarantee that it will be in compliance at all times with all applicable environmental and health and safety laws and regulations, which could change from time to time. Any failure to comply with these environmental and health and safety requirements could subject the Company to, among other things, civil liabilities, administrative sanctions and penalty fees and possibly temporary or permanent shutdown of the Company's operations. Any imposition of fines or increases in the costs associated with compliance with environmental and health and safety laws and regulations could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company's business may be adversely affected by strikes, lockouts and labour legislation

The Company is the largest corporate employer in Georgia, with 13,227 employees as at 31 December 2011. As at the date of this Prospectus, the Company does not have any collective bargaining agreements with its employees or a trade union, although the Company has in the past been party to arrangements with the Railway Workers Trade Union of Georgia. If, in the future, the Company decides to implement any programme that, in an effort to further improve its operations and profitability, affects the size or organisation of the workforce, there can be no assurance that the Company's business will not be subject to the threat of interruptions through strikes or lockouts. Moreover, as the largest employer in Georgia, the Company and its subsidiaries are subject to certain social and political constraints with respect to its workforce and, therefore, may be unable to make any rapid or significant reductions in the number of its employees, if required. Any such interruptions or restrictions (real or perceived) on its ability to restructure its workforce could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See "*Description of the Company's Business—Legal Proceedings*" and "*Description of the Company's Business—Employees and Pensions*".

The Company may be unable to attract and retain qualified and key personnel

The Company's success depends to a significant extent on the services of its senior management and skilled engineering team. There can be no assurance, however, that these individuals will continue to make their services available to the Company in the future. The Company's ability to achieve its business objectives depends to a large degree on the services of its senior management team. The loss or unavailability of these personnel for an extended period of time could have a material adverse effect on the Company's business, financial condition, results of operations, future prospects and the trading price of the Notes. The Company does not have key-man insurance in place in respect of its senior managers.

In addition, the Company employs a number of highly qualified engineers and other personnel. However, competition in Georgia for suitably qualified and experienced executives and other personnel is intense due to the relatively small number of available qualified individuals. The Company's ability to retain its existing senior management and engineering personnel or attract additional suitably qualified personnel in the future may be limited and may depend on its ability to meet demands for higher wages. As a result, the departure of members of the Company's senior management or other highly qualified personnel, or the Company's inability to attract, employ and retain the necessary skilled and experienced personnel, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company's accounting systems and internal controls may not be as advanced as those of companies in more developed countries

The Company's management information system, financial reporting function and system of internal controls relating to the preparation of IFRS financial statements may be less developed in certain respects, and may not provide management with as detailed or as accurate information, as those of rail companies in more developed markets. However, management believes that they are sufficient for a company whose Notes are listed on the Official List and permit the Company to comply with its ongoing obligations as a listed company.

Although the Company has established an internal audit department, the internal audit department is relatively new and is staffed by personnel with limited internal audit-specific knowledge. Furthermore, this internal audit department has a limited remit and excludes the Company's subsidiaries from its work programme. In addition, while the Company maintains accounting software, it does not have computerised accounting or reporting systems designed for the preparation of stand-alone or consolidated IFRS financial statements. A number of the Company's subsidiaries also do not currently maintain computerised accounting software or software that is compatible with that used by the Company. Accordingly, the preparation of annual or interim IFRS consolidated financial statements may require more time for the Company than it does for companies in more developed countries. There are a number of additional areas where the introduction of automated and integrated processes could improve the Company's internal control systems, for example for the reconciliation of management accounts and in its treasury and budgeting processes, as well as in relation to its monthly cash flow budgets. Delays in preparing management accounts, or management being provided with insufficiently detailed information or inappropriate controls over monthly cash flow projections, could impact the decision-making process of senior management, as well as the management of the Company's liquidity. Moreover, the Company's ability to generate financial information in a timely manner is dependent on a small group of accounting personnel who currently fulfil both the accounting and reporting functions. There is a shortage of qualified personnel with IFRS accounting experience in Georgia. If, for any reason, the Company failed to maintain an adequate management information system, financial reporting function or system of internal controls, or experienced delays in preparing IFRS consolidated financial statements, this could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Notwithstanding anything in this risk factor, this risk factor should not be taken as implying that the Company will be unable to comply with its obligations as a company with its securities admitted to the Official List. The Company is committed to taking appropriate action to ensure that it complies with its ongoing obligations as a listed company.

The Company relies heavily on information systems to operate its business, and any failure of these systems could have a material adverse effect on the Company's operations

The Company's business is dependent on the successful and uninterrupted functioning of its information technology systems. The Company relies on these systems for complex logistical, dispatching and tracking tasks critical for its customers' transportation needs and central to the Company's business. The Company's information management systems do not include off-site system redundancy. There can be no assurance that the Company will be able to avoid significant failures or interruptions of its information systems in the future. Failures or interruptions in the Company's information technology systems may compromise the Company's ability to provide its value-added transportation, logistics and tracking services, as well as result in costly delays in the shipment of customer cargo, or otherwise lead to a significant loss of customer business, which could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company is not subject to mandatory corporate governance requirements

Georgia has not adopted a code of corporate governance, and corporate governance standards in Georgia may be less robust than in western jurisdictions. Furthermore, as a company incorporated in Georgia, the Company is not subject to the U.K. Corporate Governance Code issued by the Financial Reporting Council. As a matter of best practice, the Company has adopted and is committed to complying with certain corporate governance structures and procedures, including the appointment of independent directors to the Supervisory Board. The Company established a Nomination Committee and a Remuneration Committee in September 2011 and established an Audit Committee in February 2010. New terms of reference for the Audit Committee were adopted in September 2011. Each of these committees includes independent directors. See "*Management and Corporate Governance— Corporate Governance*". However, members of these committees may not possess the same qualifications, including auditing and financial reporting qualifications in respect of Audit Committee members, as members of similar committee members of companies in western jurisdictions. There can be no assurance that the Company will successfully identify independent directors in the future or that future committee members will acquire or possess the relevant qualifications, which could limit the effectiveness of the committees. Moreover, there can be no assurance that the Government, in its capacity as controlling shareholder or regulator, will not hamper the proper function of the committees or the Supervisory Board. In addition, the Company has adopted these measures voluntarily and is not subject to specific legal or regulatory corporate governance requirements. There can be no assurance that the Company will not in the future adopt governance structures and procedures that may be deemed to provide a lower level of assurance to investors than its current corporate governance structures and procedures.

Risks Related to Georgia

Emerging markets such as Georgia are generally subject to greater risks than more developed markets

Investing in securities involving emerging markets, such as Georgia, involves a higher degree of risk than investments in securities of corporate or sovereign issuers of more developed markets. These higher risks include, but are not limited to, higher volatility, limited liquidity, a narrow export base, current account deficits and changes in the political, economic, social, legal and regulatory environment. Emerging economies, such as the Georgian economy, are subject to rapid change and are vulnerable to market conditions and economic downturns elsewhere in the world. Although the Government has been successful in its efforts to reduce corruption, emerging markets in general may experience more instances of corruption of government officials and misuse of public funds than more mature markets.

In addition, international investors' reactions to events occurring in one emerging market country or region sometimes appear to demonstrate a "contagion" effect, in which an entire region or class of investment is disfavoured by such investors. If such a "contagion" effect occurs, Georgia could be adversely affected by negative economic or financial developments in other emerging market countries. Georgia has been adversely affected by "contagion" effects in the past, including following the 1998 Russian financial crisis and the more recent global financial crisis. No assurance can be given that it will not be affected by similar effects in the future, including the recent volatility in the Middle East. See "*—A continuation of the turmoil in global credit markets as a result of the global financial crisis has adversely affected, and may continue to adversely affect, the Georgian economy*".

As a consequence, an investment in the Company carries risks that are not typically associated with investing in more mature markets. These risks may be compounded by incomplete, unreliable or unavailable economic and statistical data on Georgia, including elements of information provided in this Prospectus. Prospective investors should also note that emerging economies such as Georgia's are subject to rapid change and that the information set out in this Prospectus may become outdated relatively quickly. Accordingly, prospective 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 suitable only for sophisticated investors who fully appreciate the significance of the risks involved. Prospective investors are urged to consult with their own legal and financial advisers before making an investment decision.

A continuation of the turmoil in global credit markets as a result of the global financial crisis has adversely affected, and may continue to adversely affect, the Georgian economy

The global financial crisis, which commenced in 2008, has severely affected global markets. Financial markets in the United States, Europe and Asia experienced, and in some cases continue to experience, a period of unprecedented turmoil and upheaval characterised by extreme volatility and declines in security prices, severely diminished liquidity and credit availability, inability to access capital markets, the bankruptcy, default, failure, collapse or sale of various financial institutions and an unprecedented level of intervention from the United States federal government and other governments. Unemployment has risen while business, economic activity and consumer confidence have declined, resulting in a severe global recession. In addition to the global financial crisis, the need for many governments to finance large and growing budget deficits and other factors have negatively affected the financial standing and the credit ratings of sovereign and quasi-sovereign issuers, particularly in Europe and the Persian Gulf region. The continuation of turmoil in global credit markets may continue to adversely affect Georgia's economy, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The risk of political instability in Georgia could have a material adverse effect on the Company's business

Since the restoration of its independence in 1991, Georgia has had an on-going substantial political transformation from a constituent republic in a federal socialist state to an independent sovereign democracy. Political conditions in Georgia were highly volatile in the 1990s and in the early part of the 2000s. Since January 2004, following the peaceful uprising in November 2003, known as the "Rose Revolution", Mikheil Saakashvili has served as President of Georgia. While Georgia has introduced policies oriented towards the acceleration of political and economic reforms, there can be no assurance that current Government policies or economic or regulatory reforms will continue at the same pace or at all. Georgia faces several challenges, including ongoing tensions with Russia and the need to implement further economic and political reforms. No assurance can be given that such reforms and economic growth will not be hindered as a result of the disruption of government continuity or any other changes affecting the stability of the Government or as a result of a rejection or reversal of reform policies. Political instability in Georgia could have negative effects on the economy and this could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The next presidential elections are scheduled to be held in 2013. Pursuant to the provisions of Georgia's constitution dated 24 August 1995 (as amended) (the "**Constitution**"), President Saakashvili cannot stand for a third term in office. A change in President may lead to political instability within the country. A number of measures of electoral reform have been passed by the Parliament in recent years, partially in response to protests following the parliamentary elections in 2008, and further reforms are being considered by the Parliament in consultation with international advisers. During its monitoring of municipal elections in May 2010, while the Organisation for Security and Cooperation in Europe (the "**OSCE**") noted significant improvements to Georgia's compliance with OSCE and the Council of Europe's standards in relation to elections, certain significant shortcomings were also cited.

The next parliamentary elections are scheduled to be held in October 2012. Any protests or criticism in relation to the conduct of such elections may lead to political instability within the country. In addition, there can be no assurance that members of the next Parliament will continue the current Parliament's economic and fiscal policies.

In 2010, a State Commission proposed significant amendments to the Constitution of Georgia (the "**Constitutional Amendments**"). Parliament approved the Constitutional Amendments in October 2010. Among the effects of the Constitutional Amendments is an enhancement of the primary governing responsibility of the Parliament and a concomitant reduction of the powers of the Presidency. Most provisions of the Constitutional Amendments will become effective after the next presidential elections, scheduled for 2013. Certain provisions relating to local self-government entered into force on 1 January 2011. There can be no assurance that the implementation of the Constitutional Amendments will not create political disruption or instability or otherwise negatively affect the political climate in Georgia.

In light of such recent political developments, there can be no assurance that the Government will be able to maintain political and civil stability or that reform and economic growth will not be hindered as a result of any such events. Any of the events referred to above could have negative effects on the economy in Georgia, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Regional tensions could have a material adverse effect on the Company's business

Since the restoration of its independence in 1991, Georgia has had on-going disputes in the Georgian regions of Abkhazia and Tskhinvali and with Russia. These disputes have led to sporadic violence and breaches of peace-keeping operations. In August 2008, the conflict in the Tskhinvali Region, Georgia (the "**2008 Conflict**") escalated as Georgian troops engaged with local militias and Russian forces that crossed the international border. In the days that followed the initial outbreak of hostilities, Georgia declared a state of war as Russian forces launched bombing raids deep into Georgia, targeted and destroyed Georgian infrastructure (including railway assets of the Company), blockaded part of the Georgian coast, took control of the Tskhinvali Region, Georgia (the regional administrative centre) and Abkhazia, Georgia and landed marines on the Abkhaz coast. After five days of heavy fighting, the Georgian forces were defeated, enabling the Russians to enter Georgia uncontested and occupy the cities of Poti, Gori, Senaki and Zugdidi. In August 2008, Georgia and Russia signed a French-brokered ceasefire that called for the withdrawal of Russian forces. Russian troops, however, continue to occupy Abkhazia, Georgia and the Tskhinvali Region, Georgia, and tensions continue. Russia's subsequent recognition of the independence of Abkhazia, Georgia and the Tskhinvali Region, Georgia was rejected by Georgia. Georgia withdrew from the CIS in August 2009.

Russia has indicated that it views the eastward expansion of the North Atlantic Treaty Organisation ("**NATO**"), potentially including ex-Soviet republics, such as Georgia, as hostile. Any future deterioration or worsening of Georgia's relationship with Russia, including any major changes in Georgia's relations with Western governments and institutions, in particular in terms of national security, Georgia's importance to Western energy supplies, the amount of aid granted to Georgia or the ability of Georgian manufacturers to access world export markets, may have a negative effect on the stability of Georgia, both in political and economic terms, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Economic instability in Georgia could have a material adverse effect on the Company's business

Since the dissolution of the Soviet Union in the early 1990s, Georgia's society and economy have undergone a rapid transformation from a one-party state with a centrally-planned economy to a pluralist democracy with a market economy. This transformation has been marked by periods of significant instability resulting at various times in declines in GDP, hyperinflation, an unstable currency, high levels of state debt relative to GDP, the existence of a "black" and "grey" market economy, high unemployment and underemployment and the impoverishment of a portion of the Georgian population.

The combined effects of the 2008 Conflict and the global financial crisis on the Georgian economy resulted in a recession from the second half of 2008 through the first half of 2009, ending several years of relatively high economic growth following the implementation of a series of economic reforms by the Government beginning in 2004. The economy returned to growth in the second half of 2009, and this recovery has continued through the date of this Prospectus. There can be no assurance, however, that this more recent economic growth will continue or will not be reversed.

Georgia's current account deficit was 22.1 per cent. of nominal GDP in 2008, before declining to 10.6 per cent. of nominal GDP in 2009, 10.3 per cent. in 2010 and an estimated 11.7 per cent. of nominal GDP in 2011. As a result of the decrease in net foreign direct investment ("**FDI**") inflows beginning in the second half of 2008, in recent years, the current account deficit has been financed, in part, by increased borrowing. In general, a significant increase in the current account deficit, which is not accompanied by a recovery in net FDI inflows, may result in a further increase in the levels of Government borrowing to finance the current account deficit, a revaluation of the Lari or a reduction in imports, any of which could have a material adverse effect on the Georgian economy.

In addition, the Georgian economy is highly dollarised. Prior to 2008, the dollarisation rate had been declining with foreign currency deposits accounting for approximately 65 per cent. of all deposits as at 31 December 2007. As a result of the combined effects of the 2008 Conflict and the global financial crisis on Georgia, however, the dollarisation rate increased to approximately 76 per cent. as at 31 December 2008, although it has since decreased to 59.0 per cent. as at 31 December 2011. Although the NBG has adopted measures to support the development of Georgia's domestic money markets, the dollarisation rate could adversely impact the effectiveness of the implementation of the NBG's monetary and exchange rate policies.

Beginning in 2008, the Lari generally depreciated against the U.S. Dollar and other currencies, although it has generally appreciated against the U.S. Dollar and other currencies since October 2010. See "*—Fluctuations in exchange rates and inflation could have a material adverse effect on the Company's business*". Inflation had increased to an annual rate of 11.2 per cent. by the end of 2010, although it decreased to 2.0 per cent. as at 31 December 2011. A material depreciation of the Lari relative to the U.S. Dollar or the Euro, changes in monetary policy, inflation or the occurrence of other negative factors could adversely affect Georgia's economy. This, in turn, could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Certain of the Company's costs, such as materials, maintenance and repairs, energy costs and wages are sensitive to rises in general price levels in Georgia. However, due to competitive pressures, the Company may not be able to pass along the increased costs to its customers. Accordingly, if high rates of inflation return, there can be no assurance that the Company will be able to maintain or increase its margins to cover such cost increases, which could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Fluctuations in exchange rates and inflation could have a material adverse effect on the Company's business

There was significant instability in the Lari-U.S. Dollar exchange rate and the Lari-Swiss Franc exchange rate following the Russian financial crisis of August 1998 and the 2008 Conflict. While the Lari generally appreciated against the U.S. Dollar, the Swiss Franc and other major international currencies from 2001 to 2008, the Lari had generally then depreciated until October 2010. Since October 2010, however, the Lari has generally appreciated against such currencies. In addition, in November 2008, the NBG devalued the Lari by 16 per cent., a measure aimed at alleviating the negative impact of the global financial crisis on the Georgian economy. The ability of the Government and the NBG to limit any volatility of the Lari will depend on a number of political and economic factors, including the NBG's and the Government's ability to control inflation, the availability of foreign currency reserves and FDI inflows, and any failure to do so or a major depreciation or further devaluation of the Lari could adversely affect Georgia's economy. According to estimates provided by Geostat, annual inflation, as measured by the end-of-period consumer price index, in Georgia was 3.0 per cent. in 2009, 11.2 per cent. in 2010 and 2.0 per cent. in 2011. A return to high and sustained inflation could lead to market instability, a financial crisis, a reduction in consumer purchasing power and erosion of consumer confidence. Any of these events could lead to deterioration in the performance of Georgia's economy, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

Weaknesses relating to the Georgian legal system and legislation create an uncertain environment for investment and business activity in Georgia

Georgia is still developing an adequate legal framework required for the proper functioning of a market economy. Several fundamental Georgian civil, criminal, tax, administrative and commercial laws have only recently become effective. The recent nature of much of Georgian legislation and the rapid evolution of the Georgian legal system place the quality and the enforceability of laws in doubt and result in ambiguities and inconsistencies in their application.

In addition, the court system is understaffed and has been undergoing significant reforms. Judges and courts in Georgia are generally less experienced in the area of business and corporate law than is the case in certain other countries, particularly the United States and EU countries. Most court decisions are not easily available to the general public, and enforcement of court judgments may, in practice, be difficult in Georgia. The uncertainties of the Georgian judicial system could have a negative effect on the economy, which could, in turn, have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Company may experience increases in its income taxes

During the three years ended 31 December 2011 and as at the date of this Prospectus, the corporate income tax rate in Georgia has been 15 per cent. This tax rate is generally lower than the tax rate applicable to other of the Company's peer companies, particularly those operating in more developed Western countries. Furthermore, by virtue of the Economic Liberty Act passed by Parliament in July 2011 and scheduled to enter into force on 31 December 2013, subject to certain exceptions, referenda are required to be held before raising taxes and tax rates. Georgia is, however, a parliamentary democracy and any change in the composition of the Government could result in a change to such taxation policies. The next parliamentary elections are due to be held in October 2012. In addition, while President Saakashvili has been a supporter of the free market and an environment of lower tax rates, he will not be eligible to stand at the next presidential elections scheduled to be held in 2013. A change in President may also lead to a change to taxation policy in Georgia. Any significant increase in the rate of corporate income tax in Georgia could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The uncertainties of the Georgian tax system could have a material adverse effect on the Company's business and on taxation of the Notes

A new Tax Code was adopted in Georgia on 17 September 2010 and came into effect on 1 January 2011 (the "**Tax Code of Georgia**"). Differing opinions regarding the interpretation of various provisions exist both among and within Governmental ministries and organisations, including the tax authorities, creating uncertainties, inconsistencies and areas of conflict. While the Company believes that it is currently in compliance with the tax laws affecting its operations, it is possible that the relevant authorities could take differing positions with regard to interpretative issues, which may result in the Company facing tax adjustments or fines. In addition, there can be no assurance that the current tax laws or Government tax policies will not be subject to change in the future, including changes introduced as a result of a change of government. Such changes, among other things, could include the introduction of new taxes or an increase in the tax rates applicable to the Company. Any such changes in the tax laws or governmental tax policies may have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes. See also "*—The Company may experience increases in its income taxes*".

The Tax Code of Georgia does not provide a clear definition of the place of sale (or supply) of the Notes for the purposes of determining profit/income tax exposure, and, accordingly, while it is unlikely that the sale of Notes, absent a sale of Notes on the territory of Georgia or to a Georgian tax resident, will trigger any Georgian tax obligations on the part of Noteholders, there is a risk that this trigger may be interpreted differently by the tax authorities. The relative novelty of the offering of debt securities out of Georgia, as well as the ambiguities noted above concerning the application of the respective provisions of the Tax Code of Georgia, combined with the absence of established practices, may result in varying interpretations of the applicable provisions of the Tax Code of Georgia by the tax authorities. In addition, there are past instances in which the tax authorities have been known to apply varying interpretations to the respective provisions of the Tax Code of Georgia to address the impracticability or unenforceability of certain provisions with respect to non-resident tax payers.

Foreign judgments and arbitral awards may not be enforceable against the Company.

On the basis of certain precedents established by foreign judiciaries, it may not be possible to effect service of process against the Company in courts outside Georgia or in a jurisdiction to which the Company has not explicitly submitted. Pursuant to Article 68.2 of the *Law of Georgia on Private International Law*, foreign court judgments against the Company will not be recognised and enforceable in Georgian courts if: (i) the matter is within exclusive competence of Georgia; (ii) there is a violation in the service of process or other procedures under the law of the country of the court which rendered the judgment; (iii) a dispute involving the same subject matter between the same parties has already been decided by a Georgian court or by a foreign court, judgment of which has been recognised in Georgia; (iv) the court rendering the judgment is not considered competent to adjudicate the dispute under Georgian legislation; (v) the country whose court has rendered the judgment does not recognise the judgments of Georgian courts; (vi) a dispute involving the same subject matter between the same parties is already being heard in a Georgian court; or (vii) the judgment of the foreign court contradicts fundamental principles of Georgian law. Pursuant to Article 45.1 of the *Law of Georgia on Arbitration*, arbitral awards against the Company may not be recognised and enforceable in Georgia if: (i) the party against whom the award is made proves before Georgian courts that: (a) a party to the arbitration lacked legal capacity; (b) the arbitration agreement is void or set aside pursuant to the law specified by the parties in the arbitration agreement or, in the absence of such, based on the laws of the place where the award was made; (c) a party was not duly informed about the appointment of an arbitrator or the arbitration proceedings, or was not able to participate in the proceedings for other valid reasons; (d) the arbitral tribunal issued the award on a subject matter beyond the scope of the arbitration agreement; (e) the composition of the arbitral tribunal or the procedure of the arbitration was not in accordance with the arbitration agreement, or, in the absence of such agreement, the arbitration was conducted in violation of the laws of the place of arbitration; or (f) the arbitral award has not yet become binding or has been set aside or suspended by the courts of the state in which, or under the laws of which, the award was made; or (ii) the court establishes that: (a) the subject matter of the dispute is not subject to arbitration under Georgian law; or (b) the award is contrary to public policy. No treaty exists between Georgia and many Western jurisdictions, including many EU jurisdictions, for the reciprocal enforcement of foreign court judgments.

In addition, the Terms and Conditions of the Notes are governed by English law and provide that disputes arising from or in connection with the Notes may be settled by arbitration. Georgia is a party to the New York Convention. Therefore, an arbitration award obtained in a country which is also a party to the New York Convention, such as the United Kingdom, would be enforceable in Georgia, subject to the terms of the New York Convention and compliance with Georgian civil procedure regulations, the Law of Georgia on Arbitration and other procedures and requirements established by Georgian legislation. It may be difficult, however, to enforce arbitral awards in Georgia due to a number of factors, including the lack of experience of Georgian courts in international commercial transactions, certain procedural ambiguities and Georgian courts' inability to enforce such orders, all of which could introduce delay and unpredictability into the process of enforcing any foreign arbitral award in Georgia.

Furthermore, the choice of English law as the governing law of the Terms and Conditions of the Notes and the transaction documents may not be given effect, and the recognition or enforcement of foreign court judgments and arbitral awards may be limited, by application of the Georgian law principle requiring compliance with mandatory provisions of the law of the country most closely connected to the transaction, including mandatory provisions of Georgian law. The nature and scope of such mandatory provisions are subject to a considerable degree of discretionary authority of the court in which recognition or enforcement of the judgment or arbitral award is being sought.

Risks Related to the Notes

Payments on the Notes could be subject to EU withholding tax in certain circumstances.

Under EC Council Directive 2003/48/EC on the taxation of savings income (the "**EU Savings Directive**"), each Member State is required to provide to the tax authorities of another Member State details of payments of interest (and/or other similar income) paid by a person within its jurisdiction to an individual or to certain other persons in that other Member State. However, for a transitional period, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-EU countries and territories, including Switzerland, have adopted similar measures (a withholding system in the case of Switzerland).

The European Commission has proposed certain amendments to the EU Savings Directive, which may, if implemented, amend or broaden the scope of the requirements described above.

If a payment is made or collected through a Member State that has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither the Company nor any Transfer Agent (as defined in "*Terms and Conditions of the Notes*") nor any other person is obliged to pay additional amounts with respect to any Note as a result of the imposition of such withholding tax. Under the Terms and Conditions of the Notes, the Company is required to maintain a Paying and Transfer Agent in a Member State that would not be obliged to withhold or deduct tax pursuant to the EU Savings Directive.

The trading price of the Notes may be volatile.

The market for the Notes will be influenced by economic and market conditions in Georgia and, to varying degrees, interest rates, currency exchange rates and inflation rates in other countries, such as the United States, the Member States of the EU and elsewhere. There can be no assurance that an active trading market for the Notes will develop, or, if one does develop, that events in Georgia or elsewhere will not cause market volatility or that such volatility will not adversely affect the liquidity or the price of the Notes or that economic and market conditions will not have any other adverse effect. If the Notes are traded after their initial issuance, they may trade at a discount to their offering price, depending upon prevailing interest rates, the market for similar securities, general economic conditions, the financial condition of the Company or other factors. Any such volatility could have a material adverse effect on the Company's business, financial condition, results of operations and prospects, as well as on the trading price of the Notes.

The Terms and Conditions of the Notes include only a limited restriction on the Company's ability to incur additional indebtedness

Although the Terms and Conditions of the Notes include a covenant limiting the ability of the Company and its Subsidiaries to incur additional Financial Indebtednesss (as defined in Condition 3), subject to certain conditions, this covenant nevertheless permits the Company and its Subsidiaries to incur substantial additional Indebtedness in addition to the Notes. See "*Terms and Conditions of the Notes—Condition 3(d)—Incurrence of Financial Indebtedness*". The incurrence of such additional Indebtedness may reduce the amount investors may recover in respect of the Notes in certain circumstances by adversely affecting the Company's ability to repay principal of, and make payments of interest on, the Notes. This could also have a material adverse effect on the trading price of the Notes.

Unsecured obligations.

The Notes constitute unsecured obligations of the Company, save to the extent required to be secured as set out in "*Terms and Conditions of the Notes – Condition 3(a) Negative Pledge*".

Changes in respect of the credit ratings of the Notes may materially and adversely affect the trading price of the Notes.

The Notes are expected to be rated BB- (outlook: stable) by Fitch and BB- (outlook: stable) by S&P. Each of Fitch and S&P is established in the European Union and is registered under the CRA Regulation. The Company cannot be certain that a credit rating will remain for any given period of time or that a credit rating will not be downgraded or withdrawn entirely by the relevant rating organisation if, in its judgment, circumstances in the future so warrant. Neither the Company nor any of the Joint Lead Managers has any obligation to inform the holders of the Notes (the "**Noteholders**") of any such revision, downgrade or withdrawal. Any adverse change in an applicable credit rating could have a material adverse effect on the trading price of the Notes.

The ratings may not reflect the potential impact of the risks discussed above, as well as any other factors that may affect the value of the Notes. A credit rating is not a recommendation by the rating organisation or any other person to buy, sell or hold securities and may be subject to revisions or withdrawal at any time by the assigning rating organisation and each should be evaluated independently from the other.

The Notes are subject to exchange rate risks and exchange controls.

The Company will pay principal and interest on the Notes in U.S. Dollars. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than U.S. Dollars. These include the risk that exchange rates may significantly change (including changes due to the depreciation of the U.S. Dollar or appreciation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to the U.S. Dollar would decrease: (i) the Investor's Currency-equivalent yield on the Notes; (ii) the Investor's Currency-equivalent value of the principal payable on the Notes; and (iii) the Investor's Currency-equivalent market value of the Notes.

Governments and monetary authorities may impose (as some have done in the past) exchange controls that could materially adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal at all. This could have a material adverse effect on the trading price of the Notes.

The Notes are subject to interest rate risks.

An investment in the Notes involves the risk that subsequent changes in market interest rates could have a material adverse effect on the value and trading price of the Notes.

The Terms and Conditions of the Notes provide for decisions of majorities to bind all Noteholders.

The Terms and Conditions of the Notes contain provisions for calling meetings of Noteholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Noteholders, including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority.

The Terms and Conditions of the Notes provide significant flexibility for value to leave the Company

The Terms and Conditions of the Notes include a covenant restricting the declaration or payment of dividends, and the making of other distributions, in respect of the Company's share capital, as well as voluntary repurchases, redemptions and repayments of the Company's share capital or subordinated indebtedness. This covenant does not prohibit, however, a variety of investments and distributions by the Company and its Subsidiaries, which, if made or paid, could reduce amounts that would otherwise be available to the Company to make payments in respect of the Notes. See "*Terms and Conditions of the Notes—Condition 3(f)—Limitation on Restricted Payments.*"

USE OF PROCEEDS

The net proceeds of the issue of the Notes, expected to be approximately U.S.$497,834,520, will be used for general corporate and liquidity management purposes, which may include (i) financing of such amounts (if any) as may become payable in connection with the 2010 Notes Tender and (ii) the payment of dividends in respect of cumulative profits for 2011 and prior years to the extent such dividends may be recommended by the Company and approved by its shareholders.

Subject to the successful completion of the issue of the Notes, the Company expects to declare a dividend in the aggregate amount of up to GEL 350 million in respect of cumulative profits for 2011 and prior years, which will, if declared, be paid, in one or more instalments. If such dividend is declared and paid, to the extent expenses are due to be reimbursed by the State under the terms of the Bypass Project Memorandum at the time of any such instalment (see "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Bypass Project Memorandum*"), the Company may retain an amount in respect thereof equivalent to CHF 138 million (approximately GEL 237.5 million) and pay out only the balance of up to approximately GEL 102.5 million in cash.

CAPITALISATION

The following table sets forth the cash and cash equivalents, bank deposits and capitalisation of the Company as at 31 December 2011.

	As at 31 December 2011	
	(U.S.$ millions)[1]	*(GEL millions)*
Cash and cash equivalents	38.6	64.5
Bank deposits[2]	45.7	76.4
Debt		
Total current loans and borrowings[3]	11.1	18.6
Total non-current loans and borrowings[4]	247.9	414.1
Net debt[5]	**174.7**	**291.8**
Equity		
Charter capital	599.0	1,000.5
Non-cash owner contribution reserve	22.8	38.0
Retained earnings	457.1	763.5
Total equity	**1,078.8**	**1,802.0**
Total capitalisation[5]	**1,337.9**	**2,234.7**

(1) For convenience, these figures have been translated into U.S.$ at the period-end GEL/U.S.$ exchange rates published by the NBG for 31 December 2011, which was GEL 1.6703 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) Bank deposits are money held in demand deposit accounts.

(3) Total current loans and borrowings are the current portion of non-current loans and borrowings.

(4) Total non-current loans and borrowings are the long-term loans and borrowings, net of current portion.

(5) Net debt ("**Net debt**") is calculated by subtracting cash and cash equivalents and bank deposits from the sum of total non-current loans and borrowings and total current loans and borrowings.

(6) Total capitalisation is the sum of total current loans and borrowings, total non-current loans and borrowings and total equity.

Prospective investors should read the above table in conjunction with "*Selected Historical Financial and Operating Information*", "*Management's Discussion and Analysis of Results of Operations and Financial Condition*" and the Consolidated Financial Statements, together with the respective notes thereto, included in this Prospectus beginning on page F-1.

Since 31 December 2011, the following changes to the Company's capital have occurred:

- On 2 March 2012, the Company transferred several land plots in the town of Samtredia, in the region surrounding Samtredia and Senaki, with an aggregate value of approximately GEL 0.1 million and which the Company treated as a non-core asset, to the State. This transaction has been treated as a withdrawal from capital.

- On 23 March 2012, the Company transferred a land plot in Tbilisi and resolved to transfer the buildings erected on it, with a value of approximately GEL 9.8 million and which the Company treated as a non-core asset, to the State. The transaction has been treated as a withdrawal from capital.

- In March 2012, as part of the Modernisation Project, a land plot in Khashuri and a building erected on it, with a value of approximately GEL 0.03 million were contributed by the State to the Company's capital.

- In March 2012, the Company declared a dividend in the total amount of GEL 28 million in respect of the Company's 2011 profits. The Company paid GEL 10 million of this dividend in April 2012 and the balance of GEL 18 million in a second instalment in May 2012.

- In April 2012, as part of the Modernisation Project, 33 land plots (including six buildings and a reservoir), with an aggregate value of approximately GEL 11.2 million, were contributed by the State to the Company's capital.

- In April 2012, land plots and assets located in Kulevi, with an aggregate value of approximately GEL 48.0 million were contributed by the State to the Company's capital.

- In April 2012, the Company transferred to the State the partially constructed Batumi Tower, as well as the land plots upon which the building is being constructed, all of the rights and obligations under the construction agreement and all other agreements executed in connection with this project, as well as cash in the amount of approximately GEL 3 million for the purposes of implementation of the project. The total value of such assets transferred to the State amounted to GEL 33.6 million.

SELECTED HISTORICAL FINANCIAL AND OPERATING INFORMATION

This section should be read together with the information contained in "Presentation of Financial and Other Information", "Use of Proceeds", "Capitalisation", "Management's Discussion and Analysis of Results of Operations and Financial Condition", the Consolidated Financial Statements and the respective notes thereto included elsewhere in this Prospectus.

The following selected consolidated historical financial information as at and for the three-month periods ended 31 March 2012 and 2011 and as at and for the years ended 31 December 2011, 2010 and 2009 has been extracted from the Consolidated Financial Statements, which are included elsewhere in this Prospectus, other than non-IFRS measures and to the extent such financial information has been translated into U.S. Dollars.

Summary Statement of Comprehensive Income Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[(1)]	*(GEL millions)*	
Revenue	63.7	105.8	103.4
Other income	3.4	5.7	4.0
Employee benefits expense	(14.3)	(23.8)	(26.3)
Depreciation and amortisation expense	(14.9)	(24.8)	(23.0)
Electricity and materials used	(7.4)	(12.3)	(12.7)
Other expenses	(8.9)	(14.7)	(20.5)
Results from operating activities	**21.6**	**35.9**	**24.9**
Finance income	6.3	10.4	10.9
Finance costs	(4.0)	(6.6)	(1.5)
Net finance income	**2.3**	**3.9**	**9.4**
Profit before income tax	**23.9**	**39.7**	**34.3**
Income tax expenses	(4.0)	(6.6)	(5.7)
Profit and total comprehensive income for the period	**19.9**	**33.1**	**28.5**

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions)[(1)]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
Revenue	283.2	477.4	404.7	318.8
Other income	7.1	12.0	17.8	10.7
Payroll expenses	(64.4)	(108.5)	(111.3)	(106.1)
Depreciation and amortisation expense	(54.6)	(92.1)	(98.7)	(96.1)
Raw materials and consumables used	(28.4)	(47.8)	(44.6)	(40.3)
Other expenses	(43.4)	(73.2)	(71.8)	(64.1)
Results from operating activities	**99.5**	**167.8**	**96.1**	**22.8**
Finance income	16.0	27.0	45.4	0.6
Finance costs	(6.2)	(10.5)	(17.7)	(4.8)
Net finance income/(costs)	**9.8**	**16.5**	**27.7**	**(4.2)**
Profit before income tax	**109.3**	**184.3**	**123.8**	**18.7**
Income tax expense	(5.9)	(9.9)	(22.3)	(2.9)
Profit and total comprehensive income for the year	**103.4**	**174.4**	**101.5**	**15.8**

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Summary Statement of Financial Position Data

	As at 31 March		As at 31 December			
	2012		2011		2010	2009
	(U.S.$ millions)[(1)]	*(GEL millions)*	*(U.S.$ millions)*[(2)]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
ASSETS						
Non-current assets						
Property, plant and equipment	1,192.5	1,979.5	1,145.4	1,913.2	1,725.6	1,699.9
Investment property	—	—	4.1	6.8	9.9	9.9
Other non-current assets	137.2	227.8	165.2	276.0	136.4	12.8
Total non-current assets	**1,329.7**	**2,207.3**	**1,314.8**	**2,196.1**	**1,871.9**	**1,722.7**
Current assets						
Non-current assets held for distribution	19.9	33.0	—	—	—	—
Inventories	13.9	23.1	14.2	23.7	18.0	23.7
Current tax assets	—	—	0.3	0.5	—	4.6
Trade and other receivables	19.2	31.8	16.4	27.4	26.9	22.2
Prepayments and other current assets	34.6	57.4	16.6	27.7	42.7	35.1
Cash and cash equivalents	25.4	42.1	38.6	64.5	335.9	1.4
Bank deposits	52.5	87.2	45.7	76.4	38.0	—
Total current assets	**165.4**	**274.6**	**131.9**	**220.3**	**461.4**	**87.0**
Total assets	**1,495.1**	**2,481.9**	**1,446.7**	**2,416.4**	**2,333.4**	**1,809.6**
EQUITY AND LIABILITIES						
Equity						
Charter capital	596.7	990.6	599.0	1,000.5	985.4	967.2
Non-cash owner contribution reserve	22.9	38.0	22.8	38.0	35.4	25.3
Retained earnings	463.0	768.6	457.1	763.5	612.3	556.2
Total equity	**1,082.7**	**1,797.2**	**1,078.8**	**1,802.0**	**1,633.0**	**1,548.7**
Non-current liabilities						
Loans and borrowings	248.1	411.8	247.9	414.1	438.4	24.9
Trade and other payables	0.0	0.0	0.0	0.05	0.05	28.9
Deferred tax liabilities	36.1	60.0	36.5	60.9	66.5	74.8
Total non-current liabilities	**284.2**	**471.7**	**284.4**	**475.0**	**504.9**	**128.6**
Current liabilities						
Loans and borrowings	5.0	8.3	11.1	18.6	19.3	3.9
Trade and other payables	48.9	81.2	27.5	46.0	61.9	66.0
Liabilities to the owner	13.4	22.3	7.9	13.2	29.2	26.6
Provisions	11.9	19.8	12.2	20.3	21.6	6.1
Other taxes payable	20.1	33.4	16.1	26.9	27.2	21.8
Dividends payable	7.8	12.9	—	—	—	—
Other current liabilities	16.9	28.0	8.6	14.4	15.0	8.0
Current tax liabilities	4.5	7.5	0.0	—	21.2	—
Total current liabilities	**128.6**	**213.4**	**83.4**	**139.3**	**195.4**	**132.4**
Total liabilities	**412.5**	**684.7**	**367.8**	**614.3**	**700.3**	**261.0**
Total equity and liabilities	**1,495.1**	**2,481.9**	**1,446.7**	**2,416.4**	**2,333.4**	**1,809.6**

(1) For convenience, these figures have been translated into U.S.$ at the period-end GEL/U.S.$ exchange rate published by the NBG for 31 March 2012, which was GEL 1.6600 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) For convenience, these figures have been translated into U.S.$ at the period-end GEL/U.S.$ exchange rate published by the NBG for 31 December 2011, which was GEL 1.6703 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Summary Cash Flow Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		**2011**
	(U.S.$ millions)[(1)]	*(GEL millions)*	
Net cash from operating activities	30.5	50.7	49.1
Net cash used in investing activities	(33.5)	(55.7)	(91.7)
Net cash used in financing activities	(12.3)	(20.5)	(22.3)
Net decrease in cash and cash equivalents	(15.4)	(25.5)	(64.9)
Cash and cash equivalents at 1 January	37.1	61.6	323.9
Effect of exchange rate fluctuations on cash and cash equivalents	1.8	3.0	(6.7)
Cash and cash equivalents at 31 March	23.5	39.0	252.3

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		**2010**	**2009**
	(U.S.$ millions)[(1)]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
Net cash from operating activities	134.0	225.9	231.5	116.7
Net cash used in investing activities	(270.2)	(455.6)	(322.0)	(89.4)
Net cash from/(used in) financing activities	(14.2)	(23.9)	390.1	(29.2)
Net increase/(decrease) in cash and cash equivalents	(150.4)	(253.6)	299.6	(1.9)
Cash and cash equivalents at 1 January	192.1	323.9	1.4	3.2
Effect of exchange rate fluctuations on cash and cash equivalents	(5.2)	(8.8)	23.0	0.1
Cash and cash equivalents at 31 December	36.5	61.6	323.9	1.4

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

Other Financial and Operating Data

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[1]	*(GEL millions)*	
Other Financial Data			
EBITDA[2]	36.5	60.6	47.9
EBITDA Margin[2] (*per cent.*)	—	57.3	46.4
Adjusted EBITDA[3]	35.7	59.3	50.1
Adjusted EBITDA Margin[3] (*per cent.*)	—	56.0	48.4
Selected Operating Data			
Freight volume (*million tonnes*)	—	4.5	4.6
Number of passengers (*millions*)	—	0.7	0.7
Number of working freight cars	—	8,269	8,002
Number of employees	—	12,698	13,997

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses. EBITDA margin is EBITDA divided by revenue. EBITDA and EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to results from operating activities or cash flows from operating activities or as a measure of liquidity or as an indicator of the Company's operating performance or any other measure of performance derived in accordance with IFRS. The Company includes EBITDA, EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(3) Adjusted EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses, certain items included in other expenses (write-off of non-current assets, inventory write-downs due to obsolescence, guarantee provisions and other provisions) and certain items included in other income (gain on sale of subsidiaries and associates, and other). Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Adjusted EBITDA and adjusted EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to cash flows from operating activities or as measures of liquidity or an indicator of the Company's operating performance or any other measures of performance derived in accordance with IFRS. The Company includes adjusted EBITDA, adjusted EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(4) Debt is comprised of current loans and borrowings and non-current loans and borrowings.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions, except as noted)[1]	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*
Other Financial Data				
EBITDA[2]	154.2	259.9	194.8	118.9
EBITDA Margin[2] (*per cent.*)	—	54.4	48.1	37.3
Adjusted EBITDA[3]	154.6	260.6	204.4	124.1
Adjusted EBITDA Margin[3] (*per cent.*)	—	54.6	50.5	38.9
Selected Ratios				
Net cash from operations to debt[4]	—	0.5	0.5	4.1
Debt[4] to Adjusted EBITDA[3]	—	1.7	2.2	0.2
Debt[4] to total equity	—	0.24	0.28	0.02
Selected Operating Data				
Freight volume (*million tonnes*)	—	20.1	19.9	17.1
Number of passengers (*millions*)	—	3.3	3.2	3.1
Number of working freight cars	—	8,122	7,659	7,910
Number of employees	—	13,227	14,335	15,100

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(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses. EBITDA margin is EBITDA divided by revenue. EBITDA and EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to results from operating activities or cash flows from operating activities or as a measure of liquidity or as an indicator of the Company's operating performance or any other measure of performance derived in accordance with IFRS. The Company includes EBITDA, EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(3) Adjusted EBITDA, as calculated by the Company, represents results from operating activities before depreciation and amortisation expenses, certain items included in other expenses (write-off of non-current assets, inventory write-downs due to obsolescence, guarantee provisions and other provisions) and certain items included in other income (gain on sale of subsidiaries and associates, and other). Adjusted EBITDA margin is adjusted EBITDA divided by revenue. Adjusted EBITDA and adjusted EBITDA margin are a non-IFRS measures that are not measurements of financial performance under IFRS and should not be considered as an alternative to cash flows from operating activities or as measures of liquidity or an indicator of the Company's operating performance or any other measures of performance derived in accordance with IFRS. The Company includes adjusted EBITDA, adjusted EBITDA margin and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies. See "*Selected Historical Financial and Operating Information—Reconciliation of EBITDA and Adjusted EBITDA*" for a discussion of the Company's use of EBITDA and adjusted EBITDA and a reconciliation of these figures to profit and total comprehensive income for the period.

(4) Debt is comprised of current loans and borrowings and non-current loans and borrowings. See Note 19 to the 2011 Audited Consolidated Financial Statements.

Reconciliation of EBITDA and Adjusted EBITDA

The following tables present a reconciliation of profit and total comprehensive income for the periods to EBITDA and adjusted EBITDA. EBITDA and adjusted EBITDA are not measures of financial performance under IFRS. EBITDA, adjusted EBITDA and other non-IFRS measures should not be considered in isolation or as an alternative to results from operating activities, cash flows from operating activities or other financial measures of the Company's results of operations or liquidity derived in accordance with IFRS. The Company includes EBITDA, adjusted EBITDA and other non-IFRS measures in this Prospectus because it believes that they are useful measures of the Company's performance and liquidity. Other companies, including those in the Company's industry, may calculate similarly titled financial measures differently from the Company. Because all companies do not calculate these financial measures in the same manner, the Company's presentation of such financial measures may not be comparable to other similarly titled measures of other companies.

For the Three-Month Periods ended 31 March 2012 and 2011

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[(1)]	*(GEL millions)*	
Profit and total comprehensive income for the year	**19.9**	**33.1**	**28.5**
Add back:			
Income tax expense	4.0	6.6	5.7
Net finance income	(2.3)	(3.9)	(9.4)
Results from operating activities	**21.6**	**35.9**	**24.9**
Add back:			
Depreciation and amortisation expenses	14.9	24.8	23.0
EBITDA	**36.5**	**60.6**	**47.9**
Adjustments for:			
Write-off of non-current assets[(2)]	—	—	4.1
Inventory write-downs due to obsolescence	—	—	—
Guarantee provisions	—	—	—
Gain on sale of subsidiaries and associates	—	—	—
Other income: other	(0.8)	(1.3)	(2.0)
Adjusted EBITDA	**35.7**	**59.3**	**50.1**
EBITDA margin[(3)] *(per cent.)*	—	57.3	46.4
Adjusted EBITDA margin[(4)] *(per cent.)*	—	56.0	48.4

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

(2) Write-off of non-current assets is a component of other expenses.

(3) EBITDA margin is EBITDA divided by revenue.

(4) Adjusted EBITDA margin is adjusted EBITDA divided by revenue.

The following table sets forth a breakdown of other income for the three month periods ended 31 March 2012 and 2011:

	For the three-month period ended 31 March		
	2012		2011
	(U.S.$ millions)[(1)]	*(GEL millions)*	
Other income	**3.4**	**5.7**	**4.0**
Income from continuing operations	2.6	4.4	2.0
Gain on sale of subsidiaries and associates	—	—	—
Other income: other	0.8	1.3	2.0

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for the first three months of 2012, which was GEL 1.6604 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

For the Years ended 31 December 2011, 2010 and 2009

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions, except as noted)[(1)]	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*	*(GEL millions, except as noted)*
Profit and total comprehensive income for the year	**103.4**	**174.4**	**101.5**	**15.8**
Add back:				
Income tax expense	5.9	9.9	22.3	2.9
Net finance income/(costs)	(9.8)	(16.5)	(27.7)	4.2
Results from operating activities	**99.5**	**167.8**	**96.1**	**22.8**
Add back:				
Depreciation and amortisation expenses	54.6	92.1	98.7	96.1
EBITDA	**154.2**	**259.9**	**194.8**	**118.9**
Adjustments for:				
Write-off of non-current assets[(2)]	2.4	4.1	4.8	6.6
Inventory write-downs due to obsolescence[(3)]	—	—	—	2.7
Guarantee provisions[(4)]	—	—	15.5	—
Gain on sale of subsidiaries and associates[(5)]	—	—	(4.3)	—
Other income: other	(2.0)	(3.4)	(6.5)	(4.1)
Adjusted EBITDA	**154.6**	**260.6**	**204.4**	**124.1**
EBITDA margin[(6)] *(per cent.)*	—	54.4	48.1	37.3
Adjusted EBITDA margin[(7)] *(per cent.)*	—	54.6	50.5	38.9

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.
(2) Write-off of non-current assets is a component of other expenses; see Note 9 of the 2011 Audited Consolidated Financial Statements and Note 8 of the 2010 Audited Consolidated Financial Statements.
(3) Inventory write-downs due to obsolescence is a component of other expenses. See Note 9 of the 2011 Audited Consolidated Financial Statements and Note 8 of the 2010 Audited Consolidated Financial Statements.
(4) Guarantee provisions is a component of other expenses and principally reflects the provision for a guarantee of indebtedness. The Company provided the guarantee for the benefit of a film production company, which had borrowed GEL 15.3 million to finance a film shot in Georgia. See Note 8 of the 2010 Audited Consolidated Financial Statements and "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Explanation of Key Comprehensive Income Items—Other expenses*".
(5) Gain on sale of subsidiaries and associates is a component of other income. Gain on sale of subsidiary represents the gain to the Company from the sale of JSC Chitakhevi-Borjomi ("**Chitakhevi**"). See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Disposals and write-offs in connection with the 2005 Restructuring Programme*". See the table below for a breakdown of other income for the years ended 31 December 2011, 2010 and 2009.
(6) EBITDA margin is EBITDA divided by revenue.
(7) Adjusted EBITDA margin is adjusted EBITDA divided by revenue.

The following table sets forth a breakdown of other income for the years ended 31 December 2011, 2010 and 2009:

	For the year ended 31 December			
	2011		2010	2009
	(U.S.$ millions)[(1)]	*(GEL millions)*	*(GEL millions)*	*(GEL millions)*
Other income	**7.1**	**12.0**	**17.8**	**10.7**
Income from continuing operations	5.1	8.6	7.0	6.6
Gain on sale of subsidiaries and associates	—	—	4.3	—
Other income: other	2.0	3.4	6.5	4.1

(1) For convenience, these figures have been translated into U.S.$ at the average GEL/U.S.$ exchange rate, based on rates published by the NBG, for 2011, which was GEL 1.6860 per U.S.$1.00. Such translation should not be construed as a representation that the Lari amounts have been or could be converted into U.S. Dollars at this rate or any other rate.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

The following discussion and analysis of the Company's operating and financial results and prospects is based on the Consolidated Financial Statements prepared in accordance with IFRS, as well as the Company's internal financial and operating records. Prospective investors should read the following discussion together with the whole of this Prospectus, including "Risk Factors" and the Consolidated Financial Statements (including the related notes), and should not rely solely on the information set out in this section.

The following discussion includes certain forward-looking statements that, although based on assumptions that the Company's management considers to be reasonable, are subject to risks and uncertainties that could cause actual events or conditions to differ materially from those expressed or implied in this Prospectus. Among the important factors that could cause the Company's actual results, performance or achievements to differ materially from those expressed in such forward-looking statements are those factors that are discussed in "Forward-Looking Statements" and "Risk Factors" in this Prospectus. All statements other than statements of historical fact, such as statements regarding the Company's future financial position, risks and uncertainties related to the Company's business, plans and objectives for future operations, are forward-looking statements.

Overview

JSC Georgian Railway is, by statute, Georgia's only railway operator. It principally provides freight services, transhipping a variety of cargo, including oil, oil products, ores and grains, originating principally in the east from the Caspian Sea and Central Asia to the Black Sea. The Company also provides passenger services. It has a vertically integrated business model, owning and operating the tracks, stations, other infrastructure and rolling stock comprising Georgia's entire national railway system, as well as the land adjoining the tracks. The Company sets its own tariffs without the need to obtain governmental approval.

The Company generates revenues from two principal business segments: the freight transportation segment (the Freight SBU), which provides freight traffic (transportation and handling) and freight car rental services; and the passenger transportation segment (the Passenger SBU), which primarily transports passengers within Georgia. The Freight SBU accounted for 95.6 per cent. of the Company's total revenue for the three-month period ended 31 March 2012 and 95.3 per cent., 93.4 per cent. and 91.4 per cent. of the Company's total revenues for the years ended 31 December 2011, 2010 and 2009, respectively.

The Company's mainline rail network, together with that of Azerbaijan Railway, forms the Caucasus corridor, a key segment of the TRACECA corridor. The Company's mainline rail network is thus a link in the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. As a key link in the transportation chain between Europe and Central Asia, the Company believes that it is uniquely positioned to capitalise on trade between Europe, the Caspian Region and Central Asia. Three of the Company's lines terminate at the Black Sea, at the port cities of Batumi, Kulevi and Poti. Access to these ports allows easy on-shipment of transit cargo to the Mediterranean basin and Europe.

The Company transports both liquid cargoes (primarily, crude oil and oil products) and dry cargoes, with liquid cargoes accounting for 48.8 per cent. of the Company's total freight transportation volumes in the three-month period ended 31 March 2012 and 52.0 per cent. and 57.5 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively. Of the Company's liquid cargoes, transit shipments accounted for 89.4 per cent. of the Company's total freight transportation volumes in the three-month period ended 31 March 2012 and 45.5 per cent. and 51.4 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively.

For the year ended 31 December 2011, the Company had consolidated revenue of GEL 477.4 million, profit and total comprehensive income of GEL 174.4 million and EBITDA of GEL 259.9 million, as compared to consolidated revenue of GEL 404.7 million, profit and total comprehensive income of GEL 101.5 million and EBITDA of GEL 194.8 million for the year ended 31 December 2010. For the three month period ended 31 March 2012, the Company had consolidated revenue of GEL 105.8 million and profit and total comprehensive income of GEL 33.1 million, as compared to consolidated revenue of GEL 103.4 million and profit and total comprehensive income of GEL 28.5 million for the three-month period ended 31 March 2011.

Current Trading and Prospects; Trends

There has been no significant change in the Company's financial or trading position since 31 March 2012, being the date of the most recent financial statements of the Company, which are included in this Prospectus.

The following information contains management's views of developments that have occurred since 31 December 2011 with known effects on the Company's financial condition and results of operations in future financial periods relative to the periods under review, and management's assessment, based on current trends and management's extrapolations, of the likelihood of certain developments in key factors affecting its business, financial condition and results of operations. For certain factors that may intervene to cause actual results to differ materially from management's expectations, see also "*Risk Factors—Risks Related to the Company's Business*".

2010 Notes Tender

On 18 June 2012, the Company invited certain holders of the 2010 Notes to tender any and all such notes for purchase by the Company for cash pursuant to the 2010 Notes Tender at a price of U.S.$1,112.50 for each U.S.$1,000 in principal amount, together with accrued and unpaid interest to the relevant settlement date for tender, subject to certain terms and conditions and restrictions, as set out in a Tender Offer Memorandum dated 18 June 2012 relating to such invitation. On 26 June 2012, the Company announced that, subject to its receipt of sufficient proceeds from the issue of the Notes to provide financing for the payment of the amounts payable under the 2010 Notes Tender, it will accept for purchase U.S.$222,480,000 in aggregate principal amount of 2010 Notes pursuant to the 2010 Notes Tender. Subject as described above, the 2010 Notes Tender is expected to be completed on or about 5 July 2012.

Change in freight tariffs and volume-based discounts

With effect from 1 January 2012, the Company increased its freight tariffs by two per cent. This increase, however, does not apply to discounted tariffs for liquid cargo (which discounts the Company expects to reduce by U.S.$1.50 per tonne with effect from 1 July 2012). With effect from 1 February 2012, the Company reduced the volume-based discount offered on the transport of crude oil and oil products by U.S.$0.50 per tonne transported. See "*Description of the Company's Business—Freight SBU—Freight Tariffs.*"

Also with effect from 1 February 2012, the Company changed its freight tariff currency from Swiss Francs to U.S. Dollars. See "*—Factors Affecting the Company's Results of Operation—Exchange Rates*". The Company may change the tariff currency again at any time on one month's notice to its customers.

The following table sets forth, in Swiss Francs and U.S. Dollars, the Company's average tariffs for April to December 2011 and for January, February and March 2012:

	April–December 2011	**January 2012**	**February 2012**	**March 2012**
	(CHF)		*(U.S.$)*	
Average Tariffs per 1,000 tonne kilometre(1)				
Crude oil	19.3	19.5	22.9	22.9
Oil products	35.0	33.1	39.4	41.2
Total liquid cargo	**26.2**	**25.6**	**30.2**	**30.1**

(1) Average tariffs are calculated as freight traffic revenue (not including any handling charges) per thousand tonne-kilometre. The Company uses a detailed formula for each individual transportation order that takes into consideration factors including the type and weight of freight and the distance over which the cargo is carried. Amounts stated are CHF per 1,000 tonne-kilometre, unless otherwise indicated.

Trends in Freight Volumes

This following discussion on trends that management expects in respect of freight volumes should be read in conjunction with the sections titled "*Factors Affecting the Company's Results of Operations—Freight Volumes*" and "*Industry—Key drivers of freight traffic—Infrastructure Developments*".

First five months of 2012

In the first three months of 2012, volumes transported by the Company decreased by 0.9 per cent., as compared to the same period of 2011. This performance was driven primarily by a decrease in liquid cargo volumes by 13.8 per cent. in the first three months of 2012, as compared to the first three months of 2011, as sustained demand in transportation services for crude oil and oil products was offset by a lack of availability of rolling stock to the Company, as well as adverse weather conditions, particularly in the first two months of the year, creating bottlenecks in ports and other infrastructure and thereby reducing cargo turnover and transportation performance. In the first three months of 2012, dry cargo volumes continued their positive development observed throughout 2011, increasing by 15.4 per cent., as compared to the first three months of 2011, despite the adverse weather conditions. This increase in the first quarter was particularly driven by year-on-year increases between the first quarter of 2012 and the first quarter of 2011, respectively, in grain products (35.8 per cent.), construction freight (29.0 per cent.) and ores (31.6 per cent.).

Beginning in April 2012 and continuing in May 2012, total volumes transported by the Company recovered from the relatively low level experienced in the first quarter of 2012 to the effect that volumes transported by the Company increased overall by 1.7 per cent. in the first five months of 2012, as compared to the same period of 2011. This increase in total volumes, however, was driven largely by an increase in dry cargo volumes by 22.2 per cent. in the first five months of 2012, as compared to the first five months of 2011, primarily reflecting the ongoing economic recovery in the region, which has, in turn, resulted in increased demand for grain products, construction materials, ores and other goods generally transported by the Company. This increase in dry cargo volumes was mostly offset by a decrease by 14.6 per cent. in liquid cargo volumes in the first five months of 2012, as compared to the first five months of 2011, primarily as a result of the lack of availability of rolling stock and the adverse weather conditions early in the year as described above. Volumes of liquid cargo transported in April and May 2012, however, increased by 2.9 per cent. and 9.6 per cent., respectively, as compared to the average monthly volumes of liquid cargo transported in the first three months of 2012, as the Company has begun to experience the positive effects of the Tank Car Lease Agreement entered into in March 2012, which provides the Company with access to additional rolling stock, as well as the effects of improved weather conditions as winter ended. See "—*Tank Car Lease Agreement*". Volumes of dry cargo transported further continued their increasing trend in April and May 2012, increasing by 28.0 per cent. and 26.4 per cent., respectively, as compared to the average monthly volumes of dry cargo transported in the first three months of 2012. These increases primarily reflected continuing higher levels of demand for the types of dry cargo transported by the Company during the ongoing economic recovery.

The following table sets forth the Company's freight volumes, stated on a million tonnes basis, by type of freight for the periods indicated:

	For the five-month period ended 31 May		**For the three-month period ended 31 March**	
	2012	**2011**	**2012**	**2011**
	(million tonnes)			
Freight cargoes				
of which:				
Liquid cargoes	3.8	4.4	2.2	2.6
Dry cargoes	4.3	3.5	2.3	2.0
Total	**8.1**	**8.0**	**4.5**	**4.6**

Liquid volumes

Over the next three to five years, management anticipates that crude oil volumes will experience sustained moderate growth, as compared to the 6.3 million tonnes of crude oil it transported in the year 2010 and 5.4 million tonnes of crude oil it transported in the year 2011. Management believes, on the basis of informal discussions with its customers, that this growth will mainly result from increases in crude oil originating in Kazakhstan, with moderate volume growth from oil originating in Azerbaijan, mostly related to the expansion of the Kulevi oil terminal. In terms of infrastructure, management estimates that the Company's current infrastructure is sufficient to support the future increases in crude oil volumes at least for the next five years, considering that the existing infrastructure has, to management's knowledge, at least the same capacity as it did in the year 2006, when crude oil volumes were at the highest in the Company's history in the post-Soviet era.

Management also believes that oil products volumes may experience a moderate increase in the long-term, particularly transit oil products. The Company expects oil products traffic from Turkmenistan (representing over 50 per cent. of transit volumes) to increase and, at least partially on the basis of this growth, the Company aims to reach the peak level of 2006. Management estimates that total production of oil products in Turkmenistan is approximately 8 million tonnes per annum and that there is scope for the Company to continue to capture an increasing portion of this transit as soon as the existing bottlenecks are resolved. In recent years, the available capacity of the limited number of ferries operating on the Caspian Sea was constrained by the increase in dry cargo volumes, causing a capacity shortage for oil products. The Company believes that the decision of Azerbaijan to add two additional large ferries will drive an increase in oil products volumes transported through the TRACECA corridor. The Company believes that this investment by Azerbaijan may also result in the redirection to the Caspian Sea of some of the Turkmen oil products currently transiting through Iran en route to European markets.

Dry volumes

Management believes that one of the key enablers of higher dry cargo volumes transported by the Company is the expansion of the fleet of ferries operating on the Caspian Sea. According to public sources, there are currently two large and seven small ferries operating on the Caspian Sea. These rail ferries operate between Bulgaria, Russia and Ukraine, as well as between Azerbaijani ports and the Caspian Sea ports of Aktau and Turkmenbashi in Kazakhstan and Turkmenistan, respectively. Azerbaijan is currently adding two large ferries to support transportation needs. One of the ferries is already operational, and the other one is expected to be operational by the end of 2012. Management believes that the addition of these two ferries will provide additional dry cargo volumes to be transported through the TRACECA corridor. Management believes that an additional factor supporting dry volumes growth in the medium and long-term will be the opening of a new, fully-integrated plant in Azerbaijan that transforms bauxite into aluminium oxide and then into aluminium. Management believes that it may be able to capture at least a portion of the export production of this plant.

Management expects other dry cargo, such as construction materials, grain and grain products, ferrous materials and others, to remain stable or experience moderate growth, as these volumes depend to a large extent on regional economic growth, which is expected to be moderate at least in the medium term.

Swiss Franc Exchange Rates

In the periods under review, the appreciation of the Swiss Franc has played a significant role in either increasing or limiting declines in the Company's revenues and increasing operating costs and capital expenditures. On 6 September 2011, the Swiss National Bank announced that it would "no longer tolerate" an exchange rate below CHF 1.20 to the Euro, that it would "enforce this minimum rate with the utmost determination" and that it was "prepared to buy foreign currencies in unlimited quantities". As a result, in the period from 6 September 2011 to 14 June 2012, the Swiss Franc has depreciated against the Lari by approximately 19.2 per cent.

Although a significant portion of the Company's capital expenditures and operating expenses, including the Company's rental charges for using railcars of other national railway operators and many of the costs of materials used for repair and maintenance, continue to be denominated in Swiss Francs, with effect from 1 February 2012, the Company changed its freight tariff currency from Swiss Francs to U.S. Dollars. See "*—Factors Affecting the Company's Results of Operations—Exchange Rates*". Accordingly, in its forecasts, management has assumed that future revenue and profit growth, if any, will be substantially dependent on volume and tariff increases, rather than the effects of currency movements.

Bypass Project Memorandum

In April 2012, the Company and the Government, represented by the Ministry of Finance and the MESD, entered into the Bypass Project Memorandum. The Bypass Project Memorandum creates a set-off mechanism for the Company to be reimbursed by the State for the Company's future expenses in relation to the Bypass Project out of dividends that would otherwise be payable to the State in respect of its shares in the Company and in exchange for the transfer, by the Company to the State, of the Existing Railway Land. The amount to be reimbursed to the Company does not cover an instalment of CHF 36.1 million due to be paid by the Company to its contractor in 2012 and is subject to an aggregate cap of CHF 138.0 million. In May 2012 and to date in June 2012, the Company paid to its contractor approximately GEL 20.4 million (CHF 11.9 million) and GEL 5.0 million (CHF 2.9 million), respectively, of the CHF 36.1 million not covered by the reimbursement obligations and the balance shall be paid by the Company out of its existing cash flows upon the completion of the corresponding work by the contractor. The Existing Railway Land will be transferred to the State upon completion of the Bypass Project or, if later, upon the full reimbursement of reimbursable expenses by the Government. If the dividends payable to the State are insufficient to cover the reimbursable expenses in full, the Company has the right to retain a pro rata ownership interest in the Existing Railway Land. See "*Description of the Company's Business—Bypass Project*".

Tank Car Lease Agreement

On 30 March 2012, the Company (as lessee) entered into an agreement to lease up to 1,000 tank cars from AS Spacecom (as lessor) until 1 April 2015 (the "**Tank Car Lease Agreement**"). Under the Tank Car Lease Agreement, the lessor is required to lease to the Company 425 tank cars within one month from the date of receipt of a request from the Company. Upon the Company's request, the lessor is also required to provide up to a maximum of 575 additional tank cars within one month of the date of receipt of such request. The daily lease price per tank car under the Tank Car Lease Agreement is U.S.$45.00. The Tank Car Lease Agreement may be terminated by the written consent of both parties and AS Spacecom may unilaterally terminate the Tank Car Lease Agreement in the event of non-payment by the Company for a period of 30 days or more. The Company is responsible for the costs and expenses related to the ordinary maintenance of tank cars leased under the Tank Car Lease Agreement. In the event that any other repairs are needed, the costs and expenses in respect of such repairs shall be reimbursed to the Company by AS Spacecom.

As a result of the availability to the Company of an increased supply of tank cars, the Company expects liquid cargo transported by the Company to increase, which would, in turn, have a positive impact on the Company's revenue from freight traffic. The Company also expects its revenue from freight car rental to increase for the same reason. The Company expects such benefits to outweigh the costs of the leasing arrangements. As at the date of this Prospectus, 375 tank cars have been received pursuant to the Tank Car Lease Agreement, with 50 further tank cars expected to be received by the end of June 2012.

Factors Affecting the Company's Results of Operations

The Company's performance and results of operations have been and continue to be affected by a number of factors, the most significant of which are set out below. See also "*Risk Factors*".

Macroeconomic and political factors

The Company's results have been, and future results are likely to be, affected by global economic activity in general, and regional and national economic activity in particular. Because substantially all of the Company's revenues are derived from freight transportation, the Company's results are particularly sensitive to trade flows of commodities, such as crude oil, oil products, ores, grain and construction materials. Specifically, freight transit volumes are affected by trade between and among the EU (and, more broadly, Europe) and the member states of the TRACECA corridor. Freight volumes in relation to intra-territorial cargoes are affected by economic activity within Georgia. See "*Industry—The Caucasus Transportation Market*".

The Company's volumes in freight prior to the global recession grew, and since recovery from the global recession began, have grown to a large extent as a result of growing trade between and among the commodity and energy-rich emerging market economies in or near the TRACECA corridor, such as Azerbaijan, Kazakhstan and Turkmenistan, on the one hand, and the EU (and, more broadly, Europe), on the other. The global recession impacted negatively the levels of economic activity in Europe in particular and in several TRACECA members, including Georgia, and consequently trade undertaken among and between these countries declined and industrial activity slowed within Georgia. The Company's volumes began to suffer a decline in August 2008, due in part to the reduced economic activity and in part to the 2008 Conflict with Russia. These declines accelerated through the rest of 2008 and peaked in the first quarter of 2009, resulting in overall reduced freight volumes for the Company in the year ended 31 December 2009. The Company's freight volumes declined in the year ended 31 December 2009 to 5,383.4 million tonne-kilometres from 6,485.3 million tonnes per kilometre in the year 2008 as demand for commodities and construction materials declined both in Georgia and in end markets of the TRACECA corridor.

Passenger volumes, particularly in the more profitable market segment of international travel, are affected by the levels of disposable income of populations both in Georgia and in the countries neighbouring Georgia. This correlation partly explains, for example, the decline in the number of passengers during the last global recession to 3.1 million passengers in the year ended 31 December 2009, from 3.4 million passengers in the year ended 31 December 2008. In particular, the number of the Company's international passengers in the summer season, when international traffic is highest due to people travelling to Black Sea resorts from Armenia and Azerbaijan, declined significantly in 2009 compared to 2008. See "*Industry—Passenger Traffic Overview*".

The gradual recovery from the global financial crisis has also resulted in increases in international trade, and the Company's freight volumes, particularly transit volumes, have recovered, increasing to 5,986.7 million tonne-kilometres in 2011 and 6,190.8 million tonnes per kilometre in 2010 from 5,383.4 million tonnes per kilometre in 2009.

Political and military intervention can also have an effect on the Company's business. During the 2008 Conflict, for example, transit railway traffic through Georgia ceased entirely for four days and did not fully resume until September

2008. See "*Risk Factors—Risks Related to Georgia—Regional tensions could have a material adverse effect on the Company's business*".

The war in Afghanistan, conversely, has resulted in greater demand for eastbound freight transit through Georgia due to the military presence in Afghanistan requiring fuel and other supplies. The Company began to transport such cargo in the third quarter of 2010 through a freight forwarder, having taken the strategic decision, in light of temporary oil tank car capacity constraints, to reallocate some of its oil tank car fleet previously used for the transport of liquid cargo from the Azerbaijan westbound route to the eastbound route towards Afghanistan. Such eastbound cargoes travel much longer distances and return with less tonnage once delivery has been made. They are not subject to any customer volume-related tariff discounts. As a result, cargoes on this route generate higher revenue and profitability than liquid cargoes transported from Azerbaijan despite the lower volume base. In order to respond to growing demand for liquid cargo volumes, the Company has ordered 250 new oil tank cars that it expects to put into operation in the next twelve months. To ensure an adequate stock of oil tank cars pending delivery of these new tank cars, the Company has agreed with Ukrainian Railways to exchange up to 1,000 of the Company's idle dry cargo railcars for 1,000 Ukrainian Railways oil tank cars over a period of twelve months starting from June 2011. To date, approximately 200 railcars have been exchanged under this agreement. The Company's management believes that this number is sufficient to address its current requirements and to match rail car supply to demand.

As at the date hereof, there is uncertainty in the global markets regarding the prospects for a continuation of the recovery.

For a description of the Company's freight volumes and passenger volumes during the periods presented, see "*Description of the Company's Business—Business Operations—Freight SBU—Freight Composition*" and "*Description of the Company's Business—Business Operations—Passenger SBU—Passenger Customers*" and "*—Freight volumes*".

Operational efficiency

The Company has undertaken several initiatives with the overall objectives to increase the efficiency of and otherwise optimise its operations and reduce operational and other costs. In 2005, the Company launched a restructuring programme (the "**2005 Restructuring Programme**") based on the proposals of an independent consultant. The 2005 Restructuring Programme, which was substantially completed in 2008, transformed the Company into an efficient, vertically-integrated company with a strong focus on its core operations. As part of the 2005 Restructuring Programme, the Company separated its operations into the three SBUs, each with separate reporting functions; reorganised the corporate and management systems of the Company; disposed of substantially all of the Company's non-core and non-performing assets in order to realign the Company's asset base; invested in the refurbishment of its assets, particularly rolling stock and rail tracks; and conducted efforts to increase the profitability and cash-generating potential of the Company.

In September 2010, the Company began the implementation phase of its Modernisation Project. The key objectives of the Modernisation Project are:

- optimising freight and passenger traffic;
- optimising stations, depots and infrastructure;
- optimising freight and passenger rolling stock;
- reducing operational expenses;
- improving operational safety;
- improving social and environmental safety;
- increasing train speeds; and
- introducing a clear and defined maintenance programme.

The Modernisation Project focuses primarily on the mainline that runs from Tbilisi to the Black Sea, in particular to the terminals at the Poti and Batumi ports. Based on its own internal estimates and the results of the feasibility study completed by SYSTRA and SNCFI, the Company expects the Modernisation Project to result in a reduction of capital expenditures required for maintenance of its infrastructure and a decrease in operating costs.

To improve profitability and efficiency of the Passenger SBU, the Company has taken a series of measures to improve average revenue per passenger kilometre. These include:

- introducing higher levels of service by investing in new, or improving existing, railcars;
- adjusting schedules with a view to optimising utilisation; and
- adjusting the segmentation of journey pricings, increasing the intervals for price changes from every 50 km to every 120 km.

In 2010, the Company introduced into operation three new modern trains and set correspondingly higher prices for tickets on those trains. The Company also attracted and expects to continue to attract new passengers that were formerly reliant on other modes of transportation, such as mini-buses and private automobiles. There were no other increases in tariffs during that year, but this introduction contributed to the increase in revenues from passenger services in 2010, as compared to 2009. Increasing revenue per passenger kilometre is one of the key objectives of the Passenger SBU.

During the periods presented, the Company has realised reductions, year-on-year, of depreciation and amortisation expense relating to assets attributable to the Freight SBU and the Passenger SBU, including through the replacement of older locomotives, railcars and a certain portion of the railway infrastructure, as part of the general effort to modernise and improve assets.

For a description of the Company's past and budgeted capital expenditures, including those relating to the Modernisation Project, see "*—Liquidity and Capital Resources—Capital expenditures*". See also, "*—Depreciation*".

Exchange rates

The Company's reporting currency is the Lari. To a material extent, the Company enters into transactions denominated in U.S. Dollars and Swiss Francs, and carries a portion of its liabilities and assets in these currencies. Therefore, variations between the rate of exchange between the U.S. Dollar or the Swiss Franc, on the one hand, and the Lari, on the other, have had and will continue to have an effect on the Company's results of operations.

For all periods under review in this Prospectus, the Company has quoted its tariffs in Swiss Francs only, except for tariffs for freight services, which, since 1 February 2012, the Company quotes in U.S. Dollars. The majority of the Company's non-Georgian freight customers pay in Swiss Francs or U.S. Dollars while Georgian customers pay in Lari. In the periods under review, approximately only three to four per cent. of the Company's freight revenues are Lari-denominated, representing principally demurrage charges to Georgian customers. In addition, a significant part of the Company's capital expenditures related to the Modernisation Project and Bypass Project are denominated in Swiss Francs, as were, to a certain extent during the period under review, its operating expenses, including rental charges for using the railcars of other national railway operators and many of the costs of materials used for repair and maintenance. With effect from 1 February 2012, however, the Company changed its freight tariff currency from Swiss Francs to U.S. Dollars, although the tariff for freight car rental is still denominated in Swiss Francs. The Company made such change due to the volatility of the exchange rates between the Swiss Franc and other currencies and also to better align costs and revenues for its customers, which mainly trade in U.S. Dollars or Lari. In April 2012, the Company engaged a consultant with a view to evaluating its options in respect of hedging, including its exposure to fluctuations in the value of the Swiss Franc and the U.S. Dollar and, as at the date of this Prospectus, the Company is in the process of negotiating appropriate hedging agreements under the guidance of this consultant. See "*—Current Trading and Prospects; Trends—Change in freight tariffs and volume-based discounts*".

During the periods discussed herein, the Swiss Franc has experienced average year-on-year appreciation relative to the Lari. Such appreciation has been a significant contributor to the revenue growth in the year ended 31 December 2011 relative to the year ended 31 December 2010, and in the year ended 31 December 2010 relative to the year ended 31 December 2009. The appreciation of the Swiss Franc during the periods under review has also had the effect of contributing to increases in Lari-denominated capital expenditures and, historically, to a certain extent, costs of materials used for repair and maintenance. However, as a result of the change by the Company to quote tariffs for freight transportation in U.S. Dollars, as well as the implementation of the Company's hedging strategies, management expects that future revenue and profit growth, if any, will be substantially dependent on volume and tariff increases rather than the effects of currency movements. See "*—Current Trading and Prospects; Trends—Swiss Franc Exchange Rates*".

The 2010 Notes (to the extent any of the 2010 Notes remain outstanding following completion of the 2010 Notes Tender) and the Notes are denominated in U.S. Dollars, and during the periods presented the Company has incurred a portion of its trade payables in U.S. Dollars. In the period from 1 January 2009 to 31 December 2010, the U.S. Dollar experienced an average year-on-year appreciation relative to the Lari. Such appreciation has had a tendency to increase operating expenses and finance costs, although the Company has offset some of these effects by reducing U.S. Dollar denominated trade payables. In the year ended 31 December 2011, the U.S. Dollar depreciated relative to the Lari. This depreciation reduced the increase in operating expenses and contributed to the reduction in finance costs. The effect of these positive developments was, however, offset in part because trade payables were lower compared to the same period in the prior year.

Fluctuations in the exchange rates between the Lari and the U.S. Dollar and the Lari and the Swiss Franc in the past are not necessarily indicative of fluctuations that may occur in the future.

See "*Exchange Rate Information*" and "*—Quantitative and Qualitative Disclosures about Market Risk—Market risk—Currency risk*."

Freight tariffs

The Company's results of operations are driven to a significant degree by freight tariffs. Although rail transportation in Georgia is a statutory monopoly, the Company's pricing policies are not subject to direct Government regulation. Under the Railway Code, the State has the power to establish tariff policies through a Rail Transport Authority. To date, however, the State has not established any such authority and the Company is not aware of any plans of the State to do so. Accordingly, as at the date of this Prospectus, the Company is not subject to any mandatory tariffs. Instead, pursuant to the Railway Code, it sets its own tariff policy independently for all types of services, including tariffs for freight transportation, freight transportation-related services and passenger services. See "*Description of the Company's Business—Business Operations—Freight SBU—Freight tariffs.*"

The Company's tariff policy is driven by a strategic choice to maintain the Caucasus corridor's competitiveness. The Company therefore generally aims to set tariffs in line with inflation and to balance out currency fluctuations between the Swiss Franc and the Lari, with specific tariff changes targeted to specific situations, for example by offering or removing discounts to specific customers. During the periods under review, the Company has been able to offset the effects of declining volumes at least in part by adjusting freight tariffs. For example, in 2009, tariff increases partially offset the 19.3 per cent. decrease in freight volumes resulting from the global recession.

The following table sets forth information in respect of the Company's freight tariffs, by type of freight, for the periods indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(CHF)		*(per cent.)*	*(CHF)*	*(per cent.)*
Average Tariffs[(1)]					
Crude oil	18.0[(3)]	14.2	26.8	13.9	2.2
Oil products	34.2[(4)]	32.1	6.5	31.9	0.6
Dry cargo	39.3	40.8	(3.7)	42.3	(3.5)[(2)]

(1) Average tariffs are calculated as freight traffic revenue (not including any handling charges) per thousand tonne-kilometre. The Company uses a detailed formula for each individual transportation order that takes into consideration various factors, including the type and weight of freight and the distance over which the cargo is carried. Amounts stated are CHF per 1,000 tonne-kilometre, unless otherwise indicated.

(2) The 3.5 per cent. decrease in 2010, as compared to 2009, was the result of the Company changing the mix of products that affected the Company's revenue per tonne, and was not the result of a decision of the Company to decrease tariffs applied to such products.

(3) Effective 1 April 2011, the Company reduced the discount it offers on the transport of crude oil by 33.0 per cent.

(4) Effective 1 April 2011, the Company reduced the discount it offers on oil products by 23.0 per cent.

The Company offers a 15 per cent. discount on its freight tariffs to customers who transport cargo with their own railcars and use the Company's services for infrastructure and locomotives. In April 2011, the Company reduced the discounts that it offers on the transport of oil and oil products. As a result, the average quarterly tariff on oil increased to CHF 19.25 per thousand tonne-kilometres in the second quarter of 2011 from CHF 14.47 in the first quarter and the average quarterly tariff on oil products increased to CHF 34.58 per thousand tonne-kilometres in the second quarter of 2011 from CHF 31.09 in the first quarter. With effect from 1 February 2012, the Company reduced the volume-based discount offered on the transport of crude oil and oil products by U.S.$0.50 per tonne transported. Also with effect from 1 January 2012, the Company increased its freight tariffs by 2.0 per cent. This increase, however, does not apply to discounted tariffs for liquid cargo. The Company may change its tariffs and discounts it applies to its tariffs upon one month's notice to its customers. See also "*Current Trading and Prospects; Trends—Change in freight tariffs and volume-based discounts*".

Freight volumes

The Company's results of operations are also driven to a significant degree by freight volumes, which are, in turn, driven by global, regional and national economic trends. In the periods presented, volumes for liquid and dry cargo recovered in the year ended 31 December 2010 from the low levels impacted by the recession in the year ended 31 December 2009, due to the positive impact of the global economic recovery. Total volumes, stated on a million tonne-kilometre basis, for the year ended 31 December 2011, as compared to the year ended 31 December 2010, showed a moderate decrease. In the first three months of 2012, volumes transported by the Company further decreased, as compared to the same period of 2011. Beginning in April 2012 and continuing in May 2012, total volumes transported by the Company recovered from the relatively low levels experienced, on average, in the first quarter of 2012 to the effect that volumes transported by the Company increased overall by 1.7 per cent. in the first five months of 2012, as compared to the same period of 2011.

The following table sets forth the Company's freight volumes, stated on a million tonne-kilometre basis, by type of freight, for the periods indicated:

	For the year ended 31 December		
	2011	**2010**	**2009**
		(million tonne kilometres)	
Liquid cargoes	**3,641.8**	**4,044.3**	**3,501.4**
of which:			
Crude oil	2,076.3	2,439.0	2,051.4
Oil products[(1)]	1,565.5	1,605.2	1,450.0
Dry cargoes	**2,344.9**	**2,146.5**	**1,882.0**
of which:			
Ores	481.5	400.5	270.6
Ferrous metals and scrap	279.5	249.8	202.9
Grain	336.6	342.0	334.3
Construction freight	251.7	209.6	163.3
Chemicals and fertilisers	173.3	152.8	142.7
Sugar	187.0	204.8	175.0
Industrial freight	101.1	105.6	111.8
Cement	51.7	77.7	141.6
Other	482.5	403.8	339.8
Total	**5,986.7**	**6,190.8**	**5,383.4**

(1) Oil products include products such as petrol, bitumen, diesel fuel and liquid natural gas (LNG).

The following table sets forth the Company's freight volumes, stated on a million tonnes basis, by type of freight, for the periods indicated:

	For the year ended 31 December					
	2011		2010		2009	
	(million tonnes)	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*
Liquid cargoes	**10.5**	**52.0**	**11.5**	**57.8**	**9.7**	**56.7**
of which:						
Crude oil	*5.4*	*26.8*	*6.3*	*31.7*	*5.2*	*30.4*
Oil products	*5.1*	*25.1*	*5.1*	*25.6*	*4.5*	*26.3*
Dry cargoes	**9.6**	**48.0**	**8.5**	**42.7**	**7.4**	**43.3**
of which:						
Ores	*1.9*	*9.6*	*1.6*	*8.0*	*1.1*	*6.4*
Construction freight	*1.6*	*8.1*	*1.2*	*6.0*	*1.1*	*6.4*
Ferrous metals and scrap	*1.2*	*5.8*	*1.0*	*5.0*	*0.8*	*4.7*
Grain	*1.2*	*6.2*	*1.4*	*7.0*	*1.1*	*6.4*
Chemicals and fertilisers	*0.5*	*2.6*	*0.4*	*2.0*	*0.4*	*2.3*
Cement	*0.5*	*2.5*	*0.4*	*2.0*	*0.7*	*4.1*
Industrial freight	*0.5*	*2.3*	*0.5*	*2.5*	*0.6*	*3.5*
Sugar	*0.5*	*2.7*	*0.6*	*3.0*	*0.5*	*2.9*
Other	*1.7*	*8.3*	*1.4*	*7.0*	*1.1*	*6.4*
Total	**20.1**	**100.0**	**19.9**	**100.0**	**17.1**	**100.0**

In the year ended 31 December 2011, liquid cargoes exceeded dry cargoes by 0.8 million tonnes, or 8.3 per cent. In the years ended 31 December 2010 and 2009, liquid cargoes represented the majority of the Company's volumes, and, of these, crude oil represented the majority. Of dry cargoes, ores, grain, ferrous metals and scrap and construction freight have represented the majority during the periods under review.

Freight volumes increased by 0.2 million tonnes, or 1.0 per cent., in the year ended 31 December 2011, as compared to the same period in 2010. The increase was principally due to an increase of dry cargoes by 1.1 million tonnes, or 12.9 per cent., led primarily by increased volumes of ores and construction freight as continuing economic recovery resulted in greater demand for such products, partially offset by the reduction in grain volumes in 2011 as the increased volumes of shipped grain in 2010 were not sustained. Liquid cargoes volumes, on the other hand, decreased by 1.0 million tonnes, or 8.7 per cent. The primary cause of this decrease was the Company's decision, in light of temporary oil tank car capacity constraints, to reallocate part of the oil tank car fleet previously used to transport liquid cargo on the westbound route from Azerbaijan to the eastbound transport of cargoes to support military operations in Afghanistan. These eastbound cargoes travel much longer distances, and their base tariffs are not subject to volume-related discounts. As a result, they generate higher revenue and profitability than the westbound transports, despite their lower volume base.

Freight volumes increased by 2.8 million tonnes, or 16.4 per cent., in the year ended 31 December 2010, as compared to the same period in 2009. The increase was due to the increases of 1.7 million tonnes, or 17.5 per cent., in liquid cargoes, and 1.1 million tonnes, or 14.9 per cent., in dry cargoes, driven principally by increased demand in the end markets of these products as recovery from the global recession began.

For a description of the freight volumes transported by the Company in the first five months of 2012, as well as the Company's expectations in relation to freight volume developments, see "*—Current Trading and Prospects; Trends—Trends in Freight Volumes*" above.

Issue of the 2010 Notes

In July 2010, the Company issued its 2010 Notes pursuant to which it received proceeds of approximately U.S.$250.0 million, which it converted into Swiss Francs. This conversion enabled the Company to record net finance income in 2010, relating principally to gains realised through appreciation of the Swiss Franc relative to the U.S. Dollar (the denomination currency of the 2010 Notes).

In 2010, the proceeds of the 2010 Notes enabled the Company to fund its capital expenditures and to place cash generated from operating activities into term deposits. Because the proceeds of the 2010 Notes have been used or reserved for capital expenditures, mostly in connection with the Modernisation Project and the Bypass Project, the Company has to date capitalised the interest accruing on these Notes. See "*—Current Trading and Prospects; Trends—2010 Notes Tender*" for a description of the 2010 Notes Tender.

Disposals and write-offs of certain assets

As part of the Company's continued implementation of the 2005 Restructuring Programme (which is now complete) and for other specific reasons that management considers non-recurring, the Company has, during the periods under review, made a series of disposals and has written off certain assets that management has determined to be non-core or no longer necessary for future operations. These include:

- In April 2012, the Company transferred to the State the partially constructed Batumi Tower, which was a project of the Company's subsidiary, Railway Property Management LLC. In addition to the transfer of the partially constructed building, the Company transferred to the State the land plots upon which the building is being constructed, all of the rights and obligations under the construction agreement and all other agreements executed in connection with this project, as well as cash in the amount of approximately GEL 3 million for the purposes of implementation of the project. The total value of assets transferred to the State amounted to approximately GEL 33.6 million.

- In February 2012, the MESD approached the Company with a request to transfer the Tbilisi Central Station, land and other assets fixed to the building to the State. In March 2012, the GMS approved the withdrawal of the abovementioned assets from the Company's authorised capital. As the Company uses certain parts of the Tbilisi Central Station, such as the rail platforms and office area, in its current operations, on 28 March 2012, the Government adopted Decree No. 559 authorising the MESD to enter into a gratuitous usufruct agreement with the Company in respect of the assets needed by the Company for its current operations. The MESD and the Company subsequently entered into such an agreement on 6 April 2012, whereby the MESD granted the Company a right of use over that portion of the Tbilisi Central Station necessary for the Company's operations. The agreement will be in effect until the completion of the Bypass Project and the completion of the Didube and Navtlughi railway stations.

- In November 2011, JSC "Nenskra", which was wholly owned by the Company's subsidiary, Georgian Railway Construction JSC ("**GRC**"), was withdrawn from the Company's authorised capital with a book value of approximately GEL 6.2 million and transferred to the State and then to the PF.

- In October 2010, the Company sold its 25 per cent. stake in Chitakhevi, a company engaged in the operation of a hydropower plant (a "**HPP**"), to EnergoPro Georgia pursuant to a share sale and purchase agreement. The sale generated a one-time gain of GEL 4.3 million. The Company recognised dividends from this subsidiary of GEL 0.6 million in 2009.

- With effect from 24 May 2010, the Company transferred its shares in Railway Telecom LLC ("**Railway Telecom**") to the MESD. In exchange, the MESD agreed to contribute cash or in-kind property with a value of GEL 6.8 million, the fair value attributed to the Railway Telecom shares. During 2010 and the first half of 2011, the MESD contributed certain land plots needed for the Company's operations. As a result, in November 2011, the Company and the MESD acknowledged that the MESD had made the requisite level of in-kind contributions, thereby fulfilling its obligations in connection with the transfer of Railway Telecom. The income statement for the year ended 31 December 2010 therefore reflects only five months of communications services provided by this former subsidiary, affecting the comparability of certain income statement line items, including revenues, as compared to prior years. The effects are explained below in the discussion and analysis of the annual results for the year ended 31 December 2010, as compared to the same period in 2009.

- In 2011, the Company recognised write-offs in the amount of GEL 4.1 million in respect of construction-in-progress assets relating to electric lines and a supporting wall adjacent to rail tracks that management determined to be no longer necessary for operations.

- In 2010, the Company recognised write-offs in the amount of GEL 4.8 million in respect of construction-in-progress assets relating to the cancellation of two low platforms and a supporting wall adjacent to the rail tracks that management determined to be unnecessary for future operations and a HPP and a hotel that were determined to be non-core.

- In 2009, the Company recognised write-offs in the amount of GEL 6.6 million in respect of two non-current assets. The first asset was a station that was previously accounted as investment property that was leased out to a third party that was declared bankrupt in 2009, and the second was a provision in respect of an incomplete building near the Tbilisi Central Station that management determined to be unnecessary for future operations.

Cost of electricity and materials

Electricity constitutes a significant component of the Company's operating expenses. Electricity costs include principally the costs of the electricity used to move the Company's locomotives and vehicles, and the electricity used in the Company's buildings. Approximately 94.0 per cent. of the Company's railway network is electrified. Until September 2011, the Company procured most of its electricity in the open market. In September 2011, the Company signed the Electricity Agreement for the purchase and sale of electricity with EnergoPro Georgia. Management estimates that the electricity EnergoPro Georgia is obligated to deliver under the Electricity Agreement will satisfy almost 90 per cent. of its total electricity requirements. The contract has a term of ten years. The contract fixes tariffs for an initial five year period in line with the upper threshold currently contained in Resolution No. 33 of the Georgian National Energy and Water Regulatory Commission (the "**GNERC**"). Based on the GNERC resolutions, the Company expects that prices for the five years will be (i) 8.274 Lari cents per kilowatt hour for 100/35 kilowatt electricity and (ii) 9.968 Lari cents per kilowatt hour for 6/10 kilowatt electricity. Management estimates that approximately 80 to 83 per cent. of the electricity it buys is 100/35 kilowatt electricity, with the remaining 17 to 20 per cent. being 6/10 kilowatt electricity. As a result, management expects that the average price per kilowatt hour for electricity will be approximately 8.58 Lari cents for the first five years of the Electricity Agreement. From 2016, tariffs will be fixed for a further five years. The tariffs may be adjusted upwards in the limited circumstances provided for under the Electricity Agreement. See "*Description of the Company's Business—Electricity Supply*" for a description of the Electricity Agreement and electricity supply generally to the Company and in Georgia.

Prior to entering into the Electricity Contract, tariffs paid for electricity consisted of three components:

- the portion of the tariff payable to the supplier,

- transmission costs paid to the owner of the transmission lines, and

- fees paid to the Electricity System Commercial Operator ("**ESCO**") for the national electricity reserve maintenance.

These components changed from period to period and, in 2011, represented approximately 75.0 per cent., 20.0 per cent. and 5.0 per cent., respectively, of total electricity costs, as compared to approximately 69.0 per cent., 23.0 per cent. and 8.0 per cent., respectively, in 2010 and 77.0 per cent., 16.0 per cent. and 7.0 per cent. respectively, in 2009.

The following table sets forth the average price of electricity for the periods indicated:

	For the year ended 31 December		
	2011	**2010**	**2009**
		(GEL per kilowatt hour)	
Average price	0.0869	0.0756	0.0732

Average electricity tariffs increased by 14.8 per cent. in the year ended 31 December 2011, as compared to 2010, due primarily to an increase of 24.7 per cent. in the portion of the electricity tariff attributable to suppliers. This was due principally to increasing demand for electricity generally in Georgia as a result of continued economic and industrial growth and as a result of inflation. Average tariffs increased by 3.3 per cent. in the year ended 31 December 2010, as compared to the same period in 2009 due in part to the effect of the planned tariff increase.

The Company's fuel requirements consist principally of the costs of diesel used by support locomotives and vehicles and other fuel used in operations. Average purchase prices for diesel fuel, on a per kilogram basis, increased approximately 28.2 per cent., in the year ended 31 December 2011, as compared to the average in 2010 and by 42.4 per cent. in the year 2010 relative to 2009, in line with global trends.

Except for the year ended 31 December 2009, when the Company's freight volumes declined due to the effects of the global recession, and except for the increase in electricity tariffs in the third quarter of 2010 (when transmission costs were increased), the Company's electricity and fuel costs have increased throughout the periods presented, generally in line with freight volume increases requiring growing consumption of electricity and also due to the increases in electricity tariffs and fuel prices.

The Company uses steel and other materials in the repair of the rail tracks, railcars and locomotives and other infrastructure. The cost of such materials has increased during the periods presented. The Company's use of these materials has increased throughout the periods presented as the Company began, during 2008, to decrease its reliance on contractors for a significant part of the repairs.

Depreciation

The Company's depreciable assets consist principally of: its rail track infrastructure, including the tracks, tunnels, bridges and stations; transport, machinery, equipment and other, consisting principally of railcars, locomotives and moveable equipment used in freight and passenger operations; and buildings and constructions, such as the Company's headquarters, other offices and some stations.

Depreciation is recognised on a straight-line basis over the estimated useful lives of each part of a depreciable asset, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Land is not depreciated. The estimated useful lives for the current and comparative periods are as follows:

- buildings and constructions: 44 years
- rail track infrastructure: 23 years
- transport, machinery, equipment and other: 12 years

During the periods presented, the Company has been carrying out operational improvements under the 2005 Restructuring Programme and, since September 2010, the Modernisation Project and, since November 2010, the Bypass Project. However, depreciation expense has continued to decrease moderately from period to period, in part due to some of the Company's asset base reaching the end of its useful life. The Company has made strategic investments that enhance the operational efficiency of its assets. These efforts have made some of its older infrastructure redundant or obsolete.

For a more detailed description of the Company's infrastructure investments and its depreciable asset base and related depreciation, see "*—Liquidity and Capital Resources—Capital expenditures*" and Note 12 of the 2011 Audited Consolidated Financial Statements and Note 11 of the 2010 Audited Consolidated Financial Statements.

Passenger tariffs and volumes

During the periods under review, the passenger transportation segment (the Passenger SBU) represented a small percentage of the Company's total revenues: 3.9 per cent., 3.7 per cent., 4.3 per cent. and 4.9 per cent. of the Company's total revenue for the three-month period ended 31 March 2012 and for the years ended 31 December 2011, 2010 and 2009, respectively.

Passenger revenues are a function of passenger tariffs, which Management measures in terms of average tariffs per thousand passenger-kilometre and the total number of passenger kilometres, for any given period. The Company's revenue per passenger kilometre was GEL 0.024 for the year ended 31 December 2011 and GEL 0.022 Lari cents for each of the years ended 31 December 2010 and 2009.

The following table sets forth information in respect of the Company's passenger tariffs for the periods indicated:

	For the year ended 31 December		
	2011	2010	2009
	(GEL per passenger kilometre)		
Average Tariffs[(1)]	0.024	0.022	0.022

(1) Average tariffs are calculated as passenger traffic revenue per passenger-kilometre.

The following table sets forth the number of passenger kilometres for the periods indicated:

	For the year ended 31 December		
	2011	2010	2009
	(passenger kilometres)		
Domestic	623.2	636.5	615.9
International	18.2	18.2	10.0
Total	**641.4**	**654.7**	**625.9**

Explanation of Key Comprehensive Income Items

Revenue

The Company's revenue comprises freight traffic, freight car rental, passenger traffic and other income. In addition, prior to the transfer of Railway Telecom to the MESD in May 2010, the Company also generated revenue from communication services offered by this subsidiary. The Company generates substantially all of its revenue through the Freight SBU.

The Freight SBU derives revenue from freight traffic and freight car rental. Freight traffic revenue comprises revenue from freight transportation services, generated by transporting customer cargoes along the Company's railway network; revenue from freight handling, derived from storage, or "demurrage", charges to customers failing to unload a rail car within 24 hours of arrival at its agreed destination; and revenue from certain other services, including railcar marshalling and freight pick-up and delivery at customer facilities. A major portion of freight car rental revenue is generated from leasing railcars to the Company's customers, including foreign railway companies using the Company's railcars on routes through their countries, and leasing locomotives to other railway companies outside Georgia, including Azerbaijan Railway.

The Passenger SBU has consistently generated more than 80.0 per cent. of its revenue from passenger traffic. The substantial majority of passenger traffic revenue derives from the transportation of passengers. To a very limited extent, passenger traffic revenue also includes revenue from the transport of unaccompanied luggage within Georgia.

Revenue from internet services consists of the revenue generated by the former subsidiary Railway Telecom, which was disposed of in May 2010, while revenue from fibre optic cables lease consists of lease payments for the rental of capacity to unrelated parties.

Other revenue, which appears in Note 7 of the 2011 Audited Consolidated Financial Statements and Note 6 of the 2010 Audited Consolidated Financial Statements, consists of revenue from the sale of scrap metal that the Company generates from ongoing maintenance and repair and rental income from real estate to third parties, including at the Central Tbilisi Station.

Other income

Other income is primarily comprised of penalties accrued on creditors and debtors, which consists of penalty payments under contracts with the Company's service providers or to parties to which the Company provides services; payments from legal claims against third parties and gains realised upon the sale of subsidiary and other investments; and charges for the maintenance of a fibre optic cable in the Company's network some of whose capacity is owned by third parties and maintained by the Company.

Employee benefits expense

Employee benefit expense is primarily comprised of salaries, bonuses and workers compensation for injury or sickness and business trip expenses.

Depreciation and amortisation expense

Depreciation is based on the cost of an asset less its residual value. Depreciation is recognised on a straight-line basis over the estimated useful lives of each major component of an item of property, plant and equipment. Depreciation methods and useful lives are reviewed at each financial year end and adjusted if appropriate.

The Company's amortisation expense is immaterial.

Electricity and materials used

Electricity and materials used is comprised of electricity, materials and fuel. Electricity costs include principally the costs of the electricity used to move the Company's locomotives and vehicles and the electricity used in the Company's buildings. Material costs comprise the costs of repairs done directly by the Company. Fuel includes the costs of diesel used by locomotives and vehicles and other fuel used in operations.

Other expenses

Other expenses are primarily comprised of taxes other than income tax, comprising property and land taxes; guarantee provisions; freight car rental; security; repairs and maintenance; write-offs of non-current assets; communication services; and inventory write-downs due to obsolescence; and other, comprising principally office expenses, consultancy expenses, membership costs from the Organisation for the Cooperation of Railways, communications, and internet and sundry other items.

Land taxes are determined by the municipalities where the land is located, while property taxes are calculated at one per cent. of the book value of an asset, but railway infrastructure assets such as tracks are exempted from this tax.

Net finance income/(cost)

Finance income comprises interest income on funds invested and foreign currency exchange gains. Finance costs comprise interest expense on borrowings, impairment losses on trade receivables, foreign currency losses and impairment losses recognised on financial assets.

Income tax expense

Income tax expense includes the tax charge for the current period measured at the amount expected to be paid to or recovered from the taxation authorities and income tax related to origination and reversal of temporary differences. The Company's applicable income tax rate is the income tax rate of 15.0 per cent. for Georgian companies.

Operating and Financial Results

Business segments

For purposes of its business operations, the Company operates the national railway system through three SBUs: the Freight SBU, which consists of freight traffic (transportation and handling) and freight car rental services; the Passenger SBU, which primarily transports passengers and luggage within Georgia; and the Infrastructure SBU, which operates, maintains and manages the Company's principal infrastructure assets. The Infrastructure SBU is a cost centre providing services only to the Freight SBU and the Passenger SBU and does not conduct business with third-party customers.

For IFRS reporting purposes, however, the Company has two reportable segments, the freight transportation segment (the Freight SBU) and the passenger transportation segment (the Passenger SBU). A reportable segment is a segment of the Company that engages in business activities from which it may earn revenues and incur expenses. The reporting segments offer different products and services, and are managed separately because they require different technologies and marketing strategies. Segment information includes items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Items that are not allocated for IFRS reporting purposes to the Freight SBU and the Passenger SBU comprise mainly railway infrastructure, corporate assets (primarily the Company's headquarters), head office expenses, financial income and expenses, tax expenses and tax assets and liabilities. Items related to infrastructure are not allocated to a reporting segment as the Company has not implemented systems for such allocations.

During the periods under review, the freight transportation segment (the Freight SBU) generated substantially all of the Company's revenue, accounting for 95.3 per cent., 93.4 per cent. and 91.4 per cent. of total revenue for the years ended 31 December 2011, 2010 and 2009, respectively, and generated GEL 289.2 million, GEL 237.4 million and GEL 155.4 million in reportable segment profit before infrastructure costs, net interest cost and income tax for the years ended 31 December 2011, 2010 and 2009, respectively.

The passenger transportation segment (the Passenger SBU) accounted for 3.7 per cent., 4.3 per cent. and 4.9 per cent. of total revenue for the years ended 31 December 2011, 2010 and 2009, respectively. During the periods under review, the passenger transportation segment incurred reportable segment loss before infrastructure costs, net interest cost and income tax of GEL 10.9 million, GEL 10.8 million and GEL 13.0 million for the years ended 31 December 2011, 2010 and 2009, respectively. The Company aims in the medium-term to transform passenger services in Georgia into a profitable business.

Substantially all of the Company's revenue is from Georgia and CIS countries and the non-current assets of the Company are located in Georgia, and its operations are therefore presented as one geographical segment. For additional information about the Company's reportable segments, see Note 6 of the 2011 Audited Consolidated Financial Statements and Note 5 of the 2010 Audited Financial Statements.

Results of Operations for the Three-Month Periods ended 31 March 2012 and 2011

The following table sets forth the Company's results of operations for the three-month periods ended 31 March 2012 and 2011 derived from the First Quarter Condensed Consolidated Financial Statements:

	For the three-month period ended 31 March		
	2012	**2011**	**Change 2012 vs. 2011**
	(GEL millions)		*(per cent.)*
Revenue	105.8	103.4	2.3
of which:			
Freight traffic[(1)]	101.1	97.6	3.6
Passenger traffic	3.7	3.2	15.6
Other	1.0	2.6	(61.5)
Other income	5.7	4.0	42.5
Employee benefits expense	(23.8)	(26.3)	(9.5)
Depreciation and amortization expense	(24.8)	(23.0)	7.8
Electricity and materials used	(12.3)	(12.7)	(3.1)
Other expenses	(14.7)	(20.5)	(28.3)
Results from operating activities	**35.9**	**24.9**	44.2
Finance income	10.4	10.9	(4.6)
Finance costs	(6.6)	(1.5)	340.0
Net finance income/(costs)	**3.9**	**9.4**	**(58.5)**
Profit before income tax	**39.7**	**34.3**	**15.7**
Income tax expenses	(6.6)	(5.7)	15.8
Profit and total comprehensive income for the period	**33.1**	**28.5**	**16.1**

(1) Includes revenue from freight car rental.

Revenue

The following table sets forth the breakdown of the Company's revenue by business line for the periods indicated:

	For the three-month period ended 31 March		
	2012	**2011**	**Change 2012 vs. 2011**
	(GEL millions)		*(per cent.)*
Freight	101.1	97.6	3.6
Of which:			
Freight traffic	*87.3*	*89.3*	*(2.2)*
Freight car rental	*13.8*	*8.4*	*64.3*
Passenger traffic	3.7	3.2	15.6
Other[(1)]	1.0	2.6	(61.5)
Total	**105.8**	**103.4**	**2.3**

(1) Includes revenue from realisation of scrap materials.

The Company's revenue was GEL 105.8 million for the three-month period ended 31 March 2012, as compared to GEL 103.4 million for the three month period ended 31 March 2011, representing an increase of 2.3 per cent. (or GEL 2.4 million).

The increase in revenue in the first three months of 2012, as compared to the corresponding period in 2011, was primarily due to an increase in freight revenue.

Freight revenue, which is comprised of revenue from freight traffic and revenue from freight car rental, was GEL 101.1 million for the three-month period ended 31 March 2012, as compared to GEL 97.6 million for the three-month period ended 31 March 2011, representing an increase of 3.6 per cent. The increase was primarily due to the increase in freight car rental revenue, which was only partially offset by the decrease in freight traffic revenue. See "*—Revenue from freight traffic*" and "*—Revenue from freight car rental*" below.

Passenger traffic revenue was GEL 3.7 million for the three-month period ended 31 March 2012, as compared to GEL 3.2 million for the three-month period ended 31 March 2011, representing an increase of 15.6per cent. (or GEL 0.5 million). See "*—Revenue from passenger traffic*" below.

Revenue from freight traffic

The Company's revenue from freight traffic was GEL 87.3 million for the three-month period ended 31 March 2012, as compared to GEL 89.3 million for the three-month period ended 31 March 2011, representing a decrease of 2.2 per cent. (or GEL 2.0 million).

The decrease of 2.2 per cent. in revenue from freight traffic in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to a decrease in liquid cargo volumes in the first three months of 2012 of 13.8 per cent., as compared to the first three months of 2011, as sustained demand in transportation services for crude oil and oil products was offset by a lack of availability of rolling stock to the Company, as well as adverse weather conditions, particularly in the first two months of 2012, creating bottlenecks in ports and other infrastructure and thereby reducing cargo turnover and transportation performance. The decrease in liquid cargo volumes was partially offset by the reduction, with effect from 1 April 2011, in the discount the Company offers on its tariffs for the transportation of oil and oil products, as well as the reduction, with effect from 1 February 2012, of the volume-based discount offered by the Company for the transportation of oil and oil products. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Freight Tariffs*"

Revenue from freight car rental

The Company's revenue from freight car rental was GEL 13.8 million for the three-month period ended 31 March 2012, as compared to GEL 8.4 million for the three-month period ended 31 March 2011, representing an increase of 64.3 per cent. (or GEL 5.4 million).

The increase of 64.3 per cent. in revenue from freight car rental in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011 was primarily due to the increased usage of company's own railcars by other railways, including, in particular, pursuant to an agreement for the rental of 200 dry cargo railcars to Ukrainian Railways from 1 May 2011 onwards.

Revenue from passenger traffic

The increase of 15.6 per cent. in revenue from passenger traffic operations in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to overall growth in the Georgian economy, as well as severe weather conditions in the first months of 2012 that resulted in difficulties for road transportation and, in turn, increased demand for rail transportation.

Other Revenue

The Company's other revenue was GEL 1.0 million for the three-month period ended 31 March 2012, as compared to GEL 2.6 million for the three-month period ended 31 March 2011, representing a decrease of 61.5 per cent. (or GEL 1.6 million). The decrease of 61.5 per cent. in other revenue in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to lower volumes of scrap realised.

Other income

The Company's other income was GEL 5.7 million for the three-month period ended 31 March 2012, as compared to GEL 4.0 million for the three-month period ended 31 March 2011, representing an increase of 42.5 per cent. (or GEL 1.7 million). The increase of 42.5 per cent. in other income in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to an increase in revenue from accrued penalties on creditors and non-operating income.

Employee benefits expense

The Company's employee benefit expense was GEL 23.8 million for the three-month period ended 31 March 2012, as compared to GEL 26.3 million for the three-month period ended 31 March 2011, representing a decrease of 9.5 per cent. (or GEL 2.5 million). The decrease of 9.5 per cent. in employee benefits expense in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to the decrease in the number of employees during 2011.

Depreciation and amortisation expense

The Company's depreciation and amortisation expense was GEL 24.8 million for the three-month period ended 31 March 2012, as compared to GEL 23.0 million for the three-month period ended 31 March 2011, representing an increase of 7.8 per cent. (or GEL 1.8 million). The increase of 7.8 per cent. in depreciation and amortisation expense in employee benefits expense in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was primarily due to increases in the amount of rolling stock owned by the Company in the three-month period ended 31 March 2012, as compared to the three month period ended 31 March 2011.

Electricity and materials used

The following table sets forth the breakdown of the Company's costs for electricity, materials and fuel used for the periods indicated:

	For the three-month period ended 31 March		
	2012	**2011**	**Change 2012 vs. 2011**
	(GEL millions)		*(per cent.)*
Electricity	6.1	8.5	(28.2)
Materials	4.0	1.8	122.2
Fuel	2.3	2.4	(4.2)
Total	**12.3**	**12.7**	**(3.1)**

The Company's costs for electricity, materials and fuel were GEL 12.3 million for the three-month period ended 31 March 2012, as compared to GEL 12.7 million for the three-month period ended 31 March 2011, representing a decrease of 3.1 per cent. (or GEL 0.4 million). The decrease in costs for electricity, materials and fuel used in the three-month period ended 31 March 2012, as compared to the corresponding period in 2011, was principally due to the Company entering into an agreement for purchase of electricity for a fixed price with EnergoPro Georgia in September 2011, resulting in a decrease in the price of electricity in the first quarter of 2012, as compared to the first quarter of 2011. See "*Description of the Company's Business—Electricity Supply*". This was only partially offset by the increase in costs for materials of 122.2 per cent. (or GEL 2.2 million) over the same period as a result of increased internal repairs.

Other expenses

The following table sets forth the breakdown of the Company's other expenses for the periods indicated:

	For the three-month period ended 31 March		
	2012	**2011**	**Change 2012 vs. 2011**
	(GEL millions)		*(per cent.)*
Freight car rental	5.0	5.6	(10.7)
Taxes other than income tax	5.0	4.2	19.0
Security	1.8	1.9	(5.3)
Repairs and maintenance	1.6	3.7	(56.8)
Write-off of non-current assets	—	4.1	(100.0)
Other	1.2	1.0	20.0
Total	**14.7**	**20.5**	**(28.3)**

The Company's other expenses were GEL 14.7 million for the three-month period ended 31 March 2012, as compared to GEL 20.5 million for the three-month period ended 31 March 2011, representing a decrease of 28.3 per cent. (or GEL 5.8 million). The decrease was mainly caused by the Company identifying impairment indicators leading to a write-off of several items of the Company's construction in progress, whereas no such indicators were identified during the three-month period ended 31 March 2012 and a decrease in repairs and maintenance as the Company performed a greater portion of repairs itself rather than outsourcing these repairs to third parties that charge fees.

Results from operating activities

The Company's results from operating activities were GEL 35.9 million for the three-month period ended 31 March 2012, as compared to GEL 24.9 million for the three-month period ended 31 March 2011, representing an increase of 44.2 per cent. (or GEL 11.0 million), due to the reasons described above. The Company's margin on its results from operating activities was 33.9 per cent. for the three-month period ended 31 March 2012, as compared to 24.1 per cent. for the corresponding period in 2011.

Net finance income/(costs)

The Company recorded net finance income for the three-month period ended 31 March 2012 of GEL 3.9 million and GEL 9.4 million for the corresponding period in 2011.

Finance income for the three-month period ended 31 March 2012 was principally due to foreign exchange gain of GEL 6.4 million and interest income of GEL 4.0 million. See Note 9 to the First Quarter Condensed Consolidated Financial Statements. Finance income during such period was partially offset by provisions of GEL 6.5 million made on doubtful debts.

Profit before income tax

The Company's profit before income tax was GEL 39.7 million in the three-month period ended 31 March 2012, as compared to GEL 34.3 million in the three-month period ended 31 March 2011, representing an increase of 15.7 per cent. (or GEL 5.4 million), due to the reasons stated above.

Income tax expense

The Company's income tax is recognised based on management's best estimate of the weighted average annual income tax rate expected for the full financial year applied to the pre-tax income of the interim periods. The Company's income tax expense was GEL 6.6 million for the three-month period ended 31 March 2012, as compared to GEL 5.7 million for the three-month period ended 31 March 2011, representing an increase of 15.8 per cent. (or GEL 0.9 million). The increase in income tax expense for the three-month period ended 31 March 2012, as compared to the corresponding period in 2011 was principally due to increased profit. The Company's consolidated effective tax rate (calculated as income tax expense divided by profit before income tax) for the three-month period ended 31 March 2012 was 17 percent (three-month period ended 31 March 2011: 17 percent).

The Company's deferred tax benefit for the three-month period ended 31 March 2012 was GEL 1.4 million, as compared to a deferred tax expense of GEL 0.0 million for the three-month period ended 31 March 2011.

Profit and total comprehensive income for the year

The Company's profit and total comprehensive income for the three-month period ended 31 March 2012 was GEL 33.1 million, as compared to GEL 28.5 million for the three-month period ended 31 March 2011, representing an increase of 16.1 per cent. (or GEL 4.6 million), due to the reasons described above.

Results of Operations for the Years ended 31 December 2011, 2010 and 2009

The following table sets forth the Company's results of operations for the years ended 31 December 2011, 2010 and 2009 derived from the Audited Consolidated Financial Statements unless otherwise indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(GEL millions)		*(per cent.)*	*(GEL millions)*	*(per cent.)*
Revenue	477.4	404.7	18.0	318.8	26.9
of which:					
Freight traffic[(1)]	*454.9*	*377.9*	*20.4*	*290.7*	*30.0*
Passenger traffic	*15.3*	*14.7*	*4.1*	*14.0*	*5.0*
Other[(2)]	*7.2*	*12.1*	*(40.5)*	*14.2*	*(14.8)*
Other income	12.0	17.8	(32.6)	10.7	66.4
Employee benefits expense	(108.5)	(111.3)	(2.5)	(106.1)	4.9
Depreciation and amortization expense	(92.1)	(98.7)	(6.7)	(96.1)	2.7
Electricity and materials used	(47.8)	(44.6)	7.2	(40.3)	10.7
Other expenses	(73.2)	(71.8)	1.9	(64.1)	12.0
Results from operating activities	**167.8**	**96.1**	**74.6**	**22.8**	**321.5**
Finance income	27.0	45.4	(40.5)	0.6	7,466.7
Finance costs	(10.5)	(17.7)	(40.7)	(4.8)	268.8
Net finance income/(costs)	**16.5**	**27.7**	**(40.4)**	**(4.2)**	**759.5**
Profit before income tax	**184.3**	**123.8**	**48.9**	**18.7**	**562.0**
Income tax expenses	(9.9)	(22.3)	(55.6)	(2.9)	669.0
Profit and total comprehensive income for the year	**174.4**	**101.5**	**71.8**	**15.8**	**542.4**

(1) Includes revenue from freight car rental.

(2) Includes communication services, which consists principally of revenue generated by the former subsidiary Railway Telecom, which was disposed of in May 2010, revenue from lease payments for the rental of fibre optic cable capacity and internet services to unrelated parties, and, in 2010, revenue from the sale of scrap metal that the Company generates from ongoing maintenance and repair and rental income from real estate to third parties, including at the Central Tbilisi Station.

Revenue

The following table sets forth the breakdown of the Company's revenue by business line for the years indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(GEL millions)		*(per cent.)*	*(GEL millions)*	*(per cent.)*
Freight	454.9	377.9	20.4	290.7	30.0
of which:					
Freight traffic	*410.9*	*354.6*	*15.9*	*274.2*	*29.3*
Freight car rental	*44.0*	*23.3*	*88.8*	*16.5*	*41.2*
Passenger traffic	15.3	14.7	4.1	14.0	5.0
Other[(1)]	7.2	12.1	(40.5)	14.2	(14.8)
Total	**477.4**	**404.7**	**18.0**	**318.8**	**26.9**

(1) Includes communication services, which consists principally of revenue generated by the former subsidiary Railway Telecom, which was disposed of in May 2010, revenue from lease payments for the rental of fibre optic cable capacity and internet services to unrelated parties, and, in 2010, revenue from the sale of scrap metal that the Company generates from ongoing maintenance and repair and income from the rental of real estate to third parties, including at the Central Tbilisi Station.

The Company's revenue was GEL 477.4 million for the year ended 31 December 2011, as compared to GEL 404.7 million and GEL 318.8 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 18 per cent. (or GEL 72.7 million) in 2011, as compared to 2010, and an increase of 26.9 per cent. (or GEL 85.9 million) in 2010, as compared to 2009.

The increase in revenue in 2011 was primarily due to the increase in revenue in both freight traffic and freight car rental services, primarily as a result of the appreciation of the Swiss Franc relative to the Lari, as well as the termination of a former arrangement whereby Azerbaijan Railway and the Company were not required to pay each other for the first eight days of use of each other's railcars. The increase in revenue in 2010 was principally due to the increase in revenue from freight traffic, as well as increases in freight car rental and other sources.

Freight revenue, which is comprised of revenue from freight traffic and revenue from freight car rental, was GEL 454.9 million for the year ended 31 December 2011, as compared to GEL 377.9 million and GEL 290.7 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 20.4 per cent. (or GEL 77.0 million) in 2011, as compared to 2010, and an increase of 30.0 per cent. (or GEL 87.2 million) in 2010, as compared to 2009. See "*—Revenue from freight traffic*" and "*—Revenue from freight car rental*" below.

Passenger traffic revenue was GEL 15.3 million for the year ended 31 December 2011, as compared to GEL 14.7 million and GEL 14.0 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 4.1 per cent. (or GEL 0.6 million) in 2011, as compared to 2010, and an increase of 5.0 per cent. (or GEL 0.7 million) in 2010, as compared to 2009. See "*—Revenue from passenger traffic*" below.

Revenue from freight traffic

The Company's revenue from freight traffic was GEL 410.9 million for the year ended 31 December 2011, as compared to GEL 354.6 million and GEL 274.2 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 15.9 per cent. (or GEL 56.3 million) in 2011, as compared to 2010, and an increase of 29.3 per cent. (or GEL 80.4 million) in 2010, as compared to 2009.

The increase of 15.9 per cent. in revenue from freight traffic in the year ended 31 December 2011 was primarily due to the appreciation by 15.2 per cent., on an average monthly basis for the period, of the Swiss Franc relative to the Lari and due to an increase in dry cargo volumes of 1.2 million tonnes, or 198.4 million tonne-kilometres, as a result of increased demand for ores, construction materials and metals, which generate more revenue per tonne compared to liquid cargoes. This increase in dry cargo volumes was partially offset by a decrease of 1.0 million tonnes, or 402.5 million tonnes per kilometre in liquid cargo volumes, mainly as result of the strategic decision in the third quarter of 2010 to reallocate some of the oil tank car fleet previously used for the transport of liquid cargo from the Azerbaijan westbound route to the transport of cargoes to Afghanistan. In addition, the increase in average tariffs for liquid cargoes also contributed to the increase in revenue from freight traffic despite the decrease in volumes of liquid cargoes. These average tariff increases were: for crude oil, to CHF 18.03 per 1,000 tonne-kilometres in the year ended 31 December 2011 from CHF 14.24 per 1,000 tonne-kilometres in the year ended 31 December 2010; and for oil products, to CHF 34.19 per 1,000 tonne-kilometres in the year ended 31 December 2011 from CHF 32.13 per 1,000 tonne-kilometres in the year ended 31 December 2010. Dry cargo tariffs remained unchanged in 2010, although the average dry cargo tariffs decreased to CHF 39.28 per 1,000 tonne-kilometres in 2011 from CHF 40.8 per 1,000 tonne-kilometres in 2010 as a result in the change in product mix of dry cargo volumes transported in 2011, as compared to 2010.

The increase of 29.3 per cent. in revenue from freight traffic in the year ended 31 December 2010 was primarily due to the increase in freight transportation volumes of 2.8 million tonnes, or 807.4 million tonne-kilometres, of which 1.7 million tonnes, or 542.9 million tonne-kilometres, was an increase in liquid cargoes, both oil and oil products, and 1.1 million tonnes, or 265.4 million tonne-kilometres, was an increase in dry cargoes, across most dry cargo types. The increase in freight transportation volumes was primarily due to recovery from the economic downturn caused by global financial crisis. The appreciation of the Swiss Franc relative to the Lari and the increases in the tariffs for crude oil (to CHF 14.24 per 1,000 tonne-kilometre from CHF 13.93 per 1,000 tonne-kilometre) and for oil products (to CHF 32.13 per 1,000 tonne-kilometre from CHF 31.88 per 1,000 tonne-kilometre) contributed to the increase, while the decrease in tariff for dry cargo had a partially offsetting effect (to CHF 40.8 per 1,000 tonne-kilometre from 42.331 per 1,000 tonne-kilometre), in each case in 2010, as compared to 2009.

Revenue from freight car rental

The Company's revenue from freight car rental was GEL 44.0 million for the year ended 31 December 2011, as compared to GEL 23.3 million and GEL 16.5 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 88.8 per cent. (or GEL 20.7 million) in 2011, as compared to 2010, and an increase of 41.2 per cent. (or GEL 6.8 million) in 2010, as compared to 2009.

The increase in revenue from freight car rental operations in the year ended 31 December 2011 relative to the same period in 2010 was due to the appreciation, on an average daily basis, in 2011 relative to 2010, by 15.2 per cent. of the Swiss Franc relative to the Lari and to the termination of a former arrangement whereby Azerbaijan Railway and the Company were not required to pay each other for the first eight days of use of each other's railcars.

The increase in revenue from freight car rental operations in the year ended 31 December 2010 relative to the same period in 2009 was due to the increase in freight traffic supported by the increased number of railcars of the Company as a result of significant investments in rolling stock made in 2010 and 2009; the year-on-year appreciation of the Swiss Franc relative to the Lari; and improved management of rail car movement planning as a result of the Modernisation Project.

Revenue from passenger traffic

The Company's revenue from passenger traffic was GEL 15.3 million for the year ended 31 December 2011, as compared to GEL 14.7 million and GEL 14.0 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 4.1 per cent. (or GEL 0.6 million) in 2011, as compared to 2010, and an increase of 5.0 per cent. (or GEL 0.7 million) in 2010, as compared to 2009.

The 4.1 per cent. increase in revenue from passenger traffic operations in the year ended 31 December 2011, as compared to the year ended 31 December 2010, was mainly due to an increase in average revenue per passenger-km of 5.9 per cent. This increased revenue reflected the greater number of passengers travelling on the more expensive railcars commissioned in the second and third quarters of 2010.

The 5.0 per cent. increase in revenue from passenger traffic operations in the year ended 31 December 2010, as compared to the year ended 31 December 2009, was mainly due to an increase of 3.8 per cent. in the number of passengers and an increase in the average annual revenue per passenger of 1.4 per cent. caused by the growth in the number of passengers travelling on more expensive railcars compared to 2009 and a greater overall weight in the passenger volume mix of international passengers, which provide more than three times the revenue per passenger than local traffic passengers.

Other revenue

The Company's other revenue was GEL 7.2 million for the year ended 31 December 2011, as compared to GEL 12.1 million and GEL 14.2 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 40.5 per cent. (or GEL 4.9 million) in 2011, as compared to 2010, and decrease of 14.8 per cent. (or GEL 2.1 million) in 2010, as compared to 2009.

In particular, revenue from communication services was generated until May 2010 from the Company's previous 100 per cent.-owned subsidiary Railway Telecom, which was transferred to the State in that month, and the Company did not have any revenue from communication services operations in the year ended 31 December 2011. The Company's revenue from communication services was GEL 4.4 million for the year ended 31 December 2010, as compared to GEL 10.5 million for the year ended 31 December 2009, representing a decrease of 100.0 per cent. (or GEL 4.4 million) in 2011, as compared to 2010, and a decrease of 58.1 per cent. (or GEL 6.1 million) in 2010, as compared to 2009. As stated above, the decrease in 2011 and 2010 relative to 2009 is due to the effect of the disposal in May 2010 of the subsidiary generating this income.

Other revenue from sources other than communication services in the year ended 31 December 2011 was primarily represented by scrap metal sales, as well as a mix of rental income and repair services. The decrease in this other revenue in the year ended 31 December 2010 relative to the same period in 2009 was mainly due to a decrease in sales of scrap metals accumulated as a result of ongoing maintenance and repair.

Other income

The Company's other income was GEL 12.0 million for the year ended 31 December 2011, as compared to GEL 17.8 million and GEL 10.7 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 32.6 per cent. (or GEL 5.8 million) in 2011, as compared to 2010, and an increase of 66.4 per cent. (or GEL 7.1 million) in 2010, as compared to 2009. The decrease in other income in the year ended 31 December 2011 relative to the same period in 2010 and the increase in other income in the year ended 31 December 2010 relative to the same period in 2009 were each principally due to the one-time gain of GEL 4.3 million on the sale of the 25 per cent. stake in Chitakhevi in 2010.

Employee benefits expense

The Company's employee benefit expense was GEL 108.5 million for the year ended 31 December 2011, as compared to GEL 111.3 million and GEL 106.1 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 2.5 per cent. (or GEL 2.8 million) in 2011, as compared to 2010, and an increase of 4.9 per cent. (or GEL 5.2 million) in 2010, as compared to 2009. The decrease in the employee benefits expense in 2011 relative to the same period in 2010 was principally due to a decrease in the number of personnel as the consequence of the Company's ongoing efficiency initiatives, partially offset by an increase in average wages.

The increases in the employee benefits expense in 2011 and 2010, as compared to 2009 was principally due to the Company's introduction of an economic value added bonus compensation scheme in 2009 (the "**New Bonus Scheme**"), pursuant to which the Company evaluates employee performance on an annual basis and determines an appropriate level of bonus based on the financial results of the Company and the overall operational performance. The New Bonus Scheme does not set specific bonus levels to targets, but evaluates a number of factors on an annual basis. The year 2010 was the first time that a bonus payment was paid under the New Bonus Scheme. In 2011 and 2010, the Company recognised GEL 7.8 million and GEL 8.2 million, respectively, of employee benefits expenses in relation to performance bonuses paid to all employees in good standing.

Excluding these bonuses, employees benefit expense decreased in 2010, as compared to 2009, by GEL 3.0 million principally due to a decrease in the number of employees of the Company in connection with the Company's on-going efficiency initiatives.

Depreciation and amortisation expense

The Company's depreciation and amortisation expense was GEL 92.1 million for the year ended 31 December 2011, as compared to GEL 98.7 million and GEL 96.1 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 6.7 per cent. (or GEL 6.6 million) in 2011, as compared to 2010, and an increase of 2.7 per cent. (or GEL 2.6 million) in 2010, as compared to 2009. In each of the three years, depreciation and amortisation principally related to the depreciation of transport, machinery, equipment, rail track infrastructure and other (primarily buildings). Depreciation and amortisation relating to assets attributable to both freight assets and passenger assets has, for the historical periods discussed herein, continued to experience moderate decreases year-on-year, primarily as a result of some of the Company's assets reaching the end of their useful lives. The effect of these decreases in depreciation and amortisation in both freight assets and passenger assets was more than offset in the year ended 31 December 2010 by the increase in depreciation and amortisation of infrastructure assets, since in 2009 and 2010 the greater part of capital expenditures was made in railway infrastructure assets pursuant to the Modernisation Project, resulting in an overall increase of GEL 2.6 million in 2010, as compared to 2009.

Depreciation and amortisation related to freight assets was GEL 38.0 million for the year ended 31 December 2011, as compared to GEL 39.5 million and GEL 40.0 million for the years ended 31 December 2010 and 2009, respectively, representing an decrease of 3.8 per cent. (or GEL 1.5 million) in 2011, as compared to 2010, and a decrease of 1.3 per cent. (or GEL 0.5 million) in 2010, as compared to 2009. In each of the three years, depreciation and amortisation related to freight assets principally comprised the depreciation of railcars and locomotives.

Depreciation and amortisation related to passenger assets was GEL 6.7 million for the year ended 31 December 2011, as compared to GEL 7.8 million and GEL 8.4 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 14.1 per cent. (or GEL 1.1 million) in 2011, as compared to 2010, and a decrease of 7.1 per cent. (or GEL 0.6 million) in 2010, as compared to 2009.

Depreciation and amortisation related to infrastructure assets (including headquarters) was GEL 45.4 million for the year ended 31 December 2011, as compared to GEL 51.1 million and GEL 47.0 million for the years ended 31 December 2010 and 2009, respectively, representing a decrease of 11.2 per cent. (or GEL 5.7 million) in 2011, as compared to 2010, and an increase of 8.7 per cent. (or GEL 4.1 million) in 2010, as compared to 2009. The decrease in depreciation in 2011, as compared to 2010, was due to the transfers of assets to certain third parties, primarily the transfer of railway assets, such as rails, stations and other infrastructure, to Marabda-Kartsakhi Railway LLC, and the transfer of assets, including transformers and certain buildings, to JSC EnergoPro Georgia. The increase in depreciation in 2010, as compared to 2009 was primarily due to an increase in capital expenditures in infrastructure assets under the Modernisation Project. See "*Current Trading and Prospects; Trends; — Disposals and write-offs of certain assets*".

Electricity and materials used

The following table sets forth the breakdown of the Company's costs for electricity and materials used for the years indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(GEL millions)		*(per cent.)*	*(GEL millions)*	*(per cent.)*
Electricity	24.2	21.4	13.1	19.3	10.9
Materials	13.8	13.6	1.5	13.3	2.3
Fuel	9.7	9.7	0.0	7.7	26.0
Total	**47.8**	**44.6**	**7.2**	**40.3**	**10.7**

The Company's costs for electricity and materials used (which consist of electricity, materials and fuel) were GEL 47.8 million for the year ended 31 December 2011, as compared to GEL 44.6 million and GEL 40.3 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 7.2 per cent. (or GEL 3.2 million) in 2011, as compared to 2010, and an increase of 10.7 per cent. (or GEL 4.3 million) in 2010, as compared to 2009. The increase in costs from electricity and materials used in 2011, as compared to 2010, was principally due to an increase by 14.8 per cent. in average electricity tariffs during 2011, as compared to 2010. The increase in costs from electricity and materials used in 2010, as compared to 2009, was principally due to the 10.9 per cent. (or GEL 2.1 million) and 26.0 per cent. (or GEL 2.0 million) increases in costs from electricity and fuel used, respectively. The increase was principally due to increased consumption of electricity as a result of increased traffic and an increase in average electricity tariffs of 3.3 per cent. and to an increase in average fuel costs of approximately 30.5 per cent., respectively, in each case, in 2010 relative to 2009.

Other expenses

The following table sets forth the breakdown of the Company's other expenses for the years indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(GEL millions)		*(per cent.)*	*(GEL millions)*	*(per cent.)*
Freight car rental	23.4	9.0	160.0	6.4	40.6
Taxes other than income tax	17.7	16.3	8.6	16.6	(1.8)
Repairs and maintenance	11.1	5.0	122.0	9.2	(45.7)
Security	7.4	7.7	(3.9)	6.5	18.5
Write-off of non-current assets	4.1	4.8	(14.6)	6.6	(27.3)
Guarantee provisions(1)	—	15.5	(100.0)	—	100.0
Communication services	—	3.6	(100.0)	7.1	(49.3)
Inventory write-downs due to obsolescence	—	—	0	2.7	(100.0)
Other	9.6	9.9	(3.0)	9.0	10.0
Total	**73.2**	**71.8**	**1.9**	**64.1**	**12.0**

(1) The Company provided the guarantee for the benefit of a film production company, which had borrowed GEL 15.3 million to finance a film shot in Georgia. The Company was given production credit for the film and, accordingly, regarded this guarantee as a promotion and marketing expense. The Company recognised the provision because there were indications that the production company would not be able to discharge its obligations.

The Company's other expenses were GEL 73.2 million for the year ended 31 December 2011, as compared to GEL 71.8 million and GEL 64.1 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 1.9 per cent. (or GEL 1.4 million) in 2011, as compared to 2010, and an increase of 12.0 per cent. (or GEL 7.7 million) in 2010, as compared to 2009.

The increase in other expenses in 2011 relative to 2010 was primarily due to an increase in freight car rental expense. This increase resulted from the termination of the arrangement between Azerbaijan Railway and the Company under which each was able to use the other's railcars without payment for up to eight consecutive days. An additional factor contributing to the increase was the increase in repair and maintenance costs, due mostly to the appreciation of the Swiss Franc relative to the Lari. These effects were partially offset by the absence in 2011 of the guarantee provisions made in 2010 for the benefit of a film production company to finance a film shot in Georgia and of the communication expense incurred in 2010 in relation to Railway Telecom, which was disposed of in May 2010.

The increase in other expenses in 2010 relative to 2009 was primarily due to the recognition of a provision for a guarantee of indebtedness. The Company provided the guarantee for the benefit of a film production company, which had borrowed GEL 15.3 million to finance a film shot in Georgia. The Company was given production credit for the film and, accordingly, regarded this guarantee as a promotion and marketing expense. The Company recognised the provision because it was considered probable that the production company would not be able to discharge its obligations. The increase also reflected a GEL 2.6 million increase in freight car rental, principally as a result of increased traffic due to the ongoing recovery in the TRACECA region from the global financial crisis and the appreciation of the Swiss Franc against the Lari, and an increase of GEL 1.2 million in security costs, mainly resulting from an increase in the fees charged by the supplier. This increase was partially offset by a decrease of GEL 4.2 million in repairs and maintenance, principally resulting from the ongoing efforts of the Company to perform its own repairs and rely less on outsourcing, a decrease of GEL 3.5 million of communication services expenses as a result of the disposal in May 2010 of the Company's previously 100.0 per cent.-owned subsidiary, Railway Telecom and a decrease of GEL 1.8 million in write-offs of non-current assets relating to construction in progress that management decided to cancel. In addition, in 2010, the Company did not have any inventory write-downs due to obsolescence as a consequence of the Company's improved inventory management, while, in 2009, the Company had GEL 2.7 million in inventory write-downs due to obsolescence.

Results from operating activities

The Company's results from operating activities were GEL 167.8 million for the year ended 31 December 2011, as compared to GEL 96.1 million and GEL 22.8 million for the years ended 31 December 2010 and 2009, respectively, representing an increase of 74.6 per cent. (or GEL 71.7 million) in 2011, as compared to 2010, and an increase of 321.5 per cent. (or GEL 73.3 million) in 2010, as compared to 2009, in each case due to the reasons described above. The Company's margin on its results from operating activities was 35.1 per cent. for the year ended 31 December 2011, as compared to 23.7 per cent. and 7.2 per cent. for the years ended 31 December 2010 and 2009, respectively.

Net finance income/(cost)

The Company recorded net finance income in 2011 and 2010 and net finance cost in 2009. The Company's net finance income was GEL 16.5 million for the year ended 31 December 2011, as compared to GEL 27.7 million in the year ended 31 December 2010, while the net finance cost in the year ended 31 December 2009 was GEL 4.2 million.

Net finance income in 2011 was mainly due to a net foreign exchange gain of GEL 16.1 million, reflecting both the appreciation of the Swiss Franc and the depreciation of the U.S. Dollar relative to the Lari, which resulted in a decrease of U.S. Dollar-denominated liabilities (principally, represented by the 2010 Notes), as well as interest income of GEL 10.9 million interest income on the Company's bank deposits. These gains were partially offset by an impairment loss on trade receivables of GEL 7.4 million, reflecting provisions for receivables that were overdue, as well as prepaid finance costs of GEL 3.0 million that were written off in connection with the cancellation by the Company of the loan entered with the European Bank for Reconstruction and Development ("**EBRD**") on March 17, 2010, in order to partly finance the Bypass Project (the "**2010 EBRD Loan**"). See "*Operating and Financial Results—Borrowings—Other Credit Facilities*". The impairment loss on trade receivables primarily related to receivables from Azerbaijan Railway, which had been provisioned due to the expectation of late payment, rather than based on an expectation of non-payment.

Net finance income in 2010 was mainly due to a net foreign exchange gain of GEL 42.2 million resulting from gains realised from August 2010, when the proceeds of the Company's 2010 Notes were exchanged into Swiss Francs, to 31 December 2010, due to the appreciation of the Swiss Franc relative to the Lari and the depreciation of the U.S. Dollar relative to the Lari during the period. This gain was partially offset by interest expense of GEL 11.6 million on the GEL 25.0 million of notes issued by the Company in December 2009 (the "**2009 Lari Notes**"), until their repayment in August 2010, and on the 2010 Notes from August 2010 to September 2010, when the Company began to capitalise interest on the 2010 Notes, and an impairment loss on trade receivables of GEL 6.1 million, reflecting provisions for receivables that were overdue.

Because the proceeds of the 2010 Notes have been used or reserved for capital expenditures, the Company has capitalised interest accrued on the principal of the 2010 Notes since it began to implement the Modernisation Project and the Bypass Project in September and November 2010, respectively.

Profit before income tax

The Company's profit before income tax was GEL 184.3 million in the year ended 31 December 2011, as compared to GEL 123.8 million and GEL 18.7 million in the years ended 31 December 2010 and 2009, respectively, representing an increase of 48.9 per cent. (or GEL 60.5 million) in 2011, as compared to 2010, and an increase of 562.0 per cent. (or GEL 105.1 million) in 2010, as compared to 2009, in each case, due to the reasons stated above.

Income tax expense

The Company's income tax expense was GEL 9.9 million in the year ended 31 December 2011, as compared to GEL 22.3 million and GEL 2.9 million in the years ended 31 December 2010 and 2009, respectively, representing a decrease of 55.6 per cent. (or GEL 12.4 million) in 2011, as compared to 2010, and an increase of 669.0 per cent. (or GEL 19.4 million) in 2010, as compared to 2009. The decrease in income tax expense in the year ended 31 December 2011 arose from the reversal of a tax liability in the amount of GEL 13.0 million as a result of a favourable court ruling. Following the resolution of a tax dispute, the Revenue Service under the Ministry of Finance of Georgia (the "**Revenue Service**") has returned approximately GEL 13 million to the Company. The Revenue Service effected this return by recording an equivalent surplus on the Company's taxpayer card. The Company will set this surplus off against future taxes it would otherwise owe until the amount has been reduced in full. See "*Description of the Company's Business—Legal Proceedings*".

The increase in income tax expense in the year ended 31 December 2010 was due to an increase in profit, partially offset by an increase in the Company's effective tax rate to 18.0 per cent. in the year ended 31 December 2010 from 15.0 per cent. in the year ended 31 December 2009, as discussed below. The Company's statutory income tax rate is, and has been for all periods under review, 15.0 per cent. The Company's consolidated effective tax rate for the year ended 31 December 2011 was 5.4 per cent. and 18.0 per cent. for the year ended 31 December 2010. See "*Description of the Company's Business—Legal Proceedings*". The greater effective tax rate in 2010 relative to the statutory rate is due to certain expenses of GEL 3.7 million that are deductible under IFRS but not under the Tax Code.

The Company's deferred tax expense for each of the years ended 31 December 2011, 2010 and 2009 was GEL 5.6 million, GEL 8.3 million and GEL 7.0 million, respectively.

Profit and total comprehensive income for the year

The Company's profit and total comprehensive income for the year was GEL 174.4 million in the year ended 31 December 2011, as compared to GEL 101.5 million and GEL 15.8 million in the years ended 31 December 2010 and 2009, respectively, representing an increase of 71.8 per cent. (or GEL 72.9 million) in 2011, as compared to 2010, and an increase of 542.4 per cent. (or GEL 85.7 million) in 2010, as compared to 2009, in each case due to the reasons described above.

Liquidity and Capital Resources

The Company's liquidity needs arise principally from the need to finance its working capital and to fund the Modernisation Project and (subject to the reimbursement provisions of the Bypass Project Memorandum) the Bypass Project. The Company's principal sources of liquidity have, for the periods discussed herein, consisted of:

- cash generated from operations representing principally payments from freight customers and passengers;
- in the year ended 31 December 2010, the proceeds from the 2010 Notes; and
- interest earned on term deposits.

Management expects that, for at least the next three years, it will fund its working capital and the costs of the Modernisation Project from existing cash, which includes the proceeds of the 2010 Notes, and cash from operations. Management expects to fund the costs of up to CHF 138.0 million relating to the Bypass Project out of amounts to be reimbursed to the Company pursuant to the Bypass Project Memorandum and, to the extent such costs are in excess of such reimbursement, out of existing cash and cash from operations. As at 31 December 2011, the Company had cash and cash equivalents of GEL 64.5 million and bank deposits of GEL 76.4 million. See "*—Borrowing—Other credit facilities*" and "*Description of the Company's Business—Bypass Project*".

Management's policy is to maintain a conservative and prudent approach to leverage and expects leverage will continue to be an important part of its capital structure. Management's current target for the long-term is to maintain a capital structure that comprises a Net debt to EBITDA ratio of no more than 2.5:1 and a Debt to Equity ratio of approximately no more than 4:1. However, Management may from time to time revise this policy and targets depending on investment opportunities as they arise. Restrictions on existing and new credit facilities may also be more restrictive than these target ratios.

Cash flows

The Company's cash flow management policies focus on maintaining a flexible capital expenditure programme and maximising cash flow generation, in line with potential future changes in passenger numbers and freight volumes transported. Through these policies, management aims to permit both the maintenance of infrastructure and the pursuit of selective growth opportunities. Management seeks to rely on operating cash flows to finance capital expenditures, but also seeks to maintain a diversified funding structure for strategic initiatives.

The following table sets forth a summary of the Company's cash flows for the periods indicated:

	For the three-month period ended 31 March	
	2012	**2011**
	(GEL millions)	
Net cash from operating activities	50.7	49.1
Net cash used in investing activities	(55.7)	(91.7)
Net cash used in financing activities	(20.5)	(22.3)
Net decrease in cash and cash equivalents	(25.5)	(64.9)
Cash and cash equivalents at 1 January	61.6	323.9
Effect of exchange rate fluctuations on cash and cash equivalents	3.0	(6.7)
Cash and cash equivalents at 31 March	39.0	252.3

Net cash from operating activities

The Company's net cash from operating activities was GEL 50.7 million for the three-month period ended 31 March 2012, as compared to GEL 49.1 million for the three-month period ended 31 March 2011, representing an increase of 3.3 per cent. (or GEL 1.6 million). This increase was principally due to a decrease in income tax paid and an increase in cash paid to suppliers by 6.1 per cent, which was partially offset by the decrease in cash receipts from customers by 9.5 per cent.

In April and May 2012, the Company received GEL 13 million and GEL 10 million, respectively, from the Government by way of a reimbursement of VAT surplus accumulated by the Company in respect of capital projects undertaken in 2011. Given the level of the accumulated surplus, the tax authorities agreed to return these funds to the Company at its request rather than to continue to hold the monies as an offset against future VAT obligations.

Net cash used in investing activities

The Company's net cash used in investing activities was GEL 55.7 million for the three-month period ended 31 March 2012, as compared to GEL 91.7 million for the three-month period ended 31 March 2011, representing a decrease of 39.3 per cent. (or GEL 36.0 million). This decrease was principally due to a decrease in additions to property, plant and equipment and an increase in interest received, which was partially offset by an increase in term deposits.

Net cash used in financing activities

The Company's net cash used in financing activities was GEL 20.5 million for the three-month period ended 31 March 2012, as compared to GEL 22.3 for the three-month period ended 31 March 2011, principally representing interest paid on the 2010 Notes.

The following table sets forth a summary of the Company's cash flows for the periods indicated:

	For the year ended 31 December		
	2011	2010	2009
		(GEL millions)	
Net cash from operating activities	225.9	231.5	116.7
Net cash used in investing activities	(455.6)	(322.0)	(89.4)
Net cash from/(used) in financing activities	(23.9)	390.1	(29.2)
Net increase/(decrease) in cash and cash equivalents	(253.6)	299.6	(1.9)
Cash and cash equivalents at 1 January	323.9	1.4	3.2
Effect of exchange rate fluctuations on cash and cash equivalents	(8.8)	23.0	0.1
Cash and cash equivalents at 31 December	61.6	323.9	1.4

Net cash from operating activities

The Company's net cash from operating activities was GEL 225.9 million for the year ended 31 December 2011, as compared to GEL 231.5 million for the year ended 31 December 2010, representing a decrease of 2.4 per cent. (or GEL 5.6 million). This decrease was mainly due to a payment of GEL 30.3 million in the year ended 31 December 2011 in relation to the Company's income tax liability for the year 2010, as compared to a payment of GEL 4.9 million in the year ended 31 December 2010. Cash flows from operations before income taxes increased by GEL 17.6 million (or 7.4 per cent.) as a result of an increase in cash receipts from customers of GEL 47.2 million (or 10.9 per cent.), partially offset by an increase of GEL 29.5 million (or 15.1 per cent.) in cash paid to suppliers and employees, in each case, in 2011, as compared to 2010.

The Company's net cash from operating activities was GEL 231.5 million for the year ended 31 December 2010, as compared to GEL 116.7 million for the year ended 31 December 2009, representing an increase of 98.4 per cent. (or GEL 114.8 million). The increase was mainly due to an increase in cash flows from operations before income taxes of GEL 102.3 million (or 75.1 per cent.) and a decrease in income tax payments of GEL 13.1 million (or 72.8 per cent.). The increase in net cash from operating activities was due principally to an increase in cash receipts from customers of GEL 97.0 million (or 28.8 per cent.), as well as a decrease in cash paid to suppliers and employees of GEL 5.2 million (or 2.6 per cent.).

Net cash used in investing activities

The Company's net cash used in investing activities was GEL 455.6 million for the year ended 31 December 2011 as compared to GEL 322.0 million for the year ended 31 December 2010, representing an increase of 41.5 per cent. (or GEL 133.6 million), primarily as a result of payments made in the implementation of the Modernisation Project, the implementation of which began in September 2010, and the Bypass Project, the implementation of which began in November 2010.

The Company's net cash used in investing activities was GEL 322.0 million for the year ended 31 December 2010, as compared to GEL 89.4 million for the year ended 31 December 2009, representing an increase of 260.2 per cent. (or GEL 232.6 million), primarily due to an increase of GEL 191.7 million of payments and advance payments for the acquisition of property, plant and equipment, reflecting the implementation of the Modernisation Project and the Bypass Project, and an increase in term deposits of GEL 38.0 million, reflecting the transfer of cash from a current account to term deposits. The increase in 2010 was partially offset by the receipt of GEL 6.3 million in proceeds from sale of investments, as a result of the sale of the Company's 25 per cent. stake in Chitakhevi.

Net cash from/(used in) financing activities

The Company's net cash used in financing activities was GEL 23.9 million for the year ended 31 December 2011. In 2011, the Company made a payment of GEL 43.1 million in respect of interest on the 2010 Notes. On the basis of Article 29^2 (*Activities to be implemented by the Ministry of Economy and Sustainable Development*) of the *Law on the Budget of Georgia*, GEL 20 million in cash was contributed in April 2011 to the capital of the Company for the purposes of its further transfer to the capital of the Company's subsidiary, Georgian Railway Property Management LLC, which partially offset the interest payment in respect of the 2010 Notes.

The Company's net cash from financing activities was GEL 390.1 million for the year ended 31 December 2010. In 2010, the Company received GEL 455.1 million in proceeds from borrowings, which comprised the proceeds from the

2010 Notes issued in July 2010, which was partially offset by GEL 29.0 million in repayment of borrowings and dividends paid of GEL 36.0 million.

The Company's net cash used in financing activities was GEL 29.2 million for the year ended 31 December 2009. In 2009, the Company paid dividends of GEL 36.0 million and repaid borrowings of GEL 21.1 million, which were partially offset by the receipt of GEL 27.9 million in proceeds from borrowings, principally reflecting the issuance of the 2009 Lari Notes.

Borrowings

As at 31 March 2012, the outstanding indebtedness of the Company, consisting primarily of amounts outstanding in respect of the 2010 Notes, was GEL 420.1 million, including GEL 7.5 million in accrued interest thereon.

2010 Notes

On 22 July 2010, the Company issued the 2010 Notes, which are admitted to the Official List of the UKLA and to trading on the London Stock Exchange. The 2010 Notes mature on 22 July 2015 and bear interest at the rate of 9.875 per cent. per annum, which is payable semi-annually in arrear on 22 January and 22 July in each year. The terms and conditions of the 2010 Notes contain a negative pledge provision, a restriction on certain corporate reorganisations and a covenant relating to the maintenance of a net financial indebtedness ratio to not more than four times EBITDA. As at the date of this Prospectus, the Company believes that it is in compliance with all covenants under the 2010 Notes.

The entire U.S.$250.0 million of principal indebtedness represented by the 2010 Notes remains outstanding as at the date of this Prospectus. Promptly following the issuance of the 2010 Notes, the proceeds from this offering were converted into Swiss Francs and have been used or reserved to fund the Modernisation Project and the Bypass Project, with a portion of the proceeds being held as at the date of the Prospectus in term deposits.

See "*—Current Trading and Prospects; Trends—2010 Notes Tender*" for a description of the 2010 Notes Tender.

Other credit facilities

The Company's other credit facilities, which are listed below, include various general and financial covenants, typical for agreements of this nature, including certain financial ratios, restrictions on disposals of certain assets and financial reporting obligations. As at the date of this Prospectus, the Company believes that it is in compliance with all covenants under these facilities.

- On 17 March 2010, the Company entered into the 2010 EBRD Loan in order to partly finance the Bypass Project. Under this loan agreement, the Company agreed not to pay any dividend to the Government as its current shareholder until the completion of the Bypass Project. Under the 2010 EBRD Loan, among other things, the Company was obliged to maintain certain financial ratios and was prohibited from entering into any derivative transactions, including interest rate or currency swaps. The 2010 EBRD Loan also restricted investments, including by way of loans, advances or deposits by the Company in its subsidiaries or any other person or enterprise. The 2010 EBRD Loan was cancelled, undrawn, on 4 November 2011. A one-time amount of approximately €1.2 million (approximately GEL 2.3 million) has been paid by the Company in connection with the cancellation and prepaid finance costs were written off.

- On 16 July 2010, the Company entered into a GEL 32.0 million credit line agreement with JSC Bank of Georgia under which amounts borrowed bear interest at an annual rate of 14.5 per cent. The final maturity date of this facility is 15 July 2013, although the Company expects to agree an extension to 16 July 2017. The consent of the EBRD was obtained prior to the Company entering into this credit line agreement. As at 31 March 2012 and the date of this Prospectus, no amounts were or are outstanding under this credit line agreement.

- On 16 July 2010, the Company entered into a U.S.$4.0 million credit line agreement with JSC VTB Bank (Georgia), under which amounts borrowed bear interest at an annual rate of 12 per cent. The final maturity date is 16 July 2014, although the Company expects to agree an extension to 16 July 2015. The consent of the EBRD was obtained prior to the Company entering into this credit line agreement. On 12 December 2011, the credit amount available under this credit line agreement was extended to U.S.$5.0 million in addition to the maturity date being extended to July 2014. As at 31 March 2012 and the date of this Prospectus, no amounts were or are outstanding under this credit line agreement.

- In December 2009, the Company issued the 2009 Lari Notes bearing interest at 13.5 per cent. and maturing in December 2011. In August 2010, the Company exercised a call option over 100 per cent. of the 2009 Lari Notes and used part of the proceeds from the 2010 Notes to pay the remaining U.S.$1.1 million outstanding liabilities in respect of the 2009 Lari Notes.

- On 22 December 1998, the Company entered into a U.S.$20.0 million loan agreement with the EBRD with an interest rate of LIBOR plus 1.0 per cent. and a maturity of 22 December 2010. The loan was payable in semi-annual instalments of U.S.$1.1 million. In August 2010, the Company used part of the proceeds from the 2010 Notes to pay the remaining U.S.$1.1 million outstanding in respect of this loan.

Capital expenditures

The Company's total cash flows used in acquisition of property, plant and equipment for the years ended 31 December 2011, 2010 and 2009, were GEL 436.0 million, GEL 281.7 million and GEL 90.0 million, respectively. The Company has budgeted capital expenditures for the year ended 31 December 2012 of CHF 163.5 million (U.S.$274.1 million). Until September 2010, when the Company began to implement the Modernisation Project, the Company's principal capital expenditures consisted of expenditures on the acquisition of new units of, and repairs of existing, rolling stock and the rehabilitation of infrastructure assets such as bridges, rails, and electric supply assets. From September 2010, the Company also began to incur capital expenditures on the Modernisation Project. In November 2010, the Company began to incur capital expenditures relating to the Bypass Project. See "*Description of the Company's Business—Bypass Project*".

Based on its current plans and relevant estimates, the Company estimates its planned capital expenditures in the three-year period from 1 January 2012 to 31 December 2014 to be approximately CHF 405.0 million. The following table sets forth the Company's budgeted expenditures for the periods indicated:

	For the year ended 31 December		
	2012(E)[(1)]	**2013(E)[(1)]**	**2014(E)[(1)]**
		(CHF millions)	
Modernisation Project[(2)]	57.1	48.0	48.0
Bypass Project[(3)]	36.1	88.5	26.4
Other capital expenditures[(4)]	68.7	56.7	52.5
Total	**161.9**	**193.2**	**126.9**

(1) Estimates based on amounts currently budgeted by management.

(2) Based on currently contracted amounts, capital expenditure on the Modernisation Project is estimated to be CHF 48.0 million in 2015, CHF 48.0 million in 2016 and CHF 48.0 million in 2017.

(3) Payments in following years will be for the most part dependent on dividends paid by the Company in accordance with the terms of the Bypass Project Memorandum. See "*Description of the Company's Business—Bypass Project*".

(4) Includes maintenance expenditures and investments in capital repairs of electric locomotives. Current plans include the purchase of between 200 to 290 new railcars in the period from 2012 to 2016, predominantly grain hoppers. In addition, Management's current plans during that period include making capital repairs on approximately 1,000 to 1,200 of existing railcars. Management also plans to invest approximately GEL 6.7 million in the period from 2012 to 2016 in the construction of container terminals and related infrastructure equipment in addition to the existing investment of GEL 2.4 million.

See "*Description of the Company's Business—Modernisation Project*" and "*Description of the Company's Business—Bypass Project*".

Management reviews, and will continue to review, its budgeted capital expenditures from time to time and intends to maintain a capital expenditure programme that will not inhibit its payment of dividends. Management expects to adjust to its capital expenditure plan depending on a number of factors, including the evolution of the Company's actual results of operations and cash flows as against budget, market conditions, levels of demand for the Company's services, the availability of funding and other factors fully or partially outside the Company's control. See also "*Risk Factors*".

Contractual capital commitments

The table below sets forth the amount of the Company's contractual capital commitments, as at 31 December 2011, based on contractual undiscounted payments:

	As at 31 December 2011				
	Total	**Less than 1 year**	**1-2 years**	**2-5 years**	**More than 5 years**
			GEL (millions)		
Loans and borrowings[1]	558.4	41.0	41.0	476.5	—
Purchase of property, plant and equipment[2] and other[3]	42.5	42.5	—	—	—
Construction works[4]	811.6	159.0	251.0	313.3	88.3
Total	**1,156.7**	**159.7**	**155.5**	**756.1**	**85.3**

(1) Includes interest and principal payments on the 2010 Notes.

(2) Purchase of property, plant and equipment comprises mainly capital expenditures of less than GEL 100,000 and miscellaneous operating expenditures.

(3) Other comprises principally capital expenditures of less than GEL 100,000 and operating expenditures.

(4) Construction works comprises mainly construction works in relation to the Modernisation Project and excludes costs and expenses in relation to the Bypass Project.

On 31 March 2012, the Company entered into the Tank Car Lease Agreement, which management understands shall be treated under IFRS as an operating lease. See "*Current Trading and Prospectus; Trends – Tank Car Lease Agreement*". As at the date of this Prospectus, the Company does not have any other off-balance sheet liabilities or other arrangements.

Related Party Transactions

During the periods under review in this Prospectus, in the course of its business, the Company has engaged, and continues to engage, in transactions with related parties. Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operation decisions or these parties are under common ownership or control, as defined in IAS 24 "*Related Party Disclosures*".

The Company is controlled by the State, and 74.5 per cent. of the State's shares in the Company are held directly and are controlled by the EMA, an agency of the MESD, with the remaining 25.5 per cent. of the State's ownership of the Company held indirectly by the PF, which is itself 100 per cent. directly owned by the State. See "*Shareholders and Management*".

The Company's related party transactions largely consist of transactions with the State and other State-owned companies.

Transactions with management and close family members

Key management personnel consist of the five top executives of the Company. For the years ended 31 December 2011, 2010 and 2009, total salaries and bonuses received by such persons, which is included in the Company's employee benefits expense, was GEL 1.2 million, GEL 1.0 million and GEL 0.9 million, respectively.

Transactions with other related parties

The Company's other related party transactions consist of services provided to and received by, and goods purchased from, other State-owned companies and government bodies, as well as certain liabilities to the State. These consist mostly of electricity purchases from a State-owned operator. For these services, the Company paid an aggregate of

GEL 13.9 million, GEL 16.5 million and GEL 15.7 million, for the years ended 31 December 2011, 2010 and 2009, respectively.

The Company purchases services from Georgian government entities, including mainly security services from a state agency. For these services, the Company paid an aggregate of GEL 7.6 million, GEL 7.6 million and GEL 6.8 million, for the years ended 31 December 2011, 2010 and 2009, respectively.

The Company usually does not carry significant balances for these liabilities. Management estimates that the aggregate amounts of other income and expenses and the related balances with other government-related entities are not significant.

Other balances

	For the year ended 31 December		
	2011	**2010**	**2009**
Liabilities to the owners	13.2	29.2	26.7

Liabilities to the owners relate to property, plant and equipment that has been withdrawn but not yet transferred formally to the State. These liabilities are recognised at the carrying amount of assets to be transferred to the State.

For further information on certain of the Company's related party transactions, see Note 28 of the 2011 Audited Consolidated Financial Statements and Note 27 of the 2010 Audited Consolidated Financial Statements.

Quantitative and Qualitative Disclosures about Market Risk

The Company has exposure to credit risk, liquidity risk and market risk from its use of financial instruments. The Company's risk management policies are established to identify and analyse the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Company's activities. The Company, through training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

Credit risk

General

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers. The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk was GEL 168.2 million, GEL 400.7 million and GEL 23.5 million as at 31 December 2011, 2010 and 2009, respectively. For information about the maximum exposure to credit risk by type of financial asset and (with respect to trade receivables) by geographic region, see Note 24 of the 2011 Audited Consolidated Financial Statements and Note 23 of the 2010 Audited Consolidated Financial Statements.

To mitigate the credit risk of cash and bank balances, the Company holds its funds with the largest five Georgian banks. The Company does not expect any counterparty to fail to meet its obligations.

The Company's exposure to credit risk with respect to its trade and other receivables is influenced mainly by the individual characteristics of each customer. In the years ended 31 December 2011 and 2010, approximately 30 per cent. of the Company's revenue was attributable to sales transactions with a single customer, as compared to approximately 35 per cent. in 2009. Credit risk is managed by requesting prepayments from freight and passenger transportation customers. Accordingly the Company's trade receivables mainly consist of receivables from foreign railway companies.

Credit risk related to receivables from foreign railway companies is managed through the monthly monitoring of the respective receivable balances and requiring immediate repayment of the debt when the balance approaches specific limits set for each individual counterparty. In monitoring customer credit risk, customers are grouped according to their credit characteristics, including aging profile, maturity and existence of previous financial difficulties. No collateral in respect of trade and other receivables is generally required.

Impairment losses

The Company establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The main component of this allowance is a specific loss component that relates to individually significant exposures. The allowance account in respect of trade receivables is used to record impairment losses until all opportunities for recovery have been exhausted; at that point the amounts are written off against the financial asset directly. At 31 December 2011, 2010 and 2009, the collective impairment on the Company's trade receivables was nil.

The following table sets forth the aging of trade receivables as at the dates indicated:

	As at 31 December					
	2011		2010		2009	
	Gross	Impairment	Gross	Impairment	Gross	Impairment
	(GEL millions)					
Not past due	—	—	—	—	0.2	—
Past due 0-90 days	14.2	2.0	5.6	0.6	4.8	—
Past due 91-180 days	8.7	1.4	4.1	1.1	3.2	—
Past due 181-365 days	6.3	2.1	6.7	1.3	7.8	2.7
Past due more than one year	76.2	74.3	78.7	69.4	71.4	63.6
Total	**105.4**	**79.8**	**95.1**	**72.4**	**87.3**	**66.3**

Most of the impairment loss at 31 December 2011 relates to several customers that have indicated that they are not expecting to be able to pay their outstanding balances either because of economic circumstances or as a result of bankruptcy. The Company believes that the unimpaired amounts that are past due are still collectible, based on historic payment behaviour and analyses on the underlying customers' credit ratings.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation. The Company aims to have sufficient cash on demand to meet expected operational expenses for a period of three months, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

In addition, as at the date of this Prospectus, the Company has not borrowed any funds under its loan agreements with JSC Bank of Georgia and JSC VTB Bank (Georgia). See "*—Liquidity and Capital Resources—Borrowings—Other credit facilities*" for a description of these facilities.

For information about the contractual maturities of the Company's financial liabilities and other contractual obligations and commitments as at 31 December 2011, see "*—Liquidity and Capital Resources—Contractual obligations and commitments*".

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

Currency risk

The Company is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the Lari. The currencies in which these transactions primarily are denominated are U.S. Dollars and Swiss Francs. A majority of the Company's revenue has, historically, been denominated in Swiss Francs, however, with effect from 1 February 2012, the Company changed its freight tariff currency from Swiss Francs to U.S. Dollars. See "*—Current Trading and Prospects; Trends—Swiss Franc Exchange Rates*".

The following table sets forth the Company's exposure to foreign currency risk as at the dates indicated:

	As at 31 December					
	2011		2010		2009	
	U.S.$-denominated	CHF-denominated	U.S.$-denominated	CHF-denominated	U.S.$-denominated	CHF-denominated
	(GEL millions)					
Cash and cash equivalents	26.1	24.2	15.0	312.5	0.4	0.05
Bank deposits	13.4	63.1	10.6	27.4	—	—
Trade receivables	0.6	19.0	0.1	14.1	0.2	13.5
Unsecured bank facility	(0.04)	—	—	—	(3.8)	—
Unsecured bond issues	(432.0)	—	(457.6)	—	—	—
Trade and other payables	(0.08)	(0.04)	(12.3)	—	(16.8)	(1.8)
Net exposure	**(392.0)**	**106.3**	**(444.2)**	**354.1**	**(19.9)**	**11.7**

A strengthening of the Lari, as indicated in the table below, against the U.S. Dollar and the Swiss Franc would have increased (decreased) profit or loss net of taxes. There would have been no impact directly on equity.

The following table sets for the effects described above as at the dates indicated:

	Profit or loss(1)
	(GEL millions)
31 December 2011	
U.S.$ (10 per cent. strengthening)	33.3
CHF (10 per cent. strengthening)	(9.0)
31 December 2010	
U.S.$ (10 per cent. strengthening)	37.8
CHF (10 per cent. strengthening)	(30.1)
31 December 2009	
U.S.$ (10 per cent. strengthening)	1.7
CHF (10 per cent. strengthening)	(1.0)

(1) This analysis is based on foreign currency exchange rate variances that the Company considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

A weakening of the GEL against the above currencies at 31 December 2011 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Company's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Company over the expected period until maturity. As at the date of this Prospectus, the Company does not have any outstanding financial assets or liabilities that bear a variable rate of interest. The Company does not account for any fixed rate financial assets and liabilities at fair value, and therefore a change in interest rates at the relevant reporting date would not affect profit or loss or equity.

Capital management

The Company has no formal policy for capital management but management seeks to maintain a sufficient capital base for meeting the Company's operational and strategic needs, and to maintain confidence of market participants. Management seek to manage capital expenditures to maintain a conservative and prudent leverage policy. Management believes that this is achieved with efficient cash management, constant monitoring of the Company's revenues and profit, and long-term investment plans mainly financed by the Company's operating cash flows.

Critical Accounting Policies

The Company has identified the accounting policies discussed below as critical to the Company's business and results of operations. The following accounting policies are both important to the portrayal of the Company's reported amounts of expenses, assets, liabilities and the disclosure of contingent liabilities at the reporting date and require the Company's management's most subjective or complex judgments, often as a result of the need to estimate the effects of matters that are inherently uncertain. The Company's management bases its estimates and assumptions on historical experience, where applicable and other factors believed to be reasonable under the circumstances. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amount of the asset or liability affected in the future. The Company and its management cannot offer any assurance that the actual results will be consistent with these estimates and assumptions.

Useful life of property, plant and equipment

The Company reviews the useful life and depreciation methods of its property, plant and equipment at each financial year-end and makes adjustments if appropriate. Depreciation is based on the cost of an asset less its residual value. Significant components of individual assets are assessed and if a component has a useful life that is different from the remainder of that asset, that component is depreciated separately. Depreciation is recognised on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. These estimates may have a significant effect on the carrying amount of property, plant and equipment and on the depreciation recognised in the consolidated statement of comprehensive income.

Impairment allowances for trade and other receivables

Financial assets, including trade and other receivables, are assessed at each reporting date to determine whether there is any objective evidence that they are impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably. The Company considers evidence of impairment for receivables at both a specific asset and collective level. All individually significant receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Receivables that are not individually significant are collectively assessed for impairment by grouping together loans and receivables with similar risk characteristics.

In assessing collective impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends. Impairment losses are recognised in profit or loss and reflected in an allowance account. The allowance account in respect of trade receivables is used to record impairment losses until all possible opportunities for recovery have been exhausted; at that point the amounts are written off against the financial asset directly. In the event that the financial position of a customer deteriorates more than expected, the actual amount of the write-off may exceed the expected one.

New Accounting Standards

Certain new standards, amendments and interpretations have been published that were not yet effective as at 31 December 2011 and were not applied in preparing the 2011 Audited Consolidated Financial Statements. For information on these new accounting pronouncements that may impact the Company's operations, see Note 4 to the 2011 Audited Consolidated Financial Statements included elsewhere in this Prospectus.

INDUSTRY

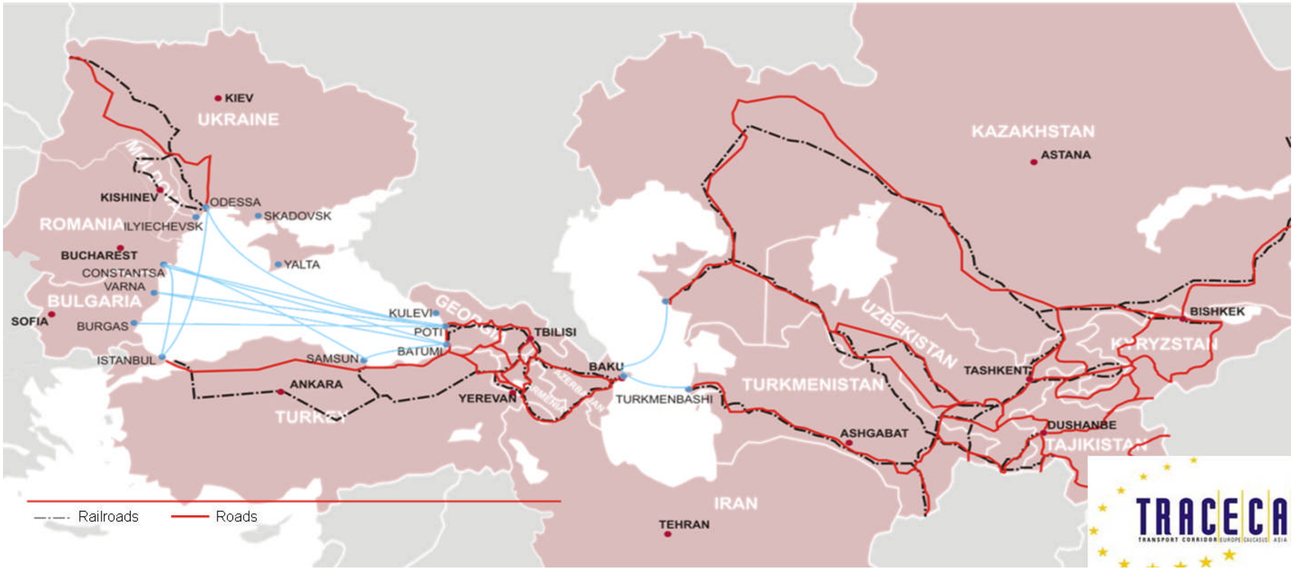
Overview

The Company's mainline rail network, together with that of Azerbaijan Railway, forms the Caucasus corridor, a key segment of the TRACECA corridor. The Company's mainline rail network is thus a link in the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. As a key link in the transportation chain between Europe and Central Asia, the Company believes that it is uniquely positioned to capitalise on increasing volumes of trade between Europe, the Caspian Region and Central Asia. Three of the Company's lines terminate at the Black Sea, at the port cities of Batumi, Kulevi and Poti. Access to these ports allows easy on-shipment of transit cargo to the Mediterranean basin and Europe.

The Caucasus Transportation Market

Introduction

The TRACECA corridor is the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. Railway transportation through the Caucasus corridor is shared by Georgia and Azerbaijan, which act as a bridge between the Caspian Sea and Black Sea regions. The map below shows key transportation links in the region:



Source: TRACECA

TRACECA

TRACECA is a technical assistance programme financed by the EU, which was first established in 1993. TRACECA is aimed at the development of the transport corridor between Europe and Asia across the Black Sea, the countries of the South Caucasus and Central Asian countries.

In 1998, the Basic Multilateral Agreement on International Transport for development of the Transport Corridor (the "**TRACECA Basic Agreement**") was signed by Armenia, Azerbaijan, Bulgaria, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Romania, Tajikistan, Turkey, Uzbekistan and the Ukraine. Iran also became a signatory member in 2009, while Turkmenistan participates in the technical assistance programme without being a signatory member. The strategic framework of the TRACECA programme is comprised of five pillars with the aim of delivering sustainable, efficient and integrated multimodal transportation system at the EU and TRACECA levels by 2015, including: (i) assisting in the development of economic relations, trade and transport communications in Europe, the Black Sea region and Asia; (ii) ensuring access to the world markets of road, rail transport and commercial navigation; (iii) ensuring traffic security, cargo safety and environmental protection; (iv) harmonising transport policy and legal structure in the field of transport; and (v) creating equal conditions of competition for transport operations.

Five expert groups have been established, comprising (i) aviation; (ii) security (in relation to all modes of transport); (iii) road and rail transport; (iv) transport infrastructure; and (v) maritime transport groups. In 2000, the Intergovernmental Commission TRACECA (the "**IGC**") was established to regulate issues relating to the implementation and application of the TRACECA Basic Agreement and in 2001 the IGC TRACECA Permanent Secretariat was established in Baku. According to figures published by the EU, it has financed 62 technical assistance and 13 investment projects through TRACECA since 1993. One of these projects was the rehabilitation of the railway line between Tbilisi and Yerevan between 2008 and 2009.

Overview of key players

The key players in the railway transportation sector in the Caucasus region are the Company, Azerbaijan Railway and South Caucasus Railways (formerly Armenian Railways and now operating under a concession to Russian Railways). The Company's railway network connects with Azerbaijan Railway's network at the Azerbaijan border, and management estimates that well over half of the Company's transit freight traffic is received from or transported to Azerbaijan Railway's network. The Company's rail network also connects with the South Caucasus Railways' network, although the tonnage transported through this connection is much lower. Since hostilities in the Abkhazia region in 1992, there has been no active link through Abkhazian Railway. There is no indication that this link will be re-opened in the near-term.

Upon completion of the construction of the new Baku-Tbilisi-Kars railway line, the Company's rail network will be connected to the railway network operated by Turkish Railway. See "*Description of the Company's Business—Baku–Tbilisi–Kars Railway Venture*"

Recent investments and acquisitions by large international corporations in the Black Sea ports of Batumi, Kulevi and Poti, highlight the strategic importance of the TRACECA and Caucasus corridors for transportation in the region. The Company's rail network serves all three of these ports. See "*—Infrastructure developments*".

Freight Traffic Overview

The Caucasus corridor is mainly used for the transportation of bulk commodity products comprised of oil and oil product liquid cargoes and dry cargos, which are largely comprised of ores, grain and construction freight.

The volume of railway freight traffic is affected by global and regional macroeconomic conditions, the availability of infrastructure capacity, including ports capacities and rolling stock, and competition from other modes of transport. Freight customers have several options for the transportation of products within the region. The substantial majority of oil produced in the Caspian Basin is transported via the pipeline network. This network is dominated by the BTC and CPC pipelines and supplemented by a number of smaller pipelines and share of the Russian pipeline system made available to Caspian Basin oil production. In addition, transportation routes involving transport by rail through the Caucasus corridor (via Georgia and Azerbaijan), Russia or Iran, as well as swaps with Iran or other transport options are also available. The transportation of dry cargo through the Caucasus corridor is mainly conducted by railway or road and growing levels of containerisation have been seen in recent years.

Key drivers of freight traffic

Georgia is a regional transport link for freight traffic and the Company is neither dependent on domestic demand nor domestic production in order to maintain its freight traffic levels. Freight traffic has typically been driven by the production of oil in the Caspian region and various infrastructure projects, including the opening of oil pipelines and pipeline and refinery expansion projects, as well as industrial activity in the region and improvement works at the Black Sea and Caspian Sea ports.

Liquid cargo

One of the key drivers of freight traffic is the production of oil and oil products in the Caspian region. The Caspian region has large oil reserves and growing production. The growth of oil production in the region is expected to continue as production increases at the major Kazakhstan fields of Tengiz, Karachaganak and Kashagan and at the Azeri, Chirag and deepwater Gunashli (ACG) fields in Azerbaijan develop. Fluctuations in the prices of oil in the region also affect oil production activities and consequently the regional demand for transportation of oil and oil products. Crude oil transported by rail through the Caucasus region is mostly high grade Azeri-light oil that is inefficient to transport in a pipeline where it gets mixed with lower grade oil. The east-bound transport of liquid cargo is principally crude oil from the Caspian and Central Asia, with volumes mainly driven by general economic factors and the level of oil production. West-bound liquid cargo transportation is largely oil products, which is driven mainly by demand factors and the oil refining capacity in the region.

Crude Oil. According to the Oil and Gas Ministry of the Republic of Kazakhstan, approximately 80 million tonnes of crude oil was produced in Kazakhstan in the first nine months of 2011, in-line with 2010 production volumes. Production volumes are expected to increase to 95 million tonnes by 2015. The Oil and Gas Ministry of the Republic of Kazakhstan expects this figure to increase to approximately 132 million tonnes of crude oil in 2020. According to the Oil and Gas Ministry of the Republic of Kazakhstan, in 2011, 9.0 million tonnes was exported via Aktau harbour in Kazakhstan, the main sea gate of Kazakhstan to the Caspian Sea, which it expects to increase to 12.0 million tonnes of crude oil in 2020. According to the State Oil Company of the Azerbaijan Republic ("**SOCAR**"), approximately 50 million tonnes of crude oil were produced in Azerbaijan in 2010. Approximately 46.0 million tonnes of crude oil was expected to be produced in the Republic of Azerbaijan in 2011, which SOCAR expects to increase to approximately 50–60 million tonnes of crude oil in 2015. SOCAR believes the transit potential for crude oil exports via the Baku-Kulevi/Batumi/Poti railway route is approximately 200–240 thousand barrels per day.

The map below shows the estimated capacities of oil transportation options for 2015, as estimated by the World Bank in 2008:

Source: World Bank, Caucasus Transport Corridor for Oil and Oil Products, 2008. Capacities shown represent capacities for 2015 as estimated by the World Bank.

The Company intends to increase crude oil volumes and targets reaching 2006 levels of approximately 8.5 million tonnes by 2015. The Company's partners in Kazakhstan, namely JSC National Company KazMunayGas ("**KMG**") and Tengiz Chevron, have indicated their willingness to increase crude oil transportation via Georgia, that it is partially driven by their willingness to increase transportation via Batumi port, which is owned by KMG. Therefore the Company believes that such growth is achievable and it proactively addresses potential capacity constraints by investing in additional tank cars. According to the Minister of Transportation of Azerbaijan, SOCAR intends to invest in an additional 1,500 tank cars to support the above-mentioned expected increases in volumes. Furthermore, on 30 March 2012, the Company (as lessee) entered into the Tank Car Lease Agreement to lease up to 1,000 tank cars from AS Spacecom (as lessor) until 1 April 2015. Under the Tank Car Lease Agreement, the lessor is required to lease to the Company 425 tank cars within one month from receiving a request from the Company. Upon the Company's request, the lessor is also required to provide up to a maximum of 575 additional tank cars within one month of the date of receipt of such request. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Tank Car Lease Agreement*".

Management believes that the BTC Pipeline accounted for approximately 38 million tonnes (or approximately 50 per cent. of the total westbound traffic) of oil transported in 2010, and the CPC Pipeline accounted for approximately 28 million tonnes (or approximately 40 per cent. of the total westbound traffic). Management also believes that the Black Sea ports served by rail accounted for approximately eight million tonnes (or approximately 10 per cent. of the total westbound traffic) in 2010. Oil products and high sulphur crude oil cannot be transported through the pipelines.

The global financial crisis has, however, resulted in a reduction in available capital for investment in the industry and a greater reluctance of financial institutions to lend money. An increased cost of capital led to short-term funding issues for infrastructure projects in the region, which in turn resulted in a hiatus in oil production, expansion of refinery facilities, port development and pipeline capacity increases. Projects in the region that have been delayed, at least in part due to economic conditions, include: (i) the expansion of the CPC Pipeline; (ii) the expansion of the Kulevi port; (iii) further development of the Kashagan oil field in Kazakhstan; and (iv) the modernisation and expansion of the Batumi port.

<u>Oil Products.</u> Transportation of oil products is a second important driver of freight volumes in the region. Oil products drive rail transport in particular, as they cannot be transported through pipelines. There are three refineries in Kazakhstan and two large refineries in Baku, Azerbaijan. Oil products are also produced at refineries in Turkmenistan and Armenia. A study published by the World Bank in 2008 forecasted that production of oil products in Kazakhstan would increase from 12.6 million tonnes in 2005 to 18.0 million tonnes in 2015. Similarly, the study forecasted that production of oil products in Azerbaijan would increase from 7.2 million tonnes per year in 2005 to 10.5 million tonnes per year in 2015. In addition, the World Bank forecasted that exports of oil products from Kazakhstan would remain constant at 3.0 million tonnes per year and exports from Azerbaijan would increase from 2.2 million tonnes in 2005 to 2.5 million tonnes in 2015. Given the unsuitability of oil products for pipeline transport, changes or fluctuation in the production and export of oil products may have a significant impact on volumes of freight traffic carried by railway in the region.

The Company expects oil products traffic from Turkmenistan (representing over 50 per cent. of transit volumes) to increase and at least partially on the basis of this growth the Company aims to reach the peak level of 2006. Management estimates that total oil products production in Turkmenistan is approximately 8 million tonnes per annum and that there is scope for it to continue to capture an increasing portion of this transit as soon as the existing bottlenecks are resolved. In recent years, the available capacity of the limited number of ferries operating on the Caspian Sea was constrained by the increase in dry cargo volumes, causing a capacity shortage for oil products. The Company believes that the decision of Azerbaijan to add two additional large ferries will drive an increase in oil products volume. The Company believes that this investment by Azerbaijan may also result in the redirection to the Caspian Sea of some of the Turkmen oil products currently transiting through Iran. These volumes are transported mainly by European traders who are willing to increase export of oil products to European markets.

Dry cargo

The major factors driving transportation of dry cargo in the region are general economic conditions, construction activity and specific industrial projects in the region. In particular, the volumes of agricultural products transported by the Company are affected by general demographic trends and consumption levels while construction material volumes are driven by construction cycles and the general economic environment. Transport of ferrous metals, scrap, ores and chemicals and fertilisers is impacted by the international market prices for these commodities. Investments in current infrastructure along the corridor, such as at the Black Sea ports, are also expected to affect the volumes of dry cargo transported by rail. The Kulevi port currently does not handle dry cargo and the substantial majority of cargo handled at the Batumi port is liquid cargo. In contrast, in 2010, 50 per cent. of cargo handled at the Poti port was bulk cargo, 34 per cent. was general cargo and 16 per cent. was liquid cargo.

Several key companies support the volumes of dry cargo traffic in Georgia, including:

- Georgian Manganese Holding ("**GMH**"), whose subsidiary produces iron alloys solely for export. Based on conversations with representatives of GMH, management believes that GMH plans to increase its capacity and expects that this will result in increased transport volumes for the Company;

- Heidelberg Cement Georgia, the largest cement producer in the Caucasus region, operates three cement plants near Tbilisi in the Kaspi and Rustavi regions with a total combined capacity of approximately 2.0 million tonnes of cement on average per year. In addition to cement production, Heidelberg Cement Georgia also sells clinker. Approximately 50 per cent. of its manufactured products are exported to Azerbaijan and Kazakhstan. According to a press release in October 2011, Heidelberg Cement Georgia announced its continued expansion in the Georgian market through the commencement of operations at a new mobile concrete plant by its subsidiary, HeidelbergBeton Georgia, in September 2011, building upon the previous expansion of operations by this subsidiary in 2009 and 2010;

- JSC Madneuli and its sister company Quartzite Ltd., both owned by Moscow-based GeoProMining Ltd., generally derive more than half of their revenues from exporting copper and have requested increased transportation volumes from the Company. According to data published on their corporate websites, JSC Madneuli has an annual throughput rate of 1.8 to 2.1 million tonnes per annum and Quartzite Ltd. has an annual throughput rate of 2.4 to 3.2 million tonnes per annum;

- Saqnakshiri JSC, a subsidiary of the Georgian Industrial Group, holds an exclusive licence to operate the Tkibuli-Shaori and Akhaltsikhe coal mines and plans to increase coal extraction and to export it to foreign markets. According to information published on Saqnakshiri JSC's website, in the future, the company plans to increase coal extraction to up to 700,000 tonnes per annum, to export enriched coal and to penetrate the international market; and

- Kutaisi Auto Mechanical Plant, a subsidiary of the Georgian Industrial Group, manufactures a range of automobile and industrial components and cooperates with a number of European automotive industry suppliers.

A future further driver in the transportation of dry goods is expected to be the completion of the Baku-Tbilisi-Kars line and the commencement of traffic flows over this new rail link. See "*—Infrastructure Developments—Railway infrastructure improvements*".

<u>Aluminium and related products.</u> Metals transported by the Company include aluminium and other aluminium products whose regional trade is driven principally by the requirements and output of an aluminium factory in Tajikistan (TALCO). In addition, the Ganja Alumina plant in Azerbaijan, which is a key consumer of bauxite in the region, re-opened in late 2011 following reconstruction works, with potential future demand of transportation of bauxites, a key raw material for alumina production, of approximately 40-80,000 tonnes per month. It is estimated that this could create approximately 1.0 million tonnes of additional cargo a year by 2012. In addition, a new integrated aluminium plant in Azerbaijan opened in November 2011, which has the potential for production and transportation of approximately 100,000 tonnes per month of aluminium cargo. Management has received preliminary indications that the Company could expect transport volumes that are somewhat close to these amounts. With the opening of the new aluminium plant in Azerbaijan, management believes that TALCO will need a new source of alumina (as TALCO is unlikely to be able to source the same amount of alumina from Azerbaijan as it has previously done). Management expects that TALCO will replace the Azeri alumina with other imported alumina and that increased amounts could be shipped through Georgian ports as the most efficient route.

<u>Grain and other agricultural products.</u> Historically, the grain transported by the Company principally originated in Russia but a combination of political factors and high prices largely ended this routing of grain in 2007. Currently, grain and grain products transported by the Company largely originates from Kazakhstan, the Ukraine and (to a lesser extent) the United States. This cargo is mostly imported through Georgian ports and Azerbaijan for consumption in Georgia and Armenia. The Russian grain transported by the Company currently is primarily transit cargo destined for Armenia. The sugar and related products that are transported by the Company are largely used in domestic Georgian consumption.

A key driver in the transport of grain and agricultural products is economic growth in the region fostering demand for such products. Increasing tourism in the region also helps drive demand. A programme developed by the Georgian Ministry of Agriculture designed to stimulate the production and export of corn is also expected to increase the volumes of grain and agricultural products transported across the Company's network. The grain terminal modernisation that has recently been undertaken by Bunge, a global agricultural trader, at the Poti port should also enhance volumes of such cargo. Management believes this will increase the attractiveness of the Caucasus corridor for the transport of Kazakh grain and may therefore facilitate an increase in rail transportation of grain products in the future. Grain transportation is cyclical and seasonal and typically tracks the harvest, with a significant amount of such transportation taking place in the second half of the year. See *"—Infrastructure Developments—Infrastructure improvements at the Black Sea ports—Poti*".

Construction Materials. The transport of construction materials (principally cement, limestone and other construction materials) typically follows construction cycles and, for example, the Company saw a peak in 2008 due to the construction boom in Azerbaijan followed by declining volumes during the financial crisis. The demand for construction materials is driven by economic growth in the region and construction activity in Georgia, Azerbaijan and, to a lesser extent, Kazakhstan. Georgia is a strategically located country with strong potential for growth for cement producers. As noted above, there are three cement plants in Georgia operated by Heidelberg Cement, which, according to its website have a total combined capacity of 2.0 million tonnes per annum. HeidelbergCement has reported ongoing volume increases in the region. Limestone is the main raw material in the production of cement and there is a strong correlation between the transport of limestone and cement. The largest limestone quarry in Georgia is in Dedoflistskaro.

There are a number of state-backed construction projects being undertaken in the region and management estimates that approximately 60 per cent. of the demand for construction materials is being driven by governments in connection with these projects. For example, there are 11 HPPs being built in Georgia, as well as other infrastructure projects such as road construction and the Bypass Project. Management believes that, even if the economic outlook were negative, various state-backed projects in Georgia would still be undertaken, particularly the HPPs that are expected to provide a cheaper source of energy in the country.

Containerised cargo. Although containerisation levels are currently low, this is expected to be a key source of growth for dry cargo traffic in the Caucasus corridor. The increased containerisation of the corridor contributes to the diversity of dry cargo that can be transported by the Company, including for example, cotton products, grains, ferrous metals and scrap, and refrigerated products. To foster such containerisation, Railway TransContainer LLC, the Company's subsidiary, has built and currently operates the Tbilisi Container Terminal. For additional information about the Company's transport of containerised cargo, see "*Description of the Company's Business—Business Operations—Freight SBU—Freight Composition*".

Infrastructure Developments

As the Company forms part of the Caucasus corridor, the development of infrastructure in the region also drives freight traffic.

Railway infrastructure improvements. The Company has announced and is in the process of implementing the Modernisation Project to improve and upgrade its railway network infrastructure. In addition, following investment from the World Bank, the Azerbaijan State Oil Fund and other sources of approximately U.S.$1.5 billion, Azerbaijan Railway's network is in the process of being restructured to rehabilitate the east-west line, acquire locomotives and support other modernisation. Based on recent conversations with Azerbaijan Railways, management believes that Azerbaijan Railway currently plans to invest in new locomotives and repair seven existing locomotives. Under South Caucasus Railway's concession with Russian Railways, management believes that approximately U.S.$270 million has been committed for infrastructure and equipment upgrades on South Caucasus Railway's network. The Company expects to benefit from the rehabilitation of Azerbaijan Railway's network, as the majority of crude oil and oil products traversing the Caucasus corridor is transported in Azerbaijan Railway's tank cars. See "*Description of the Company's Business—Modernisation Project*".

Another factor which is expected to drive freight traffic volumes in the future is the construction of the Baku-Tbilisi-Kars line, which is intended to transport both goods and passengers between Central Asia and Europe. For a description of the Baku–Tbilisi–Kars line, see "*Description of the Company's Business—Baku–Tbilisi–Kars Railway Venture*".

Infrastructure improvements at the Black Sea ports. A key driver in freight traffic is the ability for the railway to connect to the key ports of Batumi, Kulevi and Poti on the Black Sea, and management believes that the strategic importance of Georgia within the Caucasus corridor has been reinforced by recent investments in such ports:

- *Batumi*. In February 2008, a subsidiary of the Kazakhstan state-owned oil and gas company, KMG, completed the acquisition of a 100 per cent. ownership interest in Batumi Industrial Holdings Limited and Naftrans Capital Partners, which directly own and operate a marine export terminal facility and a seaport in Batumi. The Batumi port handles both liquid and dry cargo and has an existing capacity of approximately 15-16 million tonnes per year, understood to be expandable to 28 million tonnes per year. The Batumi Oil Terminal is dominated by the transit of westbound transit oil and oil products, but can handle small volumes of eastbound traffic destined for the domestic market or Armenia. The Batumi Oil Terminal has a current rail discharge capacity of 600 tank cars per day. While the discussions relating to the construction of an oil refinery at the port have been put on hold due to market conditions, the Company believes that KMG has a significant incentive to continue to use the Batumi port and, as a result, the transportation services offered by the Company.

- *Kulevi*. The Kulevi oil terminal and port was acquired by a consortium led by SOCAR in 2006 and, after two years of heavy investment, started operations in May 2008. The Kulevi oil terminal currently handles only liquid cargo, although the addition of a dry cargo terminal is contemplated. Plans to also construct an oil refinery at the port are currently on hold due to market conditions. The terminal currently has an annual processing capacity of 10 million tonnes of crude oil and refined products per year, which is understood to be expandable to 20 million tonnes per year. The terminal's railway station currently has the capacity to discharge 42 rail tank car trains simultaneously.

- *Poti*. In April 2011, APM Terminals, a unit of Maersk acquired an 80 per cent. interest in the Poti port. Poti port handles both liquid and dry cargos and in 2010, 50 per cent. of the traffic was bulk cargo, 34 per cent. was general cargo and 16 per cent. was liquid cargo. The port has reached its capacity of 7 million tonnes per year and is now developing extension areas. In this regard, Maersk has announced its intention to invest U.S.$100 million to improve the capacity of the port by 2015. Bunge has modernised a grain terminal at the Poti port to allow loading and unloading from the sea- and land-ward side and these modernisations were completed in 2011. Management also believes that this expansion will provide an opportunity to increase the transportation services provided by the Company to and from the Poti port.

As the Batumi and Kulevi ports are controlled by the state-owned oil companies of Kazakhstan and Azerbaijan, respectively, management expects that capacities and any plans to expand these port facilities will be in line with the production plans of these oil companies. Moreover, based on management's conversations with SOCAR, management believes that SOCAR plans to acquire approximately 2,000 oil tank cars, which management believes may indicate that port capacity may increase.

Infrastructure improvements at the Caspian Sea ports. Azerbaijan is currently developing new port infrastructure in Baku on the Caspian Sea. In 2009, the Ministry of Transport of Azerbaijan awarded Royal Haskoning Group a contract to provide design and engineering services, including a port master plan, for a new port facility in Baku. Royal Haskoning has stated that it expects the main focus of the new port to be a rail ferry terminal connecting ports in Kazakhstan and Turkmenistan with Baku. It also expects that the new port will include a general cargo terminal, cargo handling facilities and roll-on/roll-off facilities that should facilitate the transport of wheeled cargo such as railcars and trucks. The port facility is expected to be constructed in three phases and completed in 2014. According to press reports citing the Azerbaijan Transport Ministry, this new port facility will have a capacity of approximately one million TEU.

In recent years, the capacity of the ferries operating in the Caspian Sea was constrained by the transport of increasing volumes of dry cargo, which caused a capacity shortage for the transport of oil products across the Caspian Sea. According to public reports, there are two large and seven small ferries operating in the Caspian Sea. These rail ferries operate between Bulgaria, Russia and Ukraine, as well as between Azerbaijan ports and the Caspian Sea ports of Aktau and Turkmenbashi in Kazakhstan and Turkmenistan, respectively. Azerbaijan is currently adding two large ferries to support transport needs. One large ferry is already operational while the other one should be operational by the end of the year. Management believes that the addition of those two ferries will provide additional volumes to be transported through the corridor.

Macroeconomic factors in the region and trade between TRACECA member states and Europe

A driver of freight traffic in the Caucasus corridor is the trade flows of commodities such as crude oil, oil products, ores and grains, and construction materials within the region. Specifically, freight transit volumes are affected by trade between and among the EU (and, more broadly, Europe) and members of the TRACECA corridor. Freight volumes in relation to intra-territorial cargoes are affected by economic activity within Georgia and the Company's volumes in freight prior to the global recession grew and, since recovery from the global recession began, have grown to a large extent as a result of growing trade between and among the commodity and energy-rich emerging market economies in or near the TRACECA corridor, such as Azerbaijan, Kazakhstan and Turkmenistan, on the one hand, and the EU (and, more broadly, Europe), on the other. The global recession impacted negatively the levels of economic activity in Europe, in particular, and several TRACECA members, including Georgia, and consequently trade undertaken among and between these countries declined and industrial activity slowed within Georgia, resulting in overall reduced freight volumes for the Company in the year ended 31 December 2009. The impact of this reduced trade contributed to the decline in freight volumes experienced by the Company in the year ended 31 December 2009 as demand for commodities and construction materials declined both in Georgia and other end markets of the TRACECA corridor.

According to figures and estimates presented by the IMF, the rates of real GDP growth for 2010 and 2011 and its forecasts until 2015 for Georgia and surrounding nations are as follows:

	2010	**2011**	**2012E**	**2013E**	**2014E**	**2015E**
			(per cent. change)			
Georgia	**6.3**	**7.0**[(1)]	**6.0**	**5.5**	**5.5**	**5.5**
Armenia	2.1	4.4	3.8	4.0	4.0	4.0
Azerbaijan	5.0	0.1	3.1	1.9	2.8	2.9
Kazakhstan	7.3	7.5	5.9	6.0	6.2	6.3
Russia	4.3	4.3	4.0	3.9	3.9	3.9
Turkey	9.0	8.5[(1)]	2.3	3.2	4.0	4.3
Turkmenistan	9.2	14.7[(1)]	7.0	6.7	6.2	6.3

(1) IMF staff estimates

Source: International Monetary Fund, World Economic Outlook Database, April 2012.

Passenger Traffic Overview

Passenger transportation is comprised of both domestic and international transportation services. Domestic travel is segmented between regional and long distance travel. Long distance traffic accounts for the large majority of the Company's passenger traffic, while the regional services, in particular the suburban component, typically serve the low income section of the community and, accordingly, low fares apply to such journeys. This international service comprises the very short haul services between Tbilisi and the Azerbaijan and Armenian borders, as well as the seasonal service from Armenia to Batumi. See "*Description of the Company's Business—Passenger SBU—Passenger Customers*".

Key drivers of passenger traffic

The key drivers of passenger traffic numbers, and, accordingly, the Passenger SBU's revenue, are:

- demographic trends and disposable income of the population in the region, particularly in relation to the more profitable market segment of international travel;
- the level of service provided in terms of journey times, frequency and reliability;
- the quality of service provided;
- the standard of rolling stock in terms of cleanliness and comfort;
- the level of crowding and seat availability on trains;
- the perceived value for money of the service; and
- the competitiveness of rail transportation as opposed to other modes of transportation in terms of journey times, proximity of stations and accessibility.

Other factors expected to positively impact passenger transportation in Georgia in the near-term include the forecasted increase in tourist numbers arriving into Georgia from Azerbaijan and Armenia. In addition, the construction of the Baku-Tbilisi-Kars line, which is expected to be completed in 2013, is also expected to increase passenger numbers. See "*Description of the Company's Business—Baku–Tbilisi–Kars Railway Venture*".

For additional information about the Company's passenger services, and its strategy to transform the Passenger SBU into a profitable operation, see "*Description of the Company's Business—Business Operations—Passenger SBU*". See also "*Risk Factors—Risks Related to the Company's Business—The Company's passenger services have historically generated net losses*".

DESCRIPTION OF THE COMPANY'S BUSINESS

Overview

JSC Georgian Railway is, by statute, Georgia's only railway operator. It principally provides freight services, transhipping a variety of cargo, including oil, oil products, ores and grains, originating principally in the east from the Caspian Sea and Central Asia to the Black Sea. The Company also provides passenger services. It has a vertically integrated business model, owning and operating the tracks, stations, other infrastructure and rolling stock comprising Georgia's entire national railway system, as well as the land adjoining the tracks. The Company sets its own tariffs without the need to obtain governmental approval.

The Company's mainline rail network, together with that of Azerbaijan Railway, forms the Caucasus railway corridor, a key segment of the TRACECA corridor. The Company's mainline rail network is thus a link in the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. As a key link in the transportation chain between Europe and Central Asia, the Company believes that it is uniquely positioned to capitalise on trade between Europe and the Caspian Region and Central Asia. Three of the Company's lines terminate at the Black Sea, at the Georgian port cities of Batumi, Kulevi and Poti. Access to these ports allows easy on-shipment of transit cargo to the Mediterranean basin and Europe.

The Company operates the national railway system through three strategic business units, or SBUs: the Freight SBU, which consists of freight traffic (transportation and handling) and freight car rental services; the Passenger SBU, which primarily transports passengers within Georgia; and the Infrastructure SBU, which operates, maintains and manages the Company's principal infrastructure assets. The Infrastructure SBU provides services only to the Freight SBU and the Passenger SBU and does not conduct business with third-party customers. For the year ended 31 December 2011, the Company transported 20.1 million tonnes of freight and carried 3.3 million passengers.

The Freight SBU accounted for over 90 per cent. of the Company's total revenue in the first quarter of 2012 and each of 2011, 2010 and 2009. The Company transports both liquid cargoes (crude oil and oil products) and various dry cargoes, with liquid cargoes accounting for 48.8 per cent. of the Company's total freight transportation volumes in the three-month period ended 31 March 2012 and 52.0 per cent. in the year ended 31 December 2011. Transport of crude oil across the Company's rail network is an alternative to oil pipelines, and the crude oil transported by the Company primarily originates in Kazakhstan and Azerbaijan. Given its strategic location, management believes that as producers seek to diversify their transportation options, the Caucasus corridor should capture a relatively stable share of the transportation of crude oil in the region, which management estimates to be approximately eight to ten per cent. of total Kazakhstan and Azerbaijan production.

For the year ended 31 December 2011, the Company had consolidated revenue of GEL 477.4 million, profit and total comprehensive income of GEL 174.4 million and EBITDA of GEL 259.9 million, as compared to consolidated revenue of GEL 404.7 million, profit and total comprehensive income of GEL 101.5 million and EBITDA of GEL 194.8 million for the year ended 31 December 2010. For the three month period ended 31 March 2012, the Company had consolidated revenue of GEL 105.8 million and profit and total comprehensive income of GEL 33.1 million, as compared to consolidated revenue of GEL 103.4 million and profit and total comprehensive income of GEL 28.5 million for the three-month period ended 31 March 2011.

Strengths

The Company believes that it has a number of key competitive strengths that will enable it to capitalise on its leading position in the Georgian and Caucasus transportation markets in the future. These include:

A unique strategic location with highly attractive market fundamentals

The Company benefits from its strategic location within the Caucasus region. The Company's railway network comprises a key part of the Caucasus corridor, which is the shortest route from the Caspian Sea to the Black Sea and the Mediterranean basin. The Caucasus corridor is itself part of the TRACECA corridor, an international transportation network involving the EU and 14 states in Eastern Europe, the Caucasus and Central Asia, aimed at economic development of regional emerging market economies through the promotion of international trade flows. As a link in the transportation chain between Europe and Central Asia, the Company believes it is a key beneficiary of the growing trade between these regions. Management believes that the strategic importance of the Caucasus corridor has been reinforced by the recent investments of major corporations in three Black Sea terminals (Batumi (KMG), Kulevi (SOCAR) and Poti (APT Terminals, a unit of Maersk), each at the end of a Company line).

The Company believes that its strategic location will enable it to capitalise on increasing trade between Europe, and the Caspian Region and Central Asia, as well as the increasing demand for oil and oil products from Central Asia. The Caucasus region, including Georgia, has experienced and is expected to continue experiencing strong GDP growth. GDP growth is a key indicator to freight transportation volumes and the IMF forecasts Georgia's real GDP to grow 6 per cent. in 2012. In addition, the Company expects that projected increases in oil production, particularly in Kazakhstan and Azerbaijan, as well as increased refining capacity in the region, will benefit the Company's liquid cargo transportation activity. Given its strategic location, as producers seek to diversify their transportation options, the Caucasus corridor should capture a relatively stable share of the crude oil transported in the region, which management estimates to be approximately eight to ten per cent. of total Kazakhstan and Azerbaijan production. Management believes that future GDP growth in Georgia and other TRACECA member states will further drive demand for commodities, construction materials and ores, in turn, driving freight volumes travelling through the Caucasus corridor.

A well invested asset base

The Company believes that its growth is well supported by its own existing infrastructure and asset base. As at 31 December 2011, the Company's railway network was comprised of 1,326 kilometres of track, of which 94 per cent. was electrified, including a 527 kilometre fully-electrified mainline from the Azerbaijan and Armenian borders to the Black Sea. During the three years ended 31 December 2011, the Company paid GEL 807.7 million to acquire property, plant and equipment, including rolling stock and equipment, and to rehabilitate important infrastructure assets, including rail tracks, electric power supply lines and bridges and tunnels. This amount of investment includes amounts spent on the Modernisation Project and the Bypass Project, both of which are discretionary capital expenditure projects currently being undertaken by the Company to further increase operational efficiencies.

At its peak in the late 1980s, the portion of the Transcaucasian Railway in Georgia carried more than triple the freight volume and four times the passenger volume than it does today. Accordingly, the Company believes that it has substantial capacity for future growth and that its railway network will support such additional traffic with limited need for investment. Aside from maintenance capital expenditure incurred in the ordinary course of business, the Company does not expect any capital expenditure to be required in respect of the mainline in the medium-term, although the Company is undertaking the Modernisation Project and the Bypass Project, on a discretionary basis, in order to increase further operational efficiencies. See "—*Modernisation Project*" and "—*Bypass Project*".

As at 31 December 2011, the Company had 8,122 working and 10,256 serviceable wagons, which comprise a fleet that the Company believes provides capacity for future growth. The Company has adopted a flexible policy in respect of its rolling stock, which includes refurbishment and works to extend the lifetime of existing rolling stock, as well as both the leasing of tank cars under the Tank Car Lease Agreement and the selective acquisition of new railcars, locomotives and wagons where there is demand. The Company's capital expenditure requirements are reduced by the fact that, as a transit railway, a large portion of the cargo transported by the Company is transported using third-party rolling stock (approximately 60.8 per cent. in 2011). In the next few years, the Company expects that its principal investments will be aimed at increasing the Company's supply of rolling stock, when such increases are supported by expected increases in volumes to be transported.

A favourable regulatory framework and strong Government support

The Company's tariff policies are not subject to Government regulation and the Company sets its own freight tariff policy independently and without Government approval, despite being a statutory monopoly. In addition, the Company benefits from the strong support of the Government, which is its majority shareholder. The Company believes that the Government considers it to be a strategically important national asset. In particular, the Government has indicated that the development of the country's infrastructure is one of its highest priorities and that the Company's railway network is a critical component of that infrastructure. Moreover, the Company's provision of key passenger transportation services at affordable prices enables the State to promote regional development. Also, the Company is the largest corporate employer in Georgia, whose business also supports other employment opportunities in Georgia, as well as one of the largest tax payers in the country. The Government has shown strong support for the Company's initiatives over the years and, given the strong alignment of interests between the Company and Georgia, management believes that the Government will continue supporting the Company's operations.

A track record of resilient and profitable growth with further upside

The Company has a strong track record of generating profitable growth. In the year ended 31 December 2011 and the year ended 31 December 2010, the Company generated revenue of GEL 477.4 million and GEL 404.7 million, respectively, representing year-on-year growth of 18.0 per cent. In the three-month period ended 31 March 2012, the Company generated revenue of GEL 105.8 million, representing year-on-year growth of 2.3 per cent., as compared to revenue of GEL 103.4 million for the three-month period ended 31 March 2011. In 2011 and 2010, the Company generated an EBITDA margin of 54.4 per cent. and 48.1 per cent., respectively. Given its flexible business model and ability to set tariffs independently, the Company believes it is better positioned than many of its regional peers to weather economic cycles. For example, in 2009, the Company was able to offset the 19.3 per cent. decrease in freight volumes resulting from the global recession with tariff increases, with the effect that the Company achieved an EBITDA margin of 37.3 per cent. The Company believes that its strong market position, strong client relations, focus on operating excellence, ongoing operational improvements and ability to independently set tariffs provide sustainability to its business model.

The Company's financial and operational stability allows the Company to maintain its infrastructure in good operating condition, including through on-going maintenance and capital improvements, while also pursuing new investment projects, such as the Modernisation Project and the Bypass Project, and to achieve further asset efficiencies. The Company believes that strong growth drivers in its core freight transportation market will enable it to continue to sustain growth, including through the continued development of its container business. In particular, the Company expects that it will be able to capitalise on the expected increase in container traffic in the region through its continued development of container infrastructure in Georgia and neighbouring countries.

In addition, as part of the Baku-Tbilisi-Kars project, the Company has been granted the exclusive right to operate the Georgian portion of the planned railway connection linking Azerbaijan, Georgia and Turkey, which is expected to be completed and commence operations in early 2013. The Baku-Tbilisi-Kars project will effectively open a new rail-only corridor from the Caspian Sea to Europe via Turkey, eventually excluding the need for sea transportation. Management believes that increasing trade between Turkey and Central Asia provides it with a significant opportunity to capture trade flows, particularly raw materials imported into Turkey from Central Asia and finished goods exported by Turkey.

A high quality customer portfolio

Management believes that the Company has developed strong relationships with its key customers. The average length of professional relationship with the Company's top five customers is five years. A substantial majority of revenues is from freight services to freight forwarding companies, which tend to have a diversified customer base of freight owners, thereby increasing demand for the transport of various types of cargo and multiplying the diversity of the Company's indirect freight-owner customer base. Management believes that the Company's well-established relationships with freight forwarders help foster long-term relationships between the Company and the owners of the cargo. Key owners of cargo transported through the Company's freight forwarding customers include various international "blue chip" companies such as BP, Chevron, ExxonMobil Corporation, SOCAR and KMG. Moreover, several key cargo owners have recently invested in port infrastructure in Georgia, including at the ports of Batumi (KMG), Kulevi (SOCAR) and Poti (APT Terminals, a unit of Maersk), all served by the Company's rail lines, which increases visibility over the need for the Company's freight transportation services in the future. The Company believes that its strong relationship with key customers, assisted by the measured approach of its flexible pricing policy, is a key competitive advantage.

An experienced management team with proven track record of delivery

The Company's senior management team has extensive experience and technical expertise in infrastructure businesses. The current management team successfully executed the 2005 Restructuring Programme, which transformed the Company into one of the leading freight transporters in the Caucasus region. Moreover, the management team has also demonstrated the ability to manage growth and profitability, even in an economic downturn. For example, in 2009, the Company was able to offset the 19.3 per cent. decrease in freight volumes resulting from the global recession with tariff increases, with the effect that the Company achieved an EBITDA margin of 37.3 per cent. The Company's top five senior managers have a combined experience of over 30 years working in infrastructure businesses.

Strategy

The Company's strategic objective is to consistently achieve profitability levels above the industry average. The key elements of its strategy are:

Continue to grow its freight service business, while increasing geographic diversification

The Company is upgrading its infrastructure and rolling stock and selectively invests in new capacities to benefit from expected increases in freight volumes in its core markets. The Company expects to capture increasing demand for the transportation of oil and oil products driven by new exploration in the region (including in Azerbaijan and Kazakhstan) and increased refining capacity. In addition, management is focused on capturing volume growth through further diversification of the Company's freight mix, particularly dry cargo. To capture these increased volumes, the Company also plans to continue to adapt its fleet to the transportation of containers. It also plans to promote the containerisation of the Caucasus corridor by making strategic investments, such as in its subsidiary, Railway TransContainer LLC, which built and operates the Tbilisi Container Terminal. The Company expects that containerisation should attract new customers and expand the range of cargoes transported.

The Company also intends to capture volume growth through longer-term expansion to new geographic trading flows, such as the new Baku-Tbilisi-Kars route. The Baku-Tbilisi-Kars project comprises a plan for a new rail-only corridor from the Caspian Sea to Europe via Turkey, eventually excluding the need for sea transportation. The Baku-Tbilisi-Kars project could also open a North-South rail corridor linking Russia to Turkey. The Company may also consider leveraging the industry expertise, best-practices and extensive know-how of the management to establish strategic cross-border partnerships with railway and infrastructure companies in its region of operations, which could benefit from restructuring.

Focus on core business activities

The Company believes that the division of its operations into three business units, the Freight SBU, the Passenger SBU and the Infrastructure SBU, has provided the Company with an optimal corporate structure to operate in the railway industry. This structure enables strategic objectives to be set for each business unit in order to maximise its flexibility and operational efficiency. The Company intends to continue fostering its internal management and control processes to further emphasise its results-oriented culture, attain business excellence and maintain an effective risk management policy. Moreover, although the Company does not participate in freight forwarding, it maintains strong relationships with freight forwarding operators, which helps provide the Company with additional visibility on demand for its infrastructure and rolling stock and the potential capital expenditure needed to match this demand.

Maintain competitiveness of the Caucasus corridor and attract and retain customers through a flexible tariff policy

The Company believes that its high service levels and flexible tariff policy allow it to both foster long-term partnerships with existing freight customers and attract new customers. The Company continuously analyses demand to maintain a tariff system designed to perpetuate the long-term attractiveness of the Caucasus corridor in a manner consistent with the Company's competitive and profitable position. The Company also engages in an ongoing dialogue with its customers to help them find transportation solutions within the Caucasus corridor, including managing relationships with neighbouring railways. The Company believes that its measured approach to tariff setting, and the other benefits it offers to customers, provides them with predictability over their costs. This predictability, in turn, encourages many customers to invest in infrastructure linked to the railway network, thereby reinforcing commercial relationships and an integrated service offering with the Company. The Company also believes that this measured approach to tariff setting also enhances the longer-term predictability for management of the Company's operations and strengthens the competitive position of the corridor through Georgia as compared to alternative routes. The Company intends to continue these measures to maintain and further improve the attractiveness of transportation through Georgia, as well as its efficiency and customer service.

Maintain a lean and efficient cost structure to continue increasing profitability

The Company intends to lever its operational efficiencies to consistently improve its profitability. In particular, the Company intends to generate further cost savings by continuously working to increase productivity, optimise liquidity and engage in value creating projects, and aims to take a leadership position in bringing standardised, cost efficient operations to the region. The Modernisation Project is an important project in achieving this strategic goal, which, amongst other key objectives, aims to reduce the Company's operating costs gradually by its completion.

Furthermore, the Company plans to continuously promote employee efficiency and know-how through staff optimisation and ongoing training programmes at all levels of the Company's workforce. Management believes that a common understanding at all levels of the organisation of the strategic objectives and business principles of the Company is essential for the smooth implementation of the Modernisation Project. To achieve this, the Company promotes business education among its mid-level technical staff and engages lower-level managers in the decision-making process, while incentivising employees through the New Bonus Scheme, a group-wide, value-creation oriented bonus scheme.

Management believes that the Company can achieve further cost savings by leveraging its position as one of the leading railways in the region. As one of the largest customers to railcar and locomotive construction factories, wooden and concrete sleeper producers and energy suppliers, management believes that the Company enjoys strong bargaining power with its suppliers and is able to exert significant influence over all industry participants. The Company uses these attributes to achieve cost savings and promote efficiency improvements in the industry.

Management also aims to make the Passenger SBU profitable in the medium term. The Company is actively working to enhance passenger customer service and improve passenger train speed and comfort in order to rebalance the passenger mix and attract additional higher-paying passengers, with the ultimate aim of increasing average revenue per customer at above the inflation rate.

Develop and modernise its infrastructure

Management plans to continue improving the efficient use of its assets, including by continuing to make substantial investments to further develop and modernise its infrastructure. The Company will supplement its own efforts by engaging outside experts where appropriate. As a result of the Modernisation Project, the Company expects diminished maintenance and operating costs and an extended life-cycle of certain of its infrastructure assets. Currently, the Company believes it possesses significant flexibility in terms of capacity. The Company's objectives are to match development of its rail network infrastructure with its planned volume growth over the next twelve months, and, longer term, to match investments in rolling stock with currently evolving volume development over the next three to five years.

Relationship with the Government

The Company is controlled by the State, which holds 74.5 per cent. of its shares in the Company directly. These shares are controlled by the EMA, an agency of the MESD. The State holds the remaining 25.5 per cent. of the shares in the Company indirectly through the PF, which is itself 100 per cent. directly owned by the State. The Company provides annual reports to the GMS in respect of the Company's performance and activities and must obtain the approval of the GMS for certain matters, such as approval of annual accounts, borrowings in excess of one per cent. of the Company's authorised capital and capital-related measures (such as dividend payments).

The Company is wholly owned by the State (directly or directly and indirectly through the PF), which has the power, in its capacity as shareholder, among other matters, to replace the members of the Supervisory Board and elect new members and influence the Company's operational and financial decisions, including the payment of dividends. See "*Shareholders and Management*" and "*Risk Factors—Risks Related to the Company's Business—The Company is wholly owned by the State which could act inconsistently with the best interests of the Noteholders*".

Management believes that the Government considers the Company to be a strategically important national asset and that the Company's railway network forms an important part of Georgia's economic and social infrastructure. Due to the Company's status as a strategically important national asset, the State intends to retain at least 51 per cent. of the shares in the Company if it decides to sell any shares in the Company in the future.

The Government has established the State Transportation Committee with the objective of discussing all major transport issues within the country, and to make strategic decisions concerning the development of the transportation industry, including the national railway. This Committee is headed by the Prime Minister; its other members include the Minister of Finance, the Minister of Economy and Sustainable Development, the Minister of Infrastructural Development, the

Chief Executive Officer of the Company, the Head of the Roads Department and representatives of Black Sea port operators. Even in areas of the Company's business that do not require formal Government consent or approval, the Government may advise on decisions of the Company's management through the policies of the State Transportation Committee. Moreover, Article 3 of the Constitution of Georgia provides that the railways fall within the "exclusive competence" of the highest State bodies of Georgia. See "*Risk Factors—Risks Related to the Company's Business—The Georgian Government has the power to start establishing tariffs and could otherwise require the Company to operate on a non-commercial basis*" and "*Risk Factors—Risks Related to the Company's Business—The Company is wholly owned by the State which could act inconsistently with the best interests of the Noteholders*".

History of the Company

In 1865, the Transcaucasian Railway Company, headquartered in Tbilisi, began construction of its railway network, a portion of which comprised the Company's predecessor network. In 1871, the Transcaucasian Railway, which ran through Georgia, Armenia and Azerbaijan, commenced operations. By 1883, a connection was made between Tbilisi and Baku. In the 1890s, a tunnel was constructed, which allowed the rail transportation of oil from Azerbaijan through Georgia. The Transcaucasian Railway ultimately became part of the much larger Soviet rail network, which was a core transportation component of the Soviet economy. The Soviet rail network functioned as part of a command economy emphasising regional specialisation and interdependence in production, rather than the immediate local transportation needs of the economy. At its peak in the late 1980s, the portion of the Transcaucasian Railway in Georgia carried more than triple the freight volume and four times the passenger volume than it does today. Accordingly, the Company believes that it has substantial capacity for future growth.

Following the dissolution of the Soviet Union in 1991, the assets of the Transcaucasian Railway Company were allocated to the national railroad companies of Georgia, Armenia and Azerbaijan, and an independent Georgian railway was formed in 1992. In 1993, the Georgian railway network was a founding member of TRACECA, an agreement to provide EU technical assistance to develop an east-west corridor from Europe, across the Black Sea through the Caucasus and the Caspian Sea to Central Asia.

The Company was established as a limited liability company on 21 December 1998 pursuant to the *Law on Entrepreneurs,* Georgia's basic companies law.

After the current management joined in 2005, the Company launched the 2005 Restructuring Programme based on the proposals of an independent consultant. The 2005 Restructuring Programme transformed the Company into a more efficient, vertically-integrated company with a stronger focus on its core operations. As part of the 2005 Restructuring Programme, which was completed in 2008, the Company separated its operations into the three SBUs, each with separate reporting functions; reorganised the corporate and management systems of the Company; disposed of substantially all of the Company's non-core and non-performing assets in order to realign the Company's asset base; invested in the refurbishment of its assets, particularly rolling stock and track; and conducted efforts to increase the profitability and cash-generating potential of the Company.

In July 2010, the Company issued the 2010 Notes, which are U.S.$250 million 9.875 per cent. notes that mature in 2015. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—2010 Notes Tender*" for a description of the 2010 Notes Tender and "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Liquidity and Capital Resources—Borrowings—2010 Notes*".

Pursuant to Government Resolution No. 230 of 2 June 2011 "On Approval of JSC Partnership Fund Charter and Capital Formation", on 25 October 2011, the Government transferred 24.0 per cent. of its shares in the Company, by way of capital contribution, to the PF.

The Company changed its corporate form from that of a limited liability company and was re-registered as a joint stock company under the *Law on Entrepreneurs* on 12 April 2012 pursuant to Order No. 1-3/269 of the Enterprise Management Agency (the "**EMA**") dated 12 April 2012, approving the Charter and the consent of the PF dated 12 April 2012 and the MESD dated 12 April 2012.

Pursuant to Government Resolution No. 789 of 30 April 2012 on "*Contributing the Shares of JSC "Georgian Railway" owned by the State into the capital of JSC Partnership Fund"*, on 3 May 2012 the State transferred additional shares in the Company representing 1.5 per cent. of the Company's authorised capital, by way of capital contribution, to the PF.

The Rail System

As Georgia's only railway operator, the Company owns and operates the national freight and passenger railway network, including the tracks, terminals, other infrastructure and rolling stock, as well as the land adjoining the tracks. As at 31 December 2011, the rail assets of the Company included:

- a railway network of 1,326 kilometres, of which 94 per cent. was electrified, including a 527 kilometre fully-electrified mainline from the Azerbaijan and Armenian borders to the Black Sea (of which 293 kilometres was double-track line);
- 114 stations; and
- significant rolling stock, including 95 working electric freight locomotives, 44 working diesel freight/shunting locomotives, 20 working passenger locomotives, 8,122 working freight cars, 98 working passenger railcars and 69 working EMUs.

The Company's mainline railway network comprises a key segment of the TRACECA corridor, forming a critical link in the shortest route from the Caspian Sea and Central Asia to the Black Sea and the Mediterranean basin. Three of the Company's lines terminate at the Black Sea, at the Georgian ports of Batumi, Kulevi and Poti. Access to these ports allows easy on-shipment of transit cargo to the Mediterranean basin and Europe.

The Company's operations are governed by the Railway Code, which sets forth the rights, obligations and responsibilities of parties involved in railway transportation in Georgia, including the Company, although the Company sets its own tariffs. See "—*Regulation*".

Business Operations

The Company provides principally freight, as well as passenger, services. It also operates its own infrastructure services. The Company's operations are organised into three strategic business units:

- *Freight SBU*: the Freight SBU consists of freight traffic (transportation and handling) and freight car rental services;
- *Passenger SBU*: the Passenger SBU primarily transports passengers within Georgia; and
- *Infrastructure SBU*: the Infrastructure SBU operates, maintains and manages the Company's principal infrastructure assets.

Each SBU is managed by a separate member of the Board of Directors, who is responsible for the performance of the relevant SBU and who reports directly to the Chief Executive Officer of the Company. Each of the SBUs, in turn, maintains its own administrative divisions, and the Freight SBU and Passenger SBU each have their own finance director.

For the year ended 31 December 2011, the Freight SBU and the Passenger SBU accounted for 95.3 per cent. and 3.7 per cent. respectively, of the Company's total revenue of GEL 477.4 million, as compared to 93.4 per cent. and 4.3 per cent., respectively, of the Company's total revenue of GEL 404.7 million for the year ended 31 December 2010. The Infrastructure SBU has a cost centre providing services only to the Freight SBU and the Passenger SBU. It does not conduct business with third-party customers. The Company also generates revenue by selling scrap metal from ongoing maintenance and repair and by leasing real estate to third parties, including at the Central Tbilisi Station.

Freight SBU

The Company's Freight SBU provides two types of freight service: (i) freight traffic, which consists of freight transportation and freight handling services; and (ii) freight car rental. Freight transportation services encompass the transportation for customers of cargoes along the Company's railway network. Freight handling services, including railcar marshalling and delivering freight to and from customer facilities, are provided at stations that provide commercial freight services. Freight car rental includes leasing railcars to the Company's customers, including foreign railway companies who may choose to utilise the Company's railcars on freight routes through their countries, and leasing locomotives to other railway companies outside Georgia.

Responsibility for train dispatching, one of the key operations in a railway business, lies with the Freight SBU. Dispatch personnel schedule and, in the event of a delay, reschedule all freight and passenger trains. Although dispatching covers both freight and passenger services, management believes that placing the dispatching function within the Freight SBU promotes efficiency given the importance of freight transportation to the Company.

The Freight SBU is the principal source of the Company's revenue, accounting for 95.6 per cent., 95.3 per cent., 93.4 per cent. and 91.4 per cent. of the Company's total revenue for the three-month period ended 31 March 2012 and for the years ended 31 December 2011, 2010 and 2009, respectively.

Freight Composition

The Freight SBU transports both liquid and dry cargoes. Liquid cargoes, which are crude oil and oil products (including, *inter alia*, petrol, bitumen, diesel, fuel and liquid natural gas), accounted for 52.0 per cent. and 57.5 per cent. of the Company's total freight transportation volumes in the years ended 31 December 2011 and 2010, respectively. Crude oil transported by the Company principally originates in Kazakhstan and Azerbaijan, while a significant percentage of oil products (approximately 66.5 per cent. in the year ended 31 December 2011) originates in Azerbaijan and Turkmenistan. Management believes that a significant percentage of transit oil products that it ships west-bound is destined for European markets. The Company also transport higher-grade oil products from European markets to Georgia, Azerbaijan and Armenia. Transit of crude oil across the Company's rail network is an alternative to oil pipelines. Of the Company's liquid cargoes, transit shipments accounted for 87.6 per cent. and 89.5 per cent. in the years ended 31 December 2011 and 2010, respectively.

The Freight SBU transports various dry cargoes, including, *inter alia*, ores, construction freight, ferrous metals and scrap and grain, with no major concentration on any single type of freight. Other dry cargo includes cement, sugar, and industrial freight. Dry cargo is more diversified than liquid cargo among local, export, import and transit shipments, although, as is the case with liquid cargoes, transit shipments are also the largest component of dry cargo transportation volumes, accounting for 35.5 per cent. and 35.0 per cent. in the years ended 31 December 2011 and 2010, respectively. Construction materials transported by the Company mostly originate in Georgia and are transported within Georgia, and also to Armenia and Azerbaijan. Ores transported by the Company originate principally within Georgia, and are transported within Georgia and also to the Black Sea ports. Grain and sugar transported by the Company are mainly imports into Georgia and Georgian exports to Armenia, as well as, to a lesser degree, transit shipments. Metals transported by the Company include aluminium, bauxite and other aluminium products and their regional trade is driven principally by the requirements and output of an aluminium factory in Tajikistan.

The following table sets forth breakdown of the Freight SBU's freight transportation volumes, by type of freight transported, for the periods indicated:

	For the year ended 31 December									
	2011		2010		2009		2008		2007	
	(million tonnes)	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*
Liquid cargoes	**10.5**	**52.0**	**11.5**	**57.8**	**9.7**	**56.7**	**10.1**	**47.6**	**11.5**	**51.8**
of which:										
Crude oil	*5.4*	*26.8*	*6.3*	*31.7*	*5.2*	*30.4*	*4.9*	*23.1*	*6.5*	*29.3*
Oil products(1)	*5.1*	*25.1*	*5.1*	*25.6*	*4.5*	*26.3*	*5.2*	*24.5*	*5.0*	*22.5*
Dry cargoes	**9.6**	**48.0**	**8.5**	**42.7**	**7.4**	**43.3**	**11.1**	**52.4**	**10.7**	**48.2**
of which:										
Ores	*1.9*	*9.6*	*1.6*	*8.0*	*1.1*	*6.4*	*2.2*	*10.4*	*1.9*	*8.6*
Construction freight	*1.6*	*8.1*	*1.2*	*6.0*	*1.1*	*6.4*	*1.6*	*7.5*	*1.8*	*8.1*
Grain	*1.2*	*6.2*	*1.4*	*7.0*	*1.1*	*6.4*	*1.0*	*4.7*	*1.4*	*6.3*
Ferrous metals and scrap	*1.2*	*5.8*	*1.0*	*5.0*	*0.8*	*4.7*	*1.0*	*4.7*	*1.0*	*4.5*
Chemicals and fertilisers	*0.5*	*2.6*	*0.4*	*2.0*	*0.4*	*2.3*	*0.4*	*1.9*	*0.4*	*1.8*
Cement	*0.5*	*2.5*	*0.4*	*2.0*	*0.7*	*4.1*	*1.5*	*7.1*	*0.9*	*4.1*
Sugar	*0.5*	*2.7*	*0.6*	*3.0*	*0.5*	*2.9*	*0.6*	*2.8*	*0.7*	*3.2*
Industrial freight	*0.5*	*2.3*	*0.5*	*2.5*	*0.6*	*3.5*	*1.4*	*6.6*	*1.1*	*5.0*
Other	*1.7*	*8.3*	*1.4*	*7.0*	*1.1*	*6.4*	*1.4*	*6.6*	*1.5*	*6.8*
Total	**20.1**	**100.0**	**19.9**	**100.0**	**17.1**	**100.0**	**21.2**	**100.0**	**22.2**	**100.0**

(1) Oil products include products such as petrol, bitumen, diesel fuel and liquefied natural gas (LNG).

For information in respect of the Freight SBU's freight transportation volumes, by type of freight transported, in the first five months of 2012, see "*Management's Discussion and Analysis of Results of Operations and Financial Condition*; *Current Trading and Prospects; Trends—Trends in Freight Volumes*."

The following table sets forth the primary direction of certain cargo transported by the Freight SBU:

Liquid cargoes	
Crude oil	From Azerbaijan to Black Sea ports
Oil products	From Azerbaijan to Black Sea ports and Georgia; from Black Sea ports to Afghanistan, Georgia and Armenia
Dry cargoes	
Ores	From Georgia to Black Sea ports
Construction freight	Domestic
Ferrous metals and scrap	From Georgia, Armenia and Azerbaijan to Black Sea ports
Grain	From Black Sea ports and Kazakhstan to Georgia and Armenia
Chemicals and fertilisers	From Georgia to Black Sea ports
Cement	From Georgia to Azerbaijan and Central Asia
Industrial freight	Domestic
Sugar	From Black Sea ports to Azerbaijan and Georgia

The following table sets forth a breakdown of the Freight SBU's freight transportation volumes by destination of freight transported for the periods indicated:

	For the year ended 31 December							
	2011		**2010**		**2009**		**2008**	
	(million tonnes)	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*
Liquid cargoes	**10.5**	**52.0**	**11.5**	**57.8**	**9.7**	**56.7**	**10.1**	**47.6**
of which:								
Local	*0.4*	*1.8*	*0.2*	*1.0*	*0.04*	*0.2*	*0.04*	*0.2*
Export	*0.05*	*0.2*	*0.1*	*0.5*	*0.6*	*3.5*	*0.04*	*0.2*
Import	*0.9*	*4.4*	*1.0*	*5.0*	*1.0*	*5.8*	*0.9*	*4.2*
Transit	*9.2*	*45.5*	*10.2*	*51.3*	*8.7*	*50.9*	*9.1*	*42.9*
Dry cargoes	**9.7**	**48.0**	**8.5**	**42.7**	**7.4**	**43.3**	**11.1**	**52.4**
of which:								
Local	*2.6*	*13.1*	*2.0*	*10.1*	*1.7*	*9.9*	*2.4*	*11.3*
Export	*1.5*	*7.7*	*1.4*	*7.0*	*1.3*	*7.6*	*1.5*	*7.1*
Import	*2.0*	*10.2*	*2.1*	*10.6*	*1.7*	*9.9*	*2.6*	*12.3*
Transit	*3.4*	*17.0*	*3.0*	*15.1*	*2.7*	*15.8*	*4.7*	*22.2*
Total	**20.1**	**100.0**	**19.9**	**100.0**	**17.1**	**100.0**	**21.2**	**100.0**

Management is seeking to increase profitability by further diversifying the types of cargoes that the Company transports. For example, the Company launched a container transportation line of business in 2009. Containerisation contributes to the diversity of dry cargo that the Company is able to transport, including for example, cotton products, grains and refrigerated products. Key dry cargo transported in containers has recently been construction materials, ferrous metals and scrap and frozen food. The Company plans to continue to adapt its fleet to the transportation of containers. The Company aims to benefit from the increasing containerisation in the region. For example, it has negotiated the transhipment of grain in containers from Kazakhstan.

The following table sets forth information in respect of the volumes of freight transported in containers for the periods indicated:

	For the year ended 31 December		
	2011	2010	2009
	(million tonnes, except as noted)		
Liquid cargoes	**10.5**	**11.5**	**9.7**
Dry cargoes	**9.7**	**8.5**	**7.4**
of which:			
Container cargoes[(1)]	*0.7*	*0.7*	*0.5*
Total cargoes	**20.1**	**19.9**	**17.1**
Container as per cent. of total cargoes *(per cent.)*	3.7	3.4	2.6
Container as per cent. of dry cargoes *(per cent.)*	7.6	7.9	6.1

(1) For the year ended 31 December 2011, ferrous metal and scrap and construction materials accounted for approximately 25.6 per cent. and 17.7 per cent., respectively, of container cargoes transported.

To foster containerisation, Railway TransContainer LLC, the Company's wholly owned subsidiary (see "*—Subsidiaries and Affiliates*"), has built and currently operates the Tbilisi Container Terminal (capacity: 25,000 TEU). Railway TransContainer LLC also owns land in Batumi and Poti on which it may construct additional container terminals. Management estimates that the capital expenditure to construct this infrastructure in Batumi is approximately GEL 3.5 million (expected capacity: 28,000 TEU). GEL 2.4 million (expected capacity: 35,000 TEU) has been budgeted for the Poti Terminal, including the related rolling stock to service the terminals. Construction of the Poti Terminal is underway and is expected to be completed in the third quarter of 2012. During the period 2013-2016, the Company plans to invest approximately GEL 4.1 million for the construction of container terminals and related infrastructure equipment.

Currently, the Company is only constructing container terminals in Georgia. However, it is undertaking a feasibility study to help it assess whether to invest in container infrastructure across the regional rail corridor. The study is expected to be completed in 2012. Management believes that there may be a market for container infrastructure in Kazakhstan, Turkmenistan and Uzbekistan, although, pending the outcome of the study, it does not currently view the construction of container terminals and related infrastructure as a core business. As a result, although the Company intends to continue to take steps to augment its transportation capabilities through containerisation, management's current plans do not include long-term ownership of container terminals or related infrastructure.

Freight Car Rental

Freight car rental includes leasing railcars to the Company's customers, including foreign railway companies who may choose to utilise the Company's railcars on freight routes through their countries, and leasing locomotives to other railway companies outside Georgia.

The Company has over different periods leased up to eight locomotives at a time to Azerbaijan Railway. The terms of the leases, which generally run for six-month periods, have historically been automatically renewed, and the Company has received no indications that renewals for locomotives currently leased will cease in the future.

Freight Rolling Stock, Repair and Maintenance

The Freight SBU manages the freight rolling stock in use on the Company's network. Customers can use Company-owned railcars, as well as either their own railcars or third-party railcars, which can be connected to Company-owned locomotives. A significant proportion of the Company's freight volumes (60.8 per cent. in 2011) was transported on rolling stock owned by other companies or customers.

The following table sets forth the Freight SBU's active, working and serviceable rolling stock assets as at the dates indicated.

	As at 31 December								
	2011			2010			2009		
	active(1)	*working*(2)	*serviceable*(3)	*active*(1)	*working*(2)	*serviceable*(3)	*active*(1)	*working*(2)	*serviceable*(3)
Locomotives(4)	—	**139**	**171**	—	**143**	**175**	—	**146**	**178**
of which:									
Diesel(5)	—	*44*	*52*	—	*48*	*56*	—	*48*	*56*
Electric............	—	*95*	*119*	—	*95*	*119*	—	*98*	*122*
Railcars(4)	**6,983**	**8,122**	**10,526**	**6,602**	**7,659**	**10,359**	**6,294**	**7,910**	**10,412**
of which:									
Open top box car..................	*2,181*	*2,376*	*2,950*	*2,114*	*2,493*	*2,910*	*2,067*	*2,773*	*2,917*
Box car............	*954*	*1,375*	*1,583*	*887*	*1,107*	*1,577*	*854*	*1,125*	*1,576*
Tank car..........	*1,339*	*1,430*	*1,588*	*1,204*	*1,276*	*1,392*	*1,178*	*1,306*	*1,396*
Grain hopper	*1,101*	*1,052*	*1,112*	*1,107*	*1,109*	*1,112*	*1,064*	*1,110*	*1,111*
Platform car.....	*750*	*1,031*	*1,400*	*653*	*857*	*1,411*	*497*	*722*	*1,1,456*
Cement hopper.............	*396*	*453*	*580*	*364*	*412*	*573*	*341*	*420*	*573*
Refrigerator car..................	*118*	*156*	*693*	*120*	*182*	*603*	*142*	*201*	*603*
Other...............	*144*	*249*	*720*	*153*	*223*	*781*	*151*	*253*	*780*
Total.................	—	**8,261**	**10,697**	—	**7,802**	**10,534**	—	**8,056**	**10,590**

(1) The Company does not maintain specific records of the breakdown of "active" locomotives.
(2) Working rolling stock is rolling stock that can be used to transport freight either immediately or following minor repairs that can be done by the Company's maintenance staff before it can be put into service.
(3) Serviceable rolling stock includes, in addition to working rolling stock, locomotives and railcars that require capital repairs in order to be returned to "working" status.
(4) Does not include locomotives and railcars being scrapped or undergoing capital repairs. Scrap consists of locomotives and railcars that have reached the end of their useful lives, for which no further life extensions are possible, or which are damaged beyond repair or for which repair would not be economically feasible.
(5) Diesel locomotives are used mainly for shunting.

The following table sets forth the percentages of the Company's freight volumes transported on the Company's own fleet and that of third parties for the periods indicated:

	For the year ended 31 December		
	2011	2010	2009
		(per cent.)	
Company's fleet	39.2	38.3	40.3
Third party owned(1)	60.8	61.8	59.7

(1) In 2011 and 2010, approximately 17 per cent. of the volumes were transported in privately-owned railcars that belonged to owners in Georgia, Azerbaijan, Kazakhstan and Russia.

Management believes that its current rolling stock allows it to operate efficiently, provided that the required maintenance and capital repairs are performed. Management also believes that utilising existing rolling stock is significantly more cost-efficient than purchasing new rolling stock or leasing more modern equipment, as management estimates that the cost of capital repairs to extend the useful life of the Company's existing rolling stock is approximately one-third of the cost of acquiring new rolling stock. Given the spare capacity of its rolling stock fleet, management is wary of aggressively expanding the Company's fleet. If the Company does experience a shortage of specific railcar types, typically it addresses this shortage through a combination of capital repairs of rolling stock from inventory and selective acquisition of new railcars.

On 30 March 2012, the Company (as lessee) entered into the Tank Car Lease Agreement with AS Spacecom (as lessor) to lease up to 1,000 tank cars until 1 April 2015. Under the Tank Car Lease Agreement, the lessor is required to lease to the Company 425 tank cars within one month from the date of receiving a request from the Company. Upon the Company's request, the lessor is also required to provide up to a maximum of 575 additional tank cars within one month of the date of receiving such request. The daily lease price per tank car under the Tank Car Lease Agreement is U.S.$45.00. The Tank Car Lease Agreement may be terminated by the written consent of both parties and AS Spacecom may unilaterally terminate the Tank Car Lease Agreement in the event of failure by the Company to make a payment within 30 days of the due date.

As a result of the availability to the Company of an increased supply of tank cars, the Company expects liquid cargo transported by the Company to increase, which, in turn, it expects to have a positive impact on the Company's revenue from freight traffic. The Company also expects its revenue from freight car rental to increase for the same reason. The Company expects such benefits to outweigh the costs of the leasing arrangements.

As at 31 December 2011, the average age of the Freight SBU's working railcars was 27 years, as compared to 26 years as at 31 December 2010 and 2009.

Most of the Freight SBU's locomotives date from the Soviet period, having been commissioned by the Company's predecessor prior to 1991.

The following tables set forth the distribution of the Freight SBU's working railcars and locomotives, respectively, by age, as at 31 December 2011:

Age	
	(per cent.)
Less than 21 years	18
21 – 25 years	25
26 – 30 years	29
31 – 35 years	17
More than 35 years	11

Age	**Electric Locomotives**	**Diesel Locomotives**
	(per cent.)	
12 – 24 years	17	33
24 – 36 years	40	67
36 – 48 years	43	—

Management believes that the age of its working railcar and locomotive fleet is not representative of the quality or state of these assets, as the technical life of a railcar is extendable through capital repairs.

The following table sets forth the distribution of the Freight SBU's working locomotives, by the number of expected remaining operating years, as at 31 December 2011:

Operating years remaining	**Diesel locomotives**	**Electric locomotives**
Less than 7 years	5	6
8 – 10 years	2	19
11 – 13 years	3	27
More than 14 years	34	43
Total	**44**	**95**

The following table sets forth the distribution of the Freight SBU's working railcar fleet, by the expected remaining number of operating years, as at 31 December 2011:

Operating years remaining	
	(per cent.)
Less than 7 years	55
8 – 10 years	19
More than 11 years	26

Management estimates that the utilisation rate for working freight railcars was 60 per cent. for the year ended 31 December 2011, while management estimates that the utilisation rate for working freight locomotives was 80 per cent. for the year ended 31 December 2011. Utilisation rate is calculated as the total number of days railcars or locomotives, as the case may be, were available compared to the number of days they generated revenue. Based on data for the year ended 31 December 2011, management estimates that the utilisation rate for tank cars was approximately 86 per cent. and approximately 71 per cent. for grain hoppers. Platform cars and box cars were the most under-utilised during that period (approximately 34-45 per cent.), which management believes reflects the diversity of dry cargo transportation options.

Prior to 2011, the Company had to acquire certain railcars outside of Georgia. The Company is now able to source all types of railcars domestically. The Company recently signed a pilot contract with a domestic manufacturer, Wagon Construction Company LLC, for the acquisition of 185 oil tank cars for an aggregate purchase price of CHF 14.1 million (approximately GEL 26.1 million), which is to be paid in Lari. As at 31 March 2012, all of the oil tank cars had been delivered.

The Company's rolling stock undergoes regular maintenance and repair. The Company's maintenance and repair work falls into two main categories: (i) scheduled repairs carried out according to current technical standards in the region and applicable regulations; and (ii) unscheduled repairs carried out according to the condition of railcars. Scheduled repairs are carried out on the basis of either the period of operation or the mileage of operation. The Company's rolling stock is generally inspected on a regular basis before loading, after unloading and during transportation through freight stations.

Under Company procedures, the Company's maintenance staff performs routine depot repairs two to three years on average after manufacturing (depending on the usage and condition of the railcar) and, thereafter, once every two years. In the middle of the useful life of a railcar, the Company performs capital depot repairs. After the end of its initially expected useful life, the Company currently uses third-party providers to perform capital repairs with life extensions (generally, by approximately 50 per cent. of the expected useful life). Routine depot repairs are still performed after life-extensions. After this extension ends, it is possible to make a similar extension with third-party providers a second time. When the second extended useful life ends, the Company may still make two further life extensions of five years each.

Unscheduled repairs are driven by the technical condition of the railcar and are directly related to the term and intensity of operation. In addition, the Company's railcars receive routine technical inspections, as a result of which minor repairs are performed at repair shops throughout the Company's network.

The following table sets forth the distribution of the Freight SBU's working railcar fleet, by the remaining number of operating years, if capital repairs with life extensions were to be made to the fleet, as at 31 December 2011:

Operating years remaining	*(per cent.)*
16 – 20 years	17
21 – 25 years	32
26 – 30 years	25
More than 30 years	26

Freight Tariffs

Although rail transportation in Georgia is a statutory monopoly, the Company's pricing policies are not subject to direct Government regulation. Under the Railway Code, the State has the power to establish tariff policies through a Rail Transport Authority. To date, however, the State has not established any such authority and the Company is not aware of any plans of the State to do so. Accordingly, as at the date of this Prospectus, the Company is not subject to any mandatory tariffs. Instead, pursuant to the Railway Code, it sets its own tariff policy independently for all types of services, including tariffs for freight transportation, freight transportation-related services and passenger services. See "*—Regulation*".

The Company has a written tariff policy specifying methods and formulas for determining the various tariffs applicable to its services. The Company publishes this policy on its website. The Company provides various services, with each activity having its own tariff, including:

- transportation tariffs, based on transportation from one station to another within Georgia;
- a station charge, which is for providing services, railcars or locomotives to support the loading or unloading of cargo at the relevant station, as well as for services such as documentation, rolling stock usage and rail-track occupation if third party railcars are used; and
- additional station charges, such as:
  - storage fees, incurred in 24-hour increments, referred to as "demurrage", if customers fail to unload a railcar within 24 hours of arrival at its agreed destination;
  - fees for providing additional diesel locomotives for manoeuvring if necessary for cargo loading/unloading; and
  - fees for cargo loading and unloading operations.

The tariff policy is reviewed and modified annually in light of changes in the Company's strategic goals, market environment and industry, as well as domestic and global economic developments.

Tariffs for freight transportation are based on the International Rail Transit Tariff decided among the signatories to the Tariff Agreement, although base tariffs established under the Tariff Agreement are not binding and the parties may vary them during the year. In addition to the Company, parties to the Tariff Agreement include the railway companies of CIS member states Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan, as well as the railway companies of Lithuania, Latvia and Estonia. The parties to the Tariff Agreement hold conferences each autumn, at which they present their tariff plans for the next year. The Company's final tariffs are based on various factors, including the type and weight of the cargo, the distance over which the cargo is carried and any discounts that may be applied at the Company's discretion.

For all periods under review in this Prospectus, the Company has quoted its tariffs in Swiss Francs only, except for tariffs for freight services, which, since 1 February 2012, the Company quotes in U.S. Dollars. The Company made this change due to the volatility of the exchange rates between the Swiss Franc and other currencies and also to better align costs and revenues for its customers and suppliers, which mainly trade in U.S. Dollars or Lari. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Change in freight tariffs and volume-based discounts.*"

Although tariffs are now set in U.S. Dollars, under Georgian law, Georgian-resident companies must pay in Lari. To the extent that the Company agrees a prepayment system with a client, the relevant client will prepay at a rate of exchange as determined by the Company on a daily basis. This exchange rate is generally several points higher than the official exchange rate set by the NBG on that day. The rate is published on the Company's website.

Unlike Georgian-resident companies, non-resident companies may either pay in foreign currency or in Lari. Regardless of the currency of payment, payments due from clients are quoted in U.S. Dollars. Customers are required to pay all amounts billed for transportation and station services before the Company provides the related services, except that fees for demurrage are not, by definition, paid in advance.

The following table sets forth information in respect of the Company's freight tariffs, by type of freight, for the periods indicated:

	For the year ended 31 December				
	2011	**2010**	**Change 2011 vs. 2010**	**2009**	**Change 2010 vs. 2009**
	(CHF)		*(per cent.)*	*(CHF)*	*(per cent.)*
Average Tariffs[(1)]					
Crude oil	18.0[(2)]	14.2	26.8	13.9	2.2
Oil products	34.2[(3)]	32.1	6.5	31.9	0.6
Dry cargo	39.3	40.8	(3.7)	42.3	(3.5)[(4)]

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(1) Average tariffs are calculated as freight traffic revenue (not including any handling charges) per thousand tonne-kilometre. The Company uses a detailed formula for each individual transportation order that takes into consideration factors including the type and weight of freight and the distance over which the cargo is carried. Amounts stated are CHF per 1,000 tonne-kilometre, unless otherwise indicated.

(2) Effective 1 April 2011, the Company reduced the discount it offers on the transport of crude oil by 33.0 per cent.

(3) Effective 1 April 2011, the Company reduced the discount it offers on the transport of oil products by 23.0 per cent.

(4) The 3.5 per cent. decrease in 2010, as compared to 2009, was the result of the Company changing the mix of products transported, and was not the result of a decision of the Company to decrease tariffs applied to such products.

To attract additional volumes, the Freight SBU offers a volume-based discount to liquid cargo transit customers whose annual volumes exceed four million tonnes per day. Based on the Company's 2011 tariffs, this discount decreases tariffs to CHF 7.8 for each tonne of crude oil transported and to CHF 10.35 for each tonne of oil products transported. As at 31 December 2011, the Company had only one liquid cargo transit customer who qualified for this discount, although in previous years up to two customers have so qualified. The Company believes that the terms of this discount help the Company to compete with pipelines and other competitors. See "*Description of the Company's Business—Business Operations—Freight SBU—Freight Competition—Competition from alternative rail routes*". The Company offers a 15 per cent. discount on its freight tariffs to customers who transport cargo with their own railcars and use the Company's services for infrastructure and locomotives.

With effect from April 2011, the Company reduced the discount it offers for its tariffs on oil and oil products, which the Company expects will help finance the acquisition of additional tank cars. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Tank Car Lease Agreement*". In the three months ended 31 March 2011, average tariffs for crude oil and oil products were CHF 14.5 and CHF 31.1 per thousand tonne-kilometre, respectively, while for the year ended 31 December 2011 (following the reduction in the volume-based discount it offers) average tariffs for crude oil and oil products were CHF 18.0 and CHF 34.2 per thousand tonne-kilometre, respectively. With effect from 1 February 2012, the Company reduced the volume-based discount it offers for the transport of oil and oil products by U.S.$0.50 per tonne transported. See also "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Current Trading and Prospects; Trends—Change in freight tariffs and volume-based discounts*".

Tariffs for dry cargo are typically higher than for liquid cargo. While certain grades of crude oil can be transported through the pipelines, alternative modes of dry cargo transportation along the TRACECA corridor are more limited. The Company also offers volume-based discounts for dry cargo customers. The Company offers two types of dry cargo discounts, one related to transit cargo and one related to refrigerated cargo. Customers whose annual volumes of dry cargo exceed 100,000 tonnes on routes to the Batumi and Poti ports through the Gardabani station (a transit route) receive a 10 per cent. discount. With respect to refrigerated cargo, customers whose annual volumes exceed 50,000 tonnes receive either (i) a 50 per cent. discount if the cargo is shipped in Company-owned refrigerator railcars or (ii) a 20 per cent. discount if the cargo is shipped in refrigerator railcars owned by other entities. As at 31 December 2011, four customers had qualified for dry cargo discounts.

Freight Customers

The Freight SBU accepts freight from both direct customers and freight forwarders. The Freight SBU works with freight forwarders in order to expand its marketing reach and to increase and diversify its customer base. As the Freight SBU does not generally enter into long-term contracts with customers it serves through freight forwarders, it is able to maintain operational flexibility and change the prices in accordance with market conditions. All of the Freight SBU's customers, whether direct or through freight forwarders, are required to pay for transportation and station services in advance, except that payments for demurrage are not, by definition, paid in advance.

The owners of cargo transported by freight forwarding companies through the Company's network include various "blue-chip" companies, such as BP, Chevron, ExxonMobil Corporation, SOCAR and KMG. As these companies often need to transport cargo through several countries using different modes of transportation, many of them prefer to use freight forwarders. Freight forwarders provide end-to-end transportation services across various transport routes and contract with the Company on such companies' behalf. In both 2011 and 2010, one customer of the Freight SBU (a freight-forwarder) represented approximately 30 per cent. of the Company's total revenue. However, management believes that the Company's revenue is not dependent on any single customer in respect of its services. Management believes that, in the case of potential distress or default by a freight forwarding company, the cargo transported by that forwarder on behalf of its customers can generally be easily absorbed by its competitors or through direct contracts with the Company at no loss to the Company.

The Company generally does not enter into long-term contracts with its customers, and does not have long-term contracts with the ultimate owners whose cargo is aggregated by freight forwarders. The Company usually enters into short-term standard form contracts with its freight forwarders and direct freight owner customers for the transportation of cargo. These contracts typically state the amount of cargo to be transported and the tariffs applied, which are based on the Company's general tariff policy. The contracts generally permit either party to terminate the contract on one month's prior written notice and are typically concluded for a period of one year. In 2006, however, the Company entered into a long-term framework agreement with a freight forwarder in relation to the transportation of oil and oil products. Pursuant to this contract, the Company undertakes to transport 4.0 million tonnes of oil and oil products every year from or through Azerbaijan to a number of listed destinations. The tariffs applicable to such services are specified in the contract. This contract has a duration of ten years and has been amended twice to date to reflect changes in matters such as applicable tariffs, duration, destinations of services and the use of a third party's locomotive for transportation from Batumi station to the facilities of the Batumi oil terminal. See "*Risk Factors—Risks Related to the Company's Business—The Company provides its freight services to a limited number of customers*".

The following table sets forth the volumes of liquid cargo transported, by principal customers, for the periods indicated:

	For the year ended 31 December					
	2011		**2010**		**2009**	
	(million tonnes)	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*
Georgia Transit[1]	8.5	81.3	9.5	82.5	5.7	58.3
BSI Trans[1]	0.0	0.0	0.0	0.0	2.6	26.4
SOCAR Georgia Petroleum	0.7	6.5	0.5	4.7	0.4	4.4
Mika Georgia[1]	0.0	0	0.2	1.8	0.2	2.1
Wissol Petroleum Georgia	0.1	1.2	0.1	1.1	0.1	1.3
Lukoil Georgia	0.2	1.8	0.1	1.1	0.1	1.0
Kastor Plus LTD	0.1	1.1	0.1	1.1	0.1	1.4
Caucasus Railway Networks	0.3	2.8	0.3	2.9	0.0	0.0
Trans Rail	0.2	1.9	0.0	0.0	0.0	0.0
Others[2]	0.3	3.3	0.5	4.8	0.5	5.2
Total	**10.5**	**100.0**	**11.5**	**100.0**	**9.7**	**100.0**

(1) Freight forwarder.
(2) Consists of smaller freight forwarders and cargo owners.

The following table sets forth the volumes of dry cargo products transported, by principal customers, for the periods indicated:

	For the year ended 31 December					
	2011		**2010**		**2009**	
	(million tonnes)	*(per cent.)*	*(million tonnes)*	*(per cent.)*	*(million tonnes)*	*(per cent.)*
Pace Georgia[1]	1.0	10.1	1.2	14.2	0.8	10.2
BSI Trans[1]	0.0	0.0	0.6	6.7	0.6	7.5
Saqcementi[2]	1.1	11.5	0.6	7.6	0.5	6.7
Energy Invest	0.0	0.0	0.4	4.8	0.4	5.5
Georgian Cement[2]	0.6	6.4	0.5	5.3	0.4	4.8
Georgian Manganese	0.3	3.1	0.3	4.0	0.3	4.6
Access Trans Georgia	0.7	6.7	0.0	0.0	0.0	0.0
Transford	0.5	4.7	0.0	0.0	0.0	0.0
Karat+	0.3	3.2	0.0	0.0	0.0	0.0
Others[3]	5.2	54.2	4.9	57.5	4.5	60.8
Total	**9.7**	**100.0**	**8.5**	**100.0**	**7.4**	**100.0**

(1) Freight forwarder.
(2) A subsidiary of Heidelberg Cement.
(3) Consists of smaller freight forwarders and cargo owners.

Freight Customer Relations, Sales and Marketing

The Company's main customer relations, sales and marketing activity in its freight business consists of on-going dialogues with freight forwarding companies and neighbouring railways to ensure competitive pricing for the TRACECA corridor. In turn, freight forwarding companies market the Company's services to potential customers.

The Freight SBU's Commercial Department is responsible for billing and other customer paperwork, and therefore tends to interact more regularly with customers than other departments. As a result, the Commercial Department generally acts as a link to customers and manages day-to-day customer relations. Senior representatives of the Freight SBU and, in some cases, the Company's management may oversee client relations with some larger customers. In addition, the Company has regular dialogue with various cargo owners to promote the rail corridor, discuss any customer-specific issues that owners may have and gain an understanding of expected volumes of transportation.

Freight Competition

Although the Company has a statutory monopoly on rail transportation in Georgia, it faces competition in respect of its freight transportation services from alternative means of transportation, particularly in respect of the transportation of crude oil. Within the region, freight transportation competition is generated from oil pipelines as well as alternative railway routes provided through Russia and Iran. The substantial majority of oil produced in the Caspian Basin is transported via the pipeline network. This network is dominated by the BTC and CPC pipelines and supplemented by a number of smaller pipelines and share of the Russian pipeline system made available to Caspian Basin oil production. In the transportation of dry cargo, railway transportation of freight also faces competition from road container transportation.

Competition from pipelines

As shown in the following table, the Company believes that there are four oil pipelines that compete directly with the Company in respect of the transportation of crude oil:

Pipeline	Route and capacity
Baku-Tbilisi-Ceyhan (BTC Pipeline)	Baku, Azerbaijan on the coast of the Caspian Sea to Ceyhan, Turkey on the coast of the Mediterranean Sea. The BTC Pipeline has a stated capacity of approximately 60 million tonnes per year.
Caspian Pipeline Consortium (CPC Pipeline)	Tengiz, Kazakhstan on the coast of the Caspian Sea to Novorossiysk, Russia on the coast of the Black Sea. The CPC Pipeline has a stated capacity of 28 million tonnes per year.
Baku-Novorossiysk	Baku, Azerbaijan on the coast of the Caspian Sea to Novorossiysk, Russia on the coast of the Black Sea. The Baku Novorossiysk had a reported capacity of 6 million tonnes per year in 2008, which is understood to be expandable to approximately 15 million tonnes per year.
Baku-Supsa	Baku, Azerbaijan on the coast of the Caspian Sea to Supsa, Georgia on the coast of the Black Sea. The Baku-Supsa Pipeline has a nominal capacity of 7.25 million tonnes per year, although it has recently been out of service.

The Company believes that the CPC Pipeline and the BTC Pipeline pose the most significant competition to its liquid cargo business. The opening of the BTC Pipeline in 2007 resulted in a negative impact on the Company's revenue from the transportation of oil and oil products in 2007 and 2008, which was only partially offset by increased oil exports from Kazakhstan transported by the Freight SBU and increases in the Company's tariffs. Prior to the impact of the global financial crisis, expansion projects were announced in respect of both the BTC and CPC pipeline. These projects have been delayed due to the impact of the global financial crisis. It is currently expected, however, that the capacity increases for the CPC Pipeline will be completed in 2015. Management does not expect that added pipeline capacity will result in a significant diversion of rail traffic or will further materially impact its competitive position or the revenue generated by its liquid cargo business. This is particularly in light of the transport diversification offered by the railway over pipelines. However, any political pressure on oil producers to use the BTC and CPC pipelines following the completion of any expansion project could result in the decrease in freight railway traffic. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition*".

The Company does not believe that either the Baku-Novorossiysk Pipeline or the Baku-Supsa Pipeline currently poses a significant competitive threat to it. In comparison to the BTC Pipeline and the CPC Pipeline, these pipelines can be considered as undersized, and the Baku-Novorossiysk pipeline traverses the North Caucasus region of Russia, which has had periodic episodes of instability in recent years.

Despite the competition posed by the pipelines, the Company believes that it is well-positioned to continue to attract significant volumes of oil and oil products for the following reasons:

- Pipelines cannot carry all grades of crude oil, and rail transport is an alternative for producers who produce grades of crude oil that cannot be transported through the pipelines or do not benefit from costs savings in using the pipelines. Crude oil gets mixed in pipelines, and pipelines are generally best suited for average grade oils. Low grade, high sulphur oil is generally not suitable for pipelines as it causes corrosion. Management believes that rail transport is the most viable alternative for high sulphur oil, which originates mostly in Kazakhstan. High grade Azeri-light oil, which has a low sulphur content, can technically be transported through pipelines. However, it would mix with lower grade oils and thereby decrease its quality. As a result, some Azeri-light oil has historically been transported by the Company in order to maintain its high quality. Oil producing countries seeking to diversify their oil transportation routes and end markets may also seek alternative modes of transport for liquid cargos. Furthermore, there is no current pipeline competition for refined petroleum products and heavy residual fuel oils cannot be transported by pipeline. Accordingly, management believe that rail is the most appropriate method of transportation for grades of crude oil not carried by pipelines, as well as refined petroleum products such as gas, kerosene, jet fuel and certain petroleum-based chemicals, that are not transported by pipeline at all.

- Both the BTC Pipeline and the CPC Pipeline have unused capacity. While expansion plans in relation to both pipelines had been announced, these are linked to the development of new oil fields and have been delayed due to market conditions. In addition, the continued flow of rail transport despite the presence of available oil pipeline capacity would suggest that the Company will be able to continue to attract significant volumes of oil.

- Smaller regional producers typically do not have guaranteed access to pipeline throughput, as they may experience difficulties in minimum quotas required in order to use the pipelines. This makes rail transport an attractive alternative for such producers. In addition, pipelines are typically built by a consortium of oil production companies, and in return for financing the construction of a pipeline, a consortium member will generally receive priority throughput access and prices that are lower than those offered to non-consortium members.

- Recent third-party investments in the Black Sea ports suggest the continued use of rail transportation. In 2010, transportation of oil to the Georgian Black Sea ports by rail represented approximately 11 per cent. of total westbound oil transportation in the Caucasus/Caspian region. Therefore, rail does not necessarily compete with pipelines but rather represents a diversification of transportation routes, which is important for oil operators in the region for risk management purposes.

Competition from alternative rail routes

There are also railway routes, which provide alternatives to the Company's rail network. In particular, these are the north route through Russia to the Baltic Sea and Northern Europe, the south route through Russia to Novorossiysk and the railway route through Iran. These include routes providing access or onward transportation to Aktau port in Kazakhstan, Turkmenbashi port in Turkmenistan, Makhachkala and Novorossiysk port in Russia, Bandar Anzali port in Iran and the Sea of Azov port in Ukraine.

The Company believes that these alternative railway routes do not pose significant competition to it for the following reasons:

- Due to the discounts offered by the Company to customers transporting high volumes of oil and oil products, management believes that the cost per tonne for the transportation of such products by rail from Baku to Batumi is significantly cheaper than that offered by its competitors on the route from Makhachkala to Novorossiysk. In addition, the railroad adjacent to the Novorossiysk port is typically frozen in winter, thus hindering traffic by railway for part of the year.

- The Company expects the proportion of freight originating in Kazakhstan and transported through Georgia to increase due to KMG's ownership of the Batumi Oil Terminal, as discussed above.

- Increased investment and modernisation of the Azerbaijan Railway, in particular of the railway track between Baku and the Georgian border, is expected to increase the volumes of freight traffic that can be transported via the route between Azerbaijan and Georgia.

- In February 2007, the governments of Georgia, Turkey and Azerbaijan signed an agreement in connection with the construction of a new Baku–Tbilisi–Kars railway line, which will transport both goods and passengers between Central Asia and Europe. Georgian Railway has been granted the exclusive right to operate the Georgian portion of the new line. Once open, the Company expects this line to attract cargo transportation business, which may currently use the alternative routes offered through Iran. The line is expected to be completed in 2013.

- The railway routes running through Iran may be less attractive than the Company's railway routes due to the strained political relations between Iran and western jurisdictions, as well as the longer distances of such rail routes.

Competition from other methods of transport

Competition from road transportation is generally only relevant in relation to container transportation. As in most countries, railway transportation is usually cheaper than road transportation only if the cargo is transported in bulk and for long distances. In Georgia, which is a relatively small country, local transportation of non-bulk cargo is usually cheaper by road. Whilst door-to-door transportation is an inherent advantage of road transportation, which the Company cannot provide, it cannot substitute for railway transport in bulk product transportation and in long distances. According to the MESD, cargo transported by road in 2010 totalled 0.6 billion tonne-kilometres, which is equivalent to only 10.0 per cent. of the Company's freight transportation volume in the same year.

The Company considers road transportation to be complimentary rather than posing a threat to its business and in 2009 established a subsidiary, Railway TransContainer LLC, to foster the increased containerisation of the region.

The Company plans to promote the containerisation of the Caucasus corridor by making strategic investments such as in its subsidiary, Railway TransContainer LLC, which built and operates the Tbilisi Container Terminal. The Company expects that containerisation can attract new customers and expand the range of cargoes transported. See "*—Strategy*" and "*—Subsidiaries and Affiliates*".

Passenger SBU

The Passenger SBU's primary activity is the transportation of passengers and, to a limited extent, unaccompanied luggage within Georgia. One of the Company's medium-term strategic objectives is to transform the Passenger SBU into a profitable operation by achieving increased revenue per passenger. To achieve this, the Company is taking a series of measures to improve average revenue per passenger. These measures include:

- introducing higher levels of service by investing in new, or improving existing, railcars;
- adjusting schedules with a view to optimising utilisation; and
- adjusting the segmentation of journey pricings, increasing the intervals for price zones from every 50 kilometres to every 120 kilometres.

In undertaking these measures, the Company aims to attract higher income commuters and other passengers who might otherwise travel by car.

The Passenger SBU accounted for 3.9 per cent., 3.7 per cent., 4.3 per cent. and 4.9 per cent. of the Company's total revenue in the three-month period ended 31 March 2012 and for the years ended 31 December 2011, 2010 and 2009, respectively. The Passenger SBU transported 3.3 million passengers in 2011, as compared to 3.2 million passengers in 2010 and 3.1 million passengers in 2009.

Passenger Rolling Stock, Repair and Maintenance

The following table sets forth the working and serviceable rolling stock assets of the Passenger SBU as at the dates indicated.

	As at 31 December			
	2011		2010	
	working	*serviceable*	*working*	*serviceable*
Locomotives[(1)]	20	25	18	22
of which:				
Diesel	*2*	*3*	*0*	*0*
Electric	*18*	*22*	*18*	*22*
EMUs	69	77	71	77
Railcars[(1)]	98	98	105	105
Total	**187**	**200**	**194**	**204**

(1) Does not include locomotives, EMUs and railcars being scrapped or intended for sale. Scrap consists of locomotives and railcars and EMUs that have reached the end of their useful lives; for which no further life extensions are possible; or which are damaged beyond repair or for which repair would not be economically feasible.

In connection with its strategy to make the Passenger SBU profitable in the medium-term, in 2010, the Company purchased three modern passenger trains for a total of GEL 16 million. Furthermore, in March 2011, the Company entered into a procurement agreement with one of China's largest train manufacturers for the purchase of five additional modern passenger trains. These five trains have a combined seat capacity of 1,500 seats. The trains are scheduled to be delivered in 2012-2013. The aggregate cost of these passenger trains is CHF 31.9 million (approximately GEL 59.1 million) and is to be paid in Swiss Francs. Management believes that the Company has sufficient railcars and rolling stock in its fleet to support the current and expected future demand of its Passenger SBU services.

The Passenger SBU's Railcar Repair Depot conducts all routine maintenance repairs of the Company's passenger railcars in-house. Third-party providers carry out almost all capital repairs.

Passenger Tariffs

As in the case of freight transportation tariffs, the Company is not subject to Government regulation in establishing prices for passenger transportation and luggage services. In many cases, however, passenger transportation tariffs are not determined by market forces due to the significant social importance to the State of providing affordable passenger transportation services. Accordingly, the Company has focused on decreasing passenger operating costs, while average passenger tariffs have remained relatively stable over the past three years, with fares unchanged for travel in older railcars.

The following table sets forth information in respect of the Company's passenger tariffs for the periods indicated:

	For the year ended 31 December		
	2011	**2010**	**2009**
		(Lari per passenger-kilometre)	
Average Tariff(1)	0.024	0.022	0.022

(1) Average tariffs are calculated as passenger traffic revenue per passenger-kilometre.

Tariffs for domestic transportation of passengers and luggage are approved by the Company's Board of Directors and are denominated in Lari. Tariffs for international transportation of passengers and luggage services within the CIS are determined at the CIS Rail Transport Tariffs Conference.

The Company offers three classes of passenger service, and tariffs are further differentiated between travel on modern or older trains. Tickets in the lowest class of rail service are generally less expensive than bus transportation. As at the date of this Prospectus, it is management's intention that any increases to tariffs will be made in line with the improvements in the Company's services, the provision of new modern trains and inflation and to make the Company's tariffs competitive with those for bus transportation and other passenger transportation services in Georgia, such as mini-buses. In respect of regional passenger traffic, where the majority of the passengers are from low-income households and are sensitive to price increases, it is management's intention to consider price increases only when new modern trains have been commissioned by the Company and for such tariffs to be in line with alternative travelling costs. See "*—Passenger Competition*".

In June 2012, the Board of Directors approved the introduction of discounts of up to 50 per cent. on student passenger fares. The Company currently intends to implement these discounts with effect from July 2012.

Passenger Customers

The Passenger SBU transported 3.3 million passengers in 2011, as compared to 3.2 million passengers and 3.1 million passengers in 2010 and 2009, respectively. The table below sets forth information in respect of the Company's passengers, by type of journey, for the periods indicated:

	For the year ended 31 December		
	2011	**2010**	**2009**
		(passengers, millions)	
Domestic	3.2	3.1	3.0
International	0.1	0.1	0.1
Total	**3.3**	**3.2**	**3.1**

Management also uses the number of passenger kilometres (the total number of kilometres travelled by all passengers during a given period) as a measure of volumes.

The following table sets forth the number of passenger kilometres for the periods indicated:

	For the year ended 31 December		
	2011	**2010**	**2009**
	(passenger kilometres, millions)		
Domestic	623.2	636.5	615.9
International	17.8	18.2	10.0
Total	**641.0**	**654.7**	**625.9**

Passenger Customer Relations, Sales and Marketing

The primary customer relations, sales and marketing activity in the Company's passenger business are points of sale for tickets. Passengers can buy tickets directly at the station before travel, aboard certain trains, through tourist agencies or via the internet. However, because a relatively small percentage of the Georgian population use the credit cards necessary to make internet purchases, the Company has also established points of sales, known as "Pay Boxes", where customers can buy tickets and locate detailed information about prices, availability and classes of travel. The Company is also planning to install ticket machines on certain trains and introduce pre-paid multi-travel cards.

Since July 2011, the Company has also maintained a customer call centre that handles approximately 600 calls per day.

Passenger Competition

The passenger railway transportation services offered by the Company faces competition from other modes of domestic transportation, principally buses, mini-vans and passenger automobiles, as well as, to a lesser degree, airplanes.

The types of transportation used by passengers in Georgia is generally determined based on their levels of income and general wealth and it is common for members of higher-income families to prefer to drive rather than travel on the railway or use other forms of passenger transportation.

An inherent advantage of transportation by road, whether by bus or mini-bus, is that it is often more direct and may be faster as the routes offered are not restricted by the location of railway tracks or stations. Since fares for bus and mini van travel are similar to passenger train fares, the passenger's choice is dictated largely by personal travel preferences and unique needs rather than factors within the control of the Company.

Infrastructure SBU

The Infrastructure SBU operates, maintains and manages the Company's principal infrastructure assets, including its track, embankments, signalling, land, electric power lines and equipment. The Infrastructure SBU is a cost centre providing services only to the Freight SBU and the Passenger SBU. It does not conduct business with third-party customers and management has no current intention for it to do so.

The principal aims of the Infrastructure SBU are to ensure safety and promote the efficient use of the Company's infrastructure assets and to decrease maintenance costs. The Infrastructure SBU promotes safety by setting speed and loading limitations on lines and at stations and by controlling signalling and blocking systems.

Infrastructure Assets

The main infrastructure assets of the Company as at 31 December 2011 included:

- a railway network of 1,326 kilometres, of which 94 per cent. was electrified including a 527 kilometre fully-electrified mainline from the Azerbaijan and Armenian borders to the Black Sea (of which 293 kilometres was double-track line);

- 1,369 bridges (mainline); and

- 55 tunnels.

The Company also had 114 stations as at 31 December 2011, although station management is the responsibility of the Freight SBU rather than the Infrastructure SBU.

As at 31 December 2011, the principal design characteristics of the railway network are as follows:

- the track gauge on the main lines was 1,520 mm; one small tourist branch line had a track gauge of 912 mm (see "*—Subsidiaries and Affiliates*");
- the design axle load on the main lines was 23.5 tonnes, while small branch lines had a lower limit per railcar; and
- the main-line tracks accommodated speeds of up to 65-90 kilometres per hour for passenger trains and 60-70 kilometres per hour for freight trains. In the gorge region, top speeds for both passenger and freight trains were significantly lower depending on the specific terrain but averaged approximately 55 kilometres per hour.

The Company expects to upgrade the design of its railway network in line with the recommendations of SYSTRA and SNCFI as a result of the completion of the initial design study for the Modernisation Project. Through these additional investments, the Company aims to increase freight capacity, increase passenger speeds and reduce operating expenses. See "*—Modernisation Project*".

Infrastructure Services

The Infrastructure SBU focuses on maintaining the Company's infrastructure assets in good condition. Management estimates that its existing infrastructure capacity is 28 million tonnes of freight per year. In 2011, the Infrastructure SBU made capital repairs (not including minor, non-technical repairs) to, or renovated, approximately 75 kilometres of track, as compared to capital repairs or renovations of approximately 32 kilometres in each of 2010 and 2009. During the two years ended 31 December 2011, approximately 99 kilometres of the track repaired or renovated were repaired or renovated in connection with the Modernisation Project. During the three years ended 31 December 2011, the Company paid GEL 807.7 million for the acquisition of property, plant and equipment, including rolling stock and equipment and to rehabilitate important infrastructure assets, including rail tracks, electric power supply lines and bridges and tunnels. This amount includes amounts spent on the Modernisation Project and the Bypass Project. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Liquidity and Capital Resources—Capital expenditures*".

Regulation

The Constitution gives special rights to the Government with respect to the railway. The railway is regarded as an asset of state importance and is expressly subject to special governance by State authorities.

The Railway Code

The primary legislative act concerning rail transport in Georgia is the Railway Code. The Railway Code sets forth the economic, legal, organisational and technological basis for the Company's activities and determines its status and role in the economy of Georgia. The Railway Code provides that the Company is Georgia's only railway operator and owner of the land underlying its railtrack and related infrastructure.

The Railway Code regulates the transportation of cargo, luggage, passengers and mail by railway and establishes responsibilities, rights and obligations of participants in the industry. The Railway Code requires the Company to provide its customers with relevant information about its services and tariffs. The Railway Code also requires the Company to undertake transportation of cargo and passengers in line with existing technical standards of service set in accordance with certain policies of the Company, as well as international agreements to which the Company is a party. The Company must transport cargo based on bills of lading, and the Railway Code permits the Company to inspect cargo to ensure that information contained in the bill of lading is correct.

Although the Railway Code addresses various matters concerning rail transport in Georgia, in many areas it delegates to the Company the authority to determine technical and operational details through its internal policies and regulations. The Railway Code does contain an internal dispute resolution mechanism, which, somewhat uniquely under Georgian legislation, implies that a claimant has an obligation to attempt to resolve a dispute with the Company in the first instance, before filing a claim in the courts. In addition, the Railway Code refers to the fact that the Georgian railway industry is subject to international agreements and treaties ratified by Georgia, as well as relevant provisions of the Constitution.

Pricing and Tariffs

Under the Railway Code, the State has the power to establish tariff policies through the Rail Transport Authority. The Rail Transport Authority has not yet been established and the Company is not aware of any plans of the State to do so. Accordingly, as at the date of this Prospectus, the Company is not subject to any mandatory tariffs. Instead, pursuant to the Railway Code, it sets its own tariff policy independently for all types of services, including, but not limited to, tariffs for freight transportation and freight transportation-related services, passenger services and luggage transportation. According to the Company's tariff policy, the Company may change its tariffs and the discounts applied to its tariffs upon one month's notice to customers.

Tariffs for freight transportation are based on the International Rail Transit Tariff decided among the signatories to the Tariff Agreement. In addition to the Company, parties to the Tariff Agreement include the railway companies of CIS member states Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan, as well as the railway companies of Lithuania, Latvia and Estonia. The parties to the Tariff Agreement hold conferences each autumn, at which they present their tariff plans for the next year. Base tariffs established under the Tariff Agreement are not binding and the parties may vary them during the year. The Company's final tariffs are based on various factors, including the type and weight of the cargo, the distance over which the cargo is carried and any discounts that may be applied at the Company's discretion.

Environmental Law and Regulation

Environmental matters are governed by the Constitution, the *Law of Georgia on Protection of the Environment*, No. 519, dated 10 December 1996 (as amended) and the *Law of Georgia on Environmental Impact Permit*, No. 5602, dated 14 December 2007 (as amended) (the "**Law on EIP**"), as well as other applicable legislation and regulations.

These laws establish the requirements for the protection of the environment. They impose specific obligations on all entities operating hazardous or polluting facilities, including requirements with respect to emissions and discharges, regular inventory maintenance and self-monitoring and reporting obligations. Operators of hazardous facilities, including the Company, may be liable for any damage caused by hazardous substances to human health, the environment, objects of cultural significance and other property or economic interests, regardless of fault.

The Law on EIP lists certain activities that have an impact on the environment and that are subject to mandatory ecological expertise by the Ministry of Environment Protection of Georgia. Such activities may be commenced only after obtaining an environmental impact permit. However, if the activity in question involves construction, no separate environmental impact permit will be issued. The ecological expertise report will be incorporated in, and become part of, the construction permit that is issued by the relevant permit-issuing authority, subject to issuance of the ecological expertise report by the Ministry of Environment Protection. An ecological expertise report must be issued at the second stage of processing a construction permit application. According to the applicable laws, the construction of railway facilities, as well as development of railway station infrastructure, is subject to mandatory ecological expertise. Therefore, the Company may be required to obtain environmental impact permits in respect of its activities. Failure to comply with the emission and discharge limits, a violation of the permit conditions and other environmental violations, depending on the seriousness of the violation, may result in revocation or suspension of the environmental impact permit or other applicable licenses or permits (such as construction permits), as well as imposition of administrative or criminal liability.

Health and Safety Law and Regulation

Pursuant to Article 60 of the Railway Code, the Company is under an obligation to ensure the safety of its activities with reference to applicable standards and principles, including: (i) a systematic approach towards planning and management of fire safety and transportation services; (ii) the compliance of technological methods and transportation processes with applicable normative acts; (iii) the protection of legal interests of persons and the railway while ensuring transportation safety; and (iv) the mutual responsibility of persons responsible for safety and the railway itself.

Further, the operations of the Company may be considered "hazardous" under the Georgian *Code on Safety and Free Movement of Goods*, adopted pursuant to the *Law of Georgia No. 6157* dated 8 May 2012. This is because such operations involve buildings, facilities, substances, technical equipment and machinery with significant risk to human life, health, property and the environment as a result of potential demolition, explosions, emissions or exposure to toxic substances. Certain aspects of the Company's facilities, including hydroelectric facilities, waste disposal sites, and facilities operating cargo lifting equipment and boilers are subject to periodic and *ad hoc* inspections by the Georgian authorities. If the inspecting authorities conclude that any part of the Company's operations is not in compliance with the applicable requirements, the Company may be subject to certain measures ranging from mandatory remediation orders and administrative penalties to suspension of operations.

Matters of occupational health and safety are governed by the Constitution, the 2010 Labour Code of Georgia, the 1997 *Law of Georgia on Healthcare*, the 2007 *Law on Protection of Population and Territory from Natural and Technogenic Emergency Situations*, the 2005 *Law of Georgia on Fire Safety* and certain other laws, including international agreements of Georgia, as well as rules and regulations promulgated thereunder.

These laws require that, among other matters, employers provide their employees with adequate information regarding the risks related to labour safety, including rules regarding the use of hazardous equipment, implement safety and emergency procedures and preventive measures designed to ensure safe operations of facilities and equip their employees with protective equipment. An employer may be liable to compensate their employees fully for damages resulting from performance of work duties if such damages is incurred as a result of the employer's fault.

In addition, where a building is associated with the production, storage or supply of energy, or power, or inflammable, explosive, poisonous or toxic substances or is otherwise considered excessively dangerous, the Civil Code of Georgia, No. 786, dated 26 June 1997 (as amended) (the "**Civil Code**") in certain cases imposes a higher standard of liability due to the increased danger. Those undertaking such activities are required to pay compensation if a potential hazard materialises and results in death, injury or disability of an individual or damage to a thing. The same liability is imposed on possessors of inflammable, explosive, poisonous, toxic or other hazardous substances when there is an increased danger associated with these substances. Such liability is imposed regardless of fault on the part of the possessor of such substances or activities. This liability is not triggered if the damage occurred as a result of a force majeure except in cases where the damage was as a result of an accident involving electricity transmission lines (cables) or damage to oil, gas and water supply systems.

In addition, the Civil Code provides that the possessor of transportation facilities used in the carriage of passengers or cargo are obliged to pay compensation if the operation of such transportation assets results in the death, bodily injury or disability of an individual, or damage to a thing, except in cases where the damage occurred as a result of a force majeure. This stricter liability is envisaged in respect of the operators of aircraft, which may be held liable even for damages outside their control.

Procurement

As a general rule, the procurement of goods and services by companies that are more than 50 per cent. owned by the State, such as the Company, is subject to the supervision of the State Procurement Agency in accordance with the *Law of Georgia on State Procurement*, No. 1388, dated 20 April 2005 (as amended) (the "**Law on State Procurement**") and other applicable regulations. The Government has the authority to adopt special procurement rules for state-owned companies permitting such companies to deviate from the general procurement rules set out in the Law on State Procurement. Currently, by virtue of Resolution N° 14 of the Government of Georgia on Approval of Special Rules on Procurement of Services and Goods for Georgian Railway LLC, dated 18 January 2012 (as amended) (the "**Procurement Regulation**), the activities of the Company are subject to special procurement rules, save for the procurement of construction services, which continue to be regulated by the Law on State Procurement. The Procurement Regulation, if not further extended, will expire on 15 January 2014.

Procurement rules under the Procurement Regulation

Typically the Company purchases goods and services by means of a tender. The Company is also entitled to use the price quotation system if (x) the anticipated price of the goods or services is less than GEL 100,000 or (y) approved by the Board of Directors. Goods and services may also be procured based on negotiations with a single supplier if (i) the anticipated price of the homogenous goods or services does not exceed GEL 50,000; (ii) the delivery of goods or services is an exclusive right of the supplier in question; (iii) the procurement relates to the service of a car of no more than five years in age (with warranty coverage), spare parts or lubricants needed for such services; (iv) the purchased goods are substituted by new ones having the same or improved parameters; (v) for the maintenance of quality and use of the goods or services, it is necessary to contract with the same supplier or subcontractor for goods and services, unless the anticipated price is more than the price initially paid; or (vi) the board of directors resolves to do so. Tenders are to be conducted by a tender commission, which is created by the Board of Directors. Members of the tender commission are employees of the Company. The Procurement Regulation is annexed by the list of goods and services specific to the Company's sphere of business. In the case of a procurement of goods or services where the Company is required to incur expenditure over more than one year, the Company is required to obtain the approval of the Supervisory Board.

Procurement rules under the Law on State Procurement

The Law on State Procurement provides that the primary modes of state procurement are electronic tender and simplified electronic tender. The State procurement can also be performed by simplified procurement which is applicable only in certain limited circumstances. The Law on State Procurement provides for simplified procurement where, for example, the list includes, but is not limited to: (i) delivery of goods or services is an exclusive competence of one person and there is no alternative; (ii) there is an emergency, in which case the goods or services procured shall not exceed the volumes necessary for dealing with the state of emergency; (iii) in order to maintain the quality and use of the goods and services it is necessary to contract with the same provider, unless the anticipated price is more than the price of initial delivery; (iv) procurements determined by respective acts of the President and/or the Government for unimpeded implementation of events having social and state significance; (v) one or more vehicle or computer is substituted with one or more vehicle or computer of the same or improved parameters; or (vi) the procurement is related to state representation.

The Procurement Regulation grants a degree of flexibility to the Company throughout the procurement process as negotiations with one person not considered to be procurement by the Law on State Procurement and based on the Procurement Regulation, the Board of Directors can exercise wide discretion throughout the process of choosing the mode of procurement.

Disposal of Fixed Assets

As the State is the majority shareholder of the Company, the Company must comply with Order No. 1-1/1732 of the MESD, dated 29 October 2010 (the "**Disposal Rules**"), which regulates the disposal of fixed assets in the capital, or on the balance sheet, of companies, which are more than 50 per cent. owned by the State. Under the Disposal Rules, fixed assets can be disposed of through one of the following methods: (a) a write-off from the balance sheet; (b) the transfer under "temporary charged possession" (for example: rental); (c) sale; and (d) a withdrawal of fixed assets from the capital of a company or the contribution of such assets to the capital of another entity. Management is also entitled to use other methods of disposal as provided for in the Civil Code of Georgia, provided that the prior approval of the Board of Directors (acting on the approval of the Supervisory Board) and the EMA (which will co-ordinate with the MESD) are obtained.

A write-off of assets is executed by the Management through the internal commission of the Company except in cases where (i) immovable property is written off, and (ii) the value of the residual balance of the written-off assets exceeds 10 per cent. of the value of the residual balance of the Company's overall fixed assets, which requires the approval of the EMA.

A transfer of fixed assets under "temporary charged possession" is executed through an auction based on a decision of the Management except in cases where (i) the area of the immovable property exceeds 50 sq/m and/or 10 per cent. of the entire area, and (ii) the value of the residual balance of the movable assets exceeds 5 per cent. of the value of the entire residual balance of the Company's assets, which require the approval of the EMA. The consent of the MESD is also necessary in cases of a direct transfer of fixed assets if any auction is not held.

A sale (through or without auction), "temporary gratuitous transfer" (*i.e.*, transfers to a third party for no remuneration) and withdrawal from or contribution of the fixed assets to the capital of another entity requires the approval of the EMA and the MESD. The rules regarding the disposal of fixed assets through an auction (public and electronic), which are applicable to State property are equally applicable to the disposal of the fixed assets of the Company.

Electricity Supply

The Company is a qualified user entitled to participate in the wholesale trade of electricity in accordance with the *Law of Georgia on Electroenergetics and Natural Gas*, dated 27 June 1997 (as amended, the "**Law on Electroenergetics and Natural Gas**") and the Decree N° 77 of the Ministry of Energy of Georgia on Approval of Electricity (Capacity) Market Rules, dated 30 August 2006 (as amended) (the "**Market Rules**"), which require, among other things, the registration of qualified users with ESCO.

To register, the applicant must submit the following documentation to ESCO: (i) the standard form application approved by ESCO; (ii) an excerpt from the entrepreneurial registry; (iii) a copy of the license, if the applicant is a licensee; and (iv) technical documentation confirming connection to the electricity grid.

Extra requirements may apply depending on the status of the applicant. Thus, direct customers, such as the Company, must also present documents confirming that during the last twelve months preceding the date of application they have consumed the requisite levels of electricity or, if the applicant did not consume that level of electricity, documentation confirming possession of an electricity grid with a capacity commensurate to required levels of electricity.

Having the status of a qualified user obliges the Company to install, repair and have equipment ready for use by, and to provide information to, ESCO.

Other

Contracting

Pursuant to Resolution N° 139 of the Government of Georgia on Certain Measures Related to Conclusion of Contracts with Foreign Counterparties, dated 11 May 2010 (as amended), State-owned companies are required to submit draft contracts that they intend to conclude with foreign counterparties for review and approval by the Government before conclusion if such contracts are considered to be in the public interest and if such contracts envisage the choice of foreign law as the governing law of such contract or the submission of dispute to international arbitral panels or foreign courts. Also, in the case of termination of such contracts, State-owned companies are required to submit a legal opinion assessing the legal risks of termination to the Government prior to termination of the contract.

In addition, under the charter of the Ministry of Justice of Georgia, companies which are more than 50 per cent. owned by the State, are required to submit draft contracts to the Ministry of Justice for the purposes of ensuring compliance with Georgian Laws if such contracts envisage the submission of the State-owned company to international arbitral panels or foreign courts.

Communications

The Company holds a licence to use numeric resources and is subject to regulation by the Georgian National Communications Commission in accordance with the *Law of Georgia on Electronic Communications* No.1514, dated 2 June 2005 (as amended).

Natural Resources

Activities relating to the exploration and extraction of minerals are subject to licensing. Licences can be issued either for (i) the extraction of minerals; or (ii) the exploration and extraction of minerals (a so-called combined license on exploration and extraction). These licences are issued through a public auction organised by the Agency for Natural Resources, a legal entity of public law existing under the Ministry of Energy and Natural Resources. The Company holds a number of mineral use licences and is responsible for compliance with their respective conditions as enforced by the Agency for Natural Resources.

Rail Safety

As at the date of this Prospectus, the Company operates under a "self-regulation" policy in respect of rail safety. The Railway Code delegates safety regulation to the Company. Accordingly, the Company has developed and implemented its own safety policies. See also "*—Environment*".

The Company experiences minor derailments from time to time, often due to technical faults in the rolling stock (sometimes owned by other railway companies). These derailments occasionally result in damage to the railtrack or oil spillages, which can cause environmental damage in the area proximate to the derailment. All such derailments are reported to the appropriate governmental authorities. In July 2011, the Company experienced three freight train derailments that involved the derailment of loaded tank cars. See "*Risk Factors—Risks Related to the Company's Business—A major accident, derailment or other incident could result in loss of the Company's rolling stock, disruption to services, environmental remediation costs and damage to the Company's reputation*" and "*—Environment*".

In the period since 1 January 2008, the Company has experienced five employee fatalities, all of which were determined by the Company to have resulted from safety violations on the part of the employee concerned. As a result, the Company did not incur any liability with respect to these accidents. In the same period, the Company has experienced four derailments (one in April 2010 and three in July 2011).

Subsidiaries and Affiliates

The following are subsidiaries through which the Company undertakes its other activities:

- *Railway TransContainer LLC*: Railway TransContainer LLC is a Georgian limited liability company, wholly owned by the Company, established in October 2009. Its corporate objective is to help strengthen the Company's presence in the container transportation market, primarily through the creation of necessary infrastructure, such as container terminals, and to promote the containerisation of the Caucasus corridor. To foster this containerisation, Railway TransContainer LLC has built and currently operates the Tbilisi Container Terminal. See "*—Freight SBU—Freight Composition*".

- *Georgian Railway Construction JSC*: Georgian Railway Construction JSC is a Georgian joint stock company, wholly owned by the Company, established in December 2009. Its corporate objective is to carry out certain construction projects for the Company and its subsidiaries. Pursuant to the subcontract between GRC and the joint venture formed by China Railway 23rd Bureau Group Co. Ltd. and JSC Khidmesheni (the "**Bypass Project Design Contractor**"), GRC has been nominated as the subcontractor to the Bypass Project Design Contractor in respect of certain construction works relating to the Bypass Project.

- *Railway Property Management LLC*: Railway Property Management LLC is a Georgian limited liability company, wholly owned by the Company, established in July 2009 to maximise value for the Company from its remaining non-core, obsolete or under-performing property assets, such as land, depots and stations not currently in use. In February 2012, the Company invested an additional GEL 13 million in this subsidiary. On 6 April 2012, the Company transferred to the State the partially constructed Batumi Tower, which was a project of Railway Property Management LLC. See "*Factors Affecting the Company's Results of Operations — Disposals and write–off of certain assets*".

- *Borjomi Bakuriani Railway LLC*: Borjomi Bakuriani Railway LLC is a subsidiary of Railway Property Management LLC. It owns a narrow-gauge tourist branch line that runs between two resort towns and uses a different gauge than the Company's other railtracks. See "*—Business Operations—Infrastructure SBU*".

Until May 2010, Railway Telecom was a wholly owned subsidiary of the Company. With effect from 24 May 2010, the Company transferred its shares in Railway Telecom to the MESD. In exchange, the MESD agreed to contribute cash or in-kind property with a value of GEL 6.8 million, the fair value attributed to the Railway Telecom shares. In November 2011, the Company and the MESD acknowledged that the MESD had made such in-kind contributions, thereby fulfilling its obligation in connection with the transfer of Railway Telecom.

In October 2010, the Company sold, by way of an auction, its 25 per cent. stake in Chitakhevi, a company engaged in the operation of a HPP, to JSC EnergoPro Georgia pursuant to a share sale and purchase agreement. The sale price was GEL 6.3 million.

In November 2011, the Company transferred its shares in JSC Nenskra, a wholly owned subsidiary of GRC, to the State, which, in turn, transferred these shares to the PF. JSC Nenskra has the rights and obligations in respect of the construction of a HPP on the Nenskra river. The book value of the transfer was approximately GEL 6.2 million.

In line with its strategy to focus on its core business activities, the Company may consider disposing of subsidiaries that it believes to be non-core at an appropriate time.

Property

The Company has a number of real estate assets, including buildings and land, related to the infrastructure required to operate the railway. The Company has entered into a contract with a state-owned security service company that provides security services throughout the Company's network, including at stations, tunnels and bridges and on its trains. See also "*—Insurance*".

Buildings

As at 31 December 2011, the Company and its subsidiaries owned 2,851 structures, approximately 1,611 of which were stand-alone buildings and the remainder of which were other constructions, such as platforms. As at the same date, of the stand-alone buildings, approximately 139 were passenger stations, 246 were passenger support structures (such as open-air shelters and retail shops), 240 were for luggage or freight storage and 435 were administrative or residential buildings. In particular, the Company owns its headquarters building in central Tbilisi, which has a total area of approximately 17,520 square metres, and, as at 31 December 2011, owned the Central Tbilisi Station, with a total area of approximately 54,850 square metres. In March 2012, the GMS approved the withdrawal of the Central Tbilisi Station and certain land plots from the Company's capital to the State, although the Company retains a right of use over that portion of the Tbilisi Central Station necessary for the Company's operations. See "*Management's Discussion and Analysis of Results of Operations and Financial Condition—Factors Affecting the Company's Results of Operations—Disposals and write-offs of certain assets*".

The Company generates some revenue from leasing space to third parties, including at the Central Tbilisi Station. The Company's subsidiary, Railway TransContainer LLC, has built and currently operates the Tbilisi Container Terminal, which has a total area of approximately 42,100 square metres.

Land

As at 31 December 2011, the Company and its subsidiaries held title to 4,925 hectares of land, comprising all of the Company's and its subsidiaries' total land in use, principally in and immediately around its right-of-ways.

The Company intends to transfer approximately 70 hectares of land that it owns in central Tbilisi to the State once the Bypass Project is completed, assuming that the State reimburses the Company for its share of the project costs, as contemplated by the Bypass Project Memorandum. See "*—Bypass Project*" and "*Risk Factors—Risks relating to the Company's business—Current and future projects designed to improve the Company's infrastructure, including the Modernisation Project and the Bypass Project, are still in the early stages of implementation and may be subject to delays or, in relation to the Modernisation Project and the Bypass Project, higher than anticipated costs*".

Modernisation Project

The Company engaged SYSTRA and SNCFI in early 2010 to prepare a full-scale feasibility study and an initial design study for the Modernisation Project. Based on the results of these studies, the Company began incurring costs for the project in September 2010. The key objectives of the Modernisation Project are:

- optimising freight and passenger traffic;
- optimising stations, depots and infrastructure;
- optimising freight and passenger rolling stock;
- reducing operational expenses;
- improving operational safety;
- improving social and environmental safety;
- increasing train speeds; and
- introducing a clear and defined maintenance programme.

The Modernisation Project has an estimated capital expenditure of CHF 389.7 million (GEL 692.9 million), of which CHF 297.1 million (GEL 528.2 million) remained outstanding as at 31 December 2011. The Company expects to complete the project by 2016. The Company expects to continue to fund the project through a combination of the proceeds from the 2010 Notes and its internal cash flows.

The Modernisation Project focuses primarily on the mainline that runs from Tbilisi to the Black Sea, in particular to the terminals at Poti and Batumi. As part of the project, the Company intends to modernise the railroad and electric supply infrastructure between Tbilisi and Batumi (315 kilometres), including the 40-kilometre mountainous gorge region in Central Georgia, with the aim of achieving passenger train speeds of 80 km/h on the gorge section and 120 km/h on the rest of the mainline, as compared to current average speeds of approximately 55 km/h in the gorge section and approximately 65-90 km/h on the rest of the mainline.

One of the key aims of the Modernisation Project is decreasing the track gradient in the gorge section. Management believes that a flatter gradient will reduce wear and tear on wheels and tracks, decreasing the need for extra locomotives in that section, and reducing extra stops to cool the brakes on the trains. In addition, the Company plans to make improvements to tunnels, bridges and level crossings and procure new rolling stock. As a result of the Modernisation Project, the Company expects diminished maintenance costs and an extended life-cycle of certain of its infrastructure assets, and management estimates that completion of the Modernisation Project may result in savings in operating costs of up to 40 per cent. as compared to 2008-2010 total operating costs in the areas affected by the Modernisation Project.

The Company has completed the purchase of substantially all equipment and materials necessary for the parts of the Modernisation Project, which the Company is implementing with its own resources. The tendering process for the work on the gorge section has already been completed and work on the gorge section has begun. Modern rails and electric supply infrastructure have already been installed on a 140 kilometre section of the line. In addition, the Passenger SBU has to date achieved speeds of 120 km/h on a 103 kilometre section of the main line, and it expects to be able to achieve that speed on a further 50 kilometre stretch by the end of 2012. The Modernisation Project is planned to take place in stages, thereby increasing the Company's flexibility.

Baku–Tbilisi–Kars Railway Venture

In February 2007, the governments of Georgia, Turkey and Azerbaijan signed an agreement in connection with the construction of a new railway connection linking Azerbaijan, Georgia and Turkey (the Baku-Tbilisi-Kars project). Construction began in 2008 and is expected to be completed in 2013.

In connection with the construction of the new railway connection linking Azerbaijan, Georgia and Turkey (the Baku-Tbilisi-Kars project), the existing Marabda-Akhalkalaki rail line, which was a secondary line in need of refurbishment, was withdrawn from the capital of the Company and contributed by the State to a project-related special purpose entity established and owned by the Government. The special purpose entity obtained a U.S.$775 million loan from the government of Azerbaijan to finance the rehabilitation of the existing Marabda-Akhalkalaki line and the construction of the connecting line from Akhalkalaki to the Turkish border. The Company has been granted the exclusive right to operate the Georgian portion of the new line.

It is expected that after completion of the project, the line will be maintained by a separate entity, which is expected to be a 50:50 joint venture between Azerbaijan Railway and the Company, although it is possible that Azerbaijan will become a member of the existing special purpose entity. It is expected that the joint venture shall be operational until the loan from the Azerbaijani government has been repaid and that the entity owning the line will charge the Company for access to the line not owned by the Company, but no charging scheme has been determined yet. Management expects that the Company will be able to set tariffs on the Georgian portion of the line.

The Baku-Tbilisi-Kars project will effectively open a new rail-only corridor from the Caspian Sea to Europe via Turkey, eventually excluding the need for sea transportation once the planned rail tunnel under the Bosporus Strait in Istanbul is complete. The Baku-Tbilisi-Kars project could also open a North-South rail corridor linking Russia to Turkey. This line will transport both freight and passengers and is expected to provide an alternative freight transport route to routes that transit through Iran. Management believes this line will be an important driver of future incremental transport volumes, particular containerised cargo, although, as it is a new route, management believes it may take time to attract significant volumes. Based on current cargo flows and assuming operations on the line commence as scheduled, management believes that, by 2015, the Company will be able to re-route at least two million tonnes of existing cargo flows (principally dry cargo currently transported by truck) with an overall increase in transportation capacity of five to 15 million tonnes between Turkey, the Caucasus, Russia and Central Asia to this route.

Management believes that increasing trade between Turkey and Central Asia provides it with a significant opportunity to capture trade flows, particularly raw materials imported into Turkey from Central Asia and finished goods exported by Turkey. With respect to Turkey-Russian trade, management believes there is an opportunity to capture additional volumes, particularly of dry cargo, that are currently shipped via Iran or the Russia-Black Sea route.

Bypass Project

In late 2008, the Municipality of Tbilisi proposed the Bypass Project to the Company, through which certain railway infrastructure components would be moved from the centre of Tbilisi to the northern part of the city, and freight and passenger trains would no longer transit through central Tbilisi. The Municipality of Tbilisi (the "**Municipality**") believed that its proposal would provide a number of benefits to the Municipality, including helping alleviate future environmental and safety concerns and, because the move would make available commercially valuable land in central Tbilisi, fostering economic improvements and job growth in the city.

After studying the proposal, the Company agreed to undertake the Bypass Project as the Company believed the project would also provide it with a number of benefits. These benefits included the receipt of proceeds from potential sales of land in central Tbilisi and re-routing operations that raise potential environmental and health and safety concerns away from the densely populated city centre.

The bypass railroad comprising part of the Bypass Project is expected to feature double track and involve the construction of 30 km of new railway lines and the reconstruction of 10 km of the existing railway line. All existing passenger trains (except one summertime train from Yerevan (Armenia) to Batumi, which already bypasses Tbilisi) terminate at the existing central passenger station in Tbilisi. As part of the Bypass Project, the Tbilisi Central Station is to be closed, and passengers will instead be required to disembark at one of the other two existing Tbilisi stations, one for west-bound traffic at Didube and the other for east-bound traffic at Navtlugi, which are connected by an existing public metro line. Upon completion of the Bypass Project and the closing of the central station, the Company anticipates that the Existing Railway Land will become available for sale and development. The Company commenced the construction tender process for the Bypass Project in December 2009 and began incurring costs for the project in November 2010. Management is working with contractors to determine a projected completion date for the Bypass Project.

The Government contributed approximately 182 hectares of land for the Bypass Project in 2010 and 2011, with a value of approximately GEL 33.1 million, to the Company. This land comprised approximately 40 per cent. of the land required to support the bypass railroad and related assets. The remaining approximately 60 per cent. of the land was acquired by the Company in 2010, 2011 and up to 31 March 2012 from private owners pursuant to a resettlement action plan (this land, together with the above-mentioned land contributed by the MESD, the "**Future Railway Land**"). The total cost for the purchases of land and related assets from private owners was approximately GEL 27.4 million. Implementation of the resettlement action plan was completed in mid-2011.

In April 2012, the Company and the Government, represented by the Ministry of Finance and the MESD, entered into the Bypass Project Memorandum in respect of the Bypass Project (as defined below). The Bypass Project Memorandum creates a set-off mechanism for the Company to be reimbursed by the State for the Company's future expenses in relation to the Bypass Project out of dividends that would otherwise be payable to the State in respect of its shares in the Company and in exchange for the transfer, by the Company to the State, of the Existing Railway Land. The amount to be reimbursed to the Company does not cover an instalment of CHF 36.1 million due to be paid by the Company to its contractor in 2012 and is subject to an aggregate cap of CHF 138.0 million. In May 2012 and to date in June 2012, the Company paid to its contractor approximately GEL 20.4 million (CHF 11.9 million) and GEL 5.0 million (CHF 2.9 million), respectively, of the CHF 36.1 million not covered by the reimbursement obligations and the balance shall be paid by the Company out of its existing cash flows upon the completion of the corresponding work by the contractor. If the dividends payable to the State are insufficient to cover the reimbursable expenses in full, the Company has the right to retain a pro rata ownership interest in the Existing Railway Land.

Electricity Supply

Approximately 94 per cent. of the Company's railway network is electrified. Until September 2011, the Company procured most of its electricity in the open market. In September 2011, the Company signed the Electricity Contract with EnergoPro Georgia. Management estimates that the electricity EnergoPro Georgia is obligated to deliver under this contract will satisfy almost 90 per cent. of its total electricity requirements. The Electricity Contract has a term of ten years, subject to early termination by the Company on each anniversary on one month's prior written notice or by either party in the circumstances permitted under Georgian contract law. In connection with this contract, the Company also entered into a lease agreement, through which a number of electricity substations are leased to the Company, and a transit energy supply contract through which EnergoPro Georgia may supply electricity through energy assets in the Company's possession for a fee. The contract will also be automatically terminated in the event that the lease agreement or transit energy supply contract are terminated. The Electricity Contract fixes tariffs for five years in line with the upper threshold currently contained in Resolution No. 33 of the GNERC, subject to certain circumstances in which these tariffs can be increased. From 2016, tariffs will be applied in accordance with any increased tariffs set by resolutions issued by GNERC.

Other Procurement

Aside from electricity, the Company's principal purchases are fuel, metal, principally in the form of steel for rails, and freight locomotives and rolling stock.

The Company purchases its fuel (principally diesel fuel for its locomotives) at spot rates from the successful bidder of the Company's annual tender for fuel suppliers.

In 2010, the Company signed a long-term contract for the purchase of rails, which management estimates will account for nearly all the rails needed for the Modernisation Project. The price for the rails was a fixed spot price that enabled the Company to mitigate the risk of price increases for what is one of the largest cost components of the Modernisation Project.

The Company purchases its freight locomotives and rolling stock largely from domestic factories. In addition, there are a number of non-Georgian suppliers in the industry from whom the Company believes it could acquire rolling stock. Following the completion of a tender process, the Company's passenger trains are to be supplied by a Chinese manufacturer, CSR Narjing Puzhen Rolling Stock Co. Ltd.

Employees and Pensions

The following table sets forth the distribution of the Company's employees, by business unit, as at the dates indicated:

	As at 31 December		
	2011	**2010**	**2009**
Head Office	450	415	500
Infrastructure SBU	5,302	7,028	6,279
Freight SBU	5,643	5,029	6,344
Passenger SBU	1,668	1,760	1,874
Subsidiaries	164	103	103
Total	**13,227**	**14,335**	**15,100**

(1) As at the date of this Prospectus, 2.8 per cent. of the Company's employees were aged under 25 years, 17.8 per cent. were aged between 25 and 34 years, 22.0 per cent. were aged between 35 and 44 years, 31.9 per cent. were aged between 45 and 54 years and 25.6 per cent. were aged 55 years and over.

The Company is the largest corporate employer in Georgia and creates additional employment in related industries, such as railcar manufacturing. The Company has experienced no material labour disputes or strikes and believes employee relations to be good. As the date of the Prospectus, the Company does not have any collective bargaining agreements with its employees or a trade union, although the Company has in the past been party to arrangements with the Railway Workers Trade Union of Georgia. See "—*Legal Proceedings*". Employees may join a trade union if they wish.

The average monthly salary (including bonuses paid) of the Company's employees was GEL 668 for each of the three month periods ended 31 March 2012 and 2011 and GEL 656 for the year ended 31 December 2011, GEL 630 for the year ended 31 December 2010 and GEL 578 for the year ended 31 December 2009. The Company has also implemented the New Bonus Scheme, a performance-based bonus plan tied to the implementation of strategic projects and the economic value added by the relevant SBU. Determination of economic value added is based on various measures, including the Company's estimated cost of capital, which is determined by the Company periodically from factors such as estimates of risk free capital rates, market premium and peer group comparisons. The New Bonus Plan applies to all staff, including senior management. In addition, in 2010, the Company introduced a new loyalty programme according to which outstanding employees receive various rewards.

The Company does not maintain a private pension fund and, accordingly, has no unfunded or other pension liabilities. Although private pension funds are permitted in Georgia, there is also a state pension scheme of which the Company's employees are members. The Company withholds 20 per cent. of each employee's salary as a personal income tax and pays this amount to the State. A part of this income tax is apportioned by the State to fund the state pension scheme. Pensions are then paid directly by the State to the employees. In addition to their salary and any bonuses, employees and their family members receive private health insurance from the Company.

See "*Shareholders and Management*" for further details relating to the Company's management.

Information Technology

The Company requires advanced information technology systems and software to ensure the smooth operation of its sophisticated logistics, dispatch and rolling stock- and freight-tracking services. Most of the Company's software and information systems are developed in-house to meet the specific demands of the Company. These systems include a centralised billing and electronic document management system used for document handling for freight transportation;

an automated system that monitors and controls rolling stock in real time; software designed to monitor movements of containers, railcars and trains in stations; a ticket sales and accounting system for passenger transportation; and a centralised multi-module software for internal bookkeeping, which improves internal processing of initial accounting documents with electronic signature authorisations, for financial and tax accounting, budgeting and treasury operations.

The Company generally utilises hardware from Hewlett-Packard Company and Cisco Systems, Inc. Its software platform is based on the 1C:Enterprise platform from 1C:Enterprise ("**1C**"), a Russian-based developer. This platform may be customised for the Company's local financial and operational environment, as well as for specific modules and procedures that the Company may wish to oversee.

The Company has three operating servers in use at all times, including a main server, a substitute server and a back-up server with a real-time link to the main server. All operations at the head office and throughout the organisation are connected on a real-time basis and management estimates that there is a delay of between seven and 27 seconds in the transfer of data from the main server to the back-up server. The Company's billing database is backed-up on a daily basis, while its "1C" accounting system is backed-up on a monthly basis. The Company does not, however, have any off-site back-up system for data protection.

Whilst the Company's management believes that the Company's current systems are sufficient for the Company's current needs and are scalable to support the expected growth in the Company's operations, a top priority of the Modernisation Project is aimed at improving and upgrading the Company's IT systems to state-of-the-art technologies in line with the Company's current and expected business activities.

Intellectual Property

The Company's name, "Georgian Railway" (in Georgian: "საქართველოს რკინიგზა"; in Latin script "Sakartvelos Rkinigza") and its logo, shown on the front cover of this Prospectus, are trademarks, which the Company has registered with "Sakpatenti", the State authority with whom trademarks and patents are registered in Georgia. The Company also maintains a corporate website, and the right to this website's domain name is owned by the Company. Management believes that the Company has taken all appropriate steps to be the rightful owner of, or be entitled to use, all of the intellectual property rights necessary to conduct its core business.

Environment

The Company is subject to various environmental protection and occupational health and safety laws and regulations relating to protection of the environment and protection of human health and safety in Georgia. The Company's Environmental Protection Unit is responsible for overseeing the Company's compliance with any such applicable environmental and health and safety laws and regulations, which are promulgated by the Ministry of Environment Protection. This unit is also responsible for the planning, implementation, monitoring and execution of the Company's environmental strategy and any contingencies that may occur from time to time. The Environmental Protection Unit, which is a sub-division of the Traffic Safety Department of the Infrastructure SBU, is staffed by ten employees.

Pursuant to applicable Georgian environmental laws and regulations imposed by the Ministry of Environment Protection, the Company is required to remediate, though clean-up and rehabilitation works (such as through repairing damaged assets or objects), any environmental damage caused by its operations. In order to comply with such obligations, the Company has specially designed rolling stock, known as "repairing trains", equipped to carry out environmental remediation work. In July 2011, the Company experienced three freight train derailments; the Company does not believe that any significant environmental damage resulted from the related spills. The Company has not experienced any material claims relating to environmental pollution. See "*Risk Factors—Risks Related to the Company's Business—Failure to comply with applicable environmental and health and safety laws and regulations may give rise to significant liabilities*" and "*Risk Factors—Risks Related to the Company's Business—A major accident, derailment or other incident could result in loss of the Company's rolling stock, disruption to services, environmental remediation costs and damage to the Company's reputation*".

Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. Moreover, to the extent insurance may be available to the Company outside Georgia (if at all), based on statistics relating to past failures on the railway, the Company does not believe it would be cost-effective to purchase insurance services for its infrastructure assets and, accordingly, in common with other State-owned enterprises, the Company does not have any insurance coverage for its infrastructure and other assets, business interruption, or third-party liability in respect of property or environmental damage arising from accidents on the Company's property or relating to the Company's operations. In addition, the Company does not maintain insurance for terrorism or war risk. The Company's customers typically purchase insurance covering the cargo transported by the Company.

The Company does maintain health insurance covering its employees and their families. As part of its contract for security services, the Company is compensated for stolen or damaged assets or goods as a result of actions such as vandalism, theft or sabotage. See "*—Property*". As at the date of this Prospectus, the Company is considering procuring directors and officers liability insurance and is in the process of obtaining proposals from various insurance companies.

Legal Proceedings

The Company is, from time to time, subject to legal proceedings and other investigations in the ordinary course of its business. Additionally, the Company is, or has been, subject to the disputes described below.

Large Taxpayers Inspection

In November 2005, the Large Taxpayers Inspection issued an order levying additional income taxes to be paid by the Company in respect of the period from 1998 to 2003. Such additional income tax amounted to approximately GEL 13 million and was deducted by the Large Taxpayers Inspection from the Company's accounts. The Company disputed this additional income tax on the grounds that (i) there had been a previous tax amnesty relating to the period in question, and (ii) the claim for tax for 1998 was outside the period prescribed by the statute of limitations. Following a number of rulings by the first and second instance courts and the Court of Appeal, on appeal by the Company to Cassation, the Supreme Court annulled the order and ruled that the Revenue Service, which has assumed the role of the Large Taxpayers Inspection, should reconsider the matter and issue a new administrative act according to which the amounts deducted in respect of the additional income tax shall be returned to the Company. Following the resolution of this dispute, the Revenue Service has transferred approximately GEL 13 million to the Company's account.

Batumi Oil Terminal

In 2005, the Company commenced proceedings against Batumi Oil Terminal Ltd. in the Tbilisi City Court. The Company and the Batumi Oil Terminal Ltd. entered into a contract in 2002 relating to the use of the Company's freight railcars. Batumi Oil Terminal Ltd. has, in turn, concluded a number of contracts with end-customers through which their cargo is transported using the Company's freight railcars. Pursuant to the contract between the Company and Batumi Oil Terminal Ltd., the latter is liable for additional fees for the use of the Company's freight railcars by third parties beyond the period contractually provided for. The Company's claim relates to approximately GEL 14 million in such additional fees that have accrued. The claim is currently being considered by the Tbilisi City Court.

Railway Workers Trade Union

In July 2010, the Railway Workers Trade Union, an affiliate of the Georgian Trade Unions Confederation, filed a claim with the Tbilisi City Court appealing the Company's decision to suspend the direct transfer of that portion of each union members' salary constituting trade union membership fees to the Railway Workers Trade Union. The direct transfer of such fees was contemplated in the agreement entered into between the Company and the Railway Workers Trade Union in April 2006 (the "**RWTU Agreement**") and the Railway Workers Trade Union alleges that the suspension of such transfer violates this agreement. Management, however, believes that there has been no such violation, as the RWTU Agreement was terminated in accordance with Georgian law following a failure of the parties to agree on amendments to the RWTU Agreement in July 2010. The RWTU Agreement provided for its reaffirmation or amendment by the parties on an annual basis and, accordingly, upon a failure of the parties to reach agreement, the RWTU Agreement automatically terminated in accordance with its terms and Georgian law. In November 2010, the Tbilisi City Court ruled in favour of the Company and found no basis on which to question the Company's suspension of the direct transfer of union membership fees to the Railway Workers Trade Union. The Railway Workers Trade Union appealed this decision, but did not meet the deadline for the payment of the Court's fees. Accordingly, in January 2011, the Tbilisi City Court refused to commence second instance proceedings and there are no ongoing proceedings in the Georgian courts in relation to Railway Workers Trade Union's claim. Management maintains that there is no basis for the Railway Workers Trade Union's claim and that its employees are free to transfer any part of their salaries to any organisation at their discretion. The Company's employees are also free to be members of any trade union. See "—*Employees and Pensions*".

SHAREHOLDERS AND MANAGEMENT

Shareholders

The Company is wholly owned by the State, both directly and indirectly through the PF. 74.5 per cent. of the State's shares in the Company are held directly by the State and controlled by the EMA, which represents and acts on behalf of the State in respect of the Company, other than in respect of any decision to sell or otherwise dispose of the shares of the Company, which is reserved to the MESD. The remaining 25.5 per cent. of the shares of the Company are held by the PF, which itself is wholly owned directly by the State.

Whilst nominally under the control of the MESD, which approves the statute of the EMA and appoints its chairman, the EMA has semi-independent status by virtue of its standing as a separate legal public entity. The EMA's budget is entirely financed by the State Budget and does not benefit from any independent funding.

On 27 March 2012, the Parliament of Georgia adopted an amendment to the law on State Property in Georgia whereby the EMA will be liquidated and all of its powers, rights and obligations will be transferred. Pursuant to further amendments currently being discussed in Parliament, all of the EMA's powers, rights and obligations, including EMA's ownership interests in the Company and its rights and obligations as a shareholder of the Company, will be transferred to a new agency, the National Agency for State Property, which will manage state property, including the shares of state-owned companies. This transfer is expected to take place by September 2012.

The PF was established by the *Law of Georgia on JSC Partnership Fund* for the purposes of promoting investment activity and economic development and creating job opportunities in Georgia. The Prime Minister of Georgia is the Chairman of the Supervisory Board of the PF. The other members of the Supervisory Board of the PF are the Ministers of Justice, Finance, Economy and Sustainable Development and Energy and Natural Resources, as well representatives of the private sector, mainly bankers and experienced businessmen. The PF is managed by a Chief Executive Officer, who in coordination with the PF's Chief Investment Officer and several senior investment officers, ensures implementation of the investment projects approved by the PF's Supervisory Board. The PF is assisted in its activities by advisory bodies. The PF typically participates in projects as an equity investor, guarantor or through debt financing, either as a lender or as a guarantor. Currently, the PF's charter capital mainly comprises shares and other ownership interests that it holds in State-owned companies, including the Company. The State's role in the management and operation of the PF is limited to the functions of a shareholder as defined under the *Law of Georgia on Entrepreneurs*, the *Law of Georgia on JSC Partnership Fund* and the PF's charter. According to the PF's charter, the State's only obligation, as shareholder, is to ensure that initial contributions to the authorised capital of the PF are made. The PF is accountable for its activities to the State as its shareholder, which may also request inspections of the PF's business activities and annual accounts in the event that it considers infringements of its charter and applicable laws to have occurred.

Due to the Company's status as a strategically important national asset, the State intends to retain at least 51 per cent. of the shares in the Company if it decides to sell shares in the Company in the future.

Overview of the Company's governing bodies

The Company's governing bodies consist of the GMS, the Supervisory Board and the Board of Directors, the last of which is responsible for the day-to-day management of the Company. A brief description of each of the GMS, the Supervisory Board and the Board of Directors is set out below.

General Meeting of Shareholders

According to the Charter, the Supervisory Board shall convene an annual GMS no later than two months following the completion of an external audit of the Company.

According to the Charter, the time, place and the agenda of the GMS shall be sent to the Company's shareholders at least 20 days prior to the date of such GMS. According to the Charter, the Supervisory Board determines the record date for the GMS. Shareholders holding at least one per cent. of the Company's shares should be notified about a GMS via registered mail.

A quorum for the GMS is established if a meeting is attended by the holders of at least 50.0 per cent. of the voting shares or their authorised representatives. If there is no quorum, a new GMS shall be convened with the same agenda and within the period determined by the Supervisory Board in accordance with the procedures set by the Charter. A quorum for the new GMS is satisfied if holders of at least 25.0 per cent. of the voting shares or their representatives are present. If there is still no quorum at this new GMS a further new GMS shall be convened and such further GMS will be deemed to be quorate irrespective of the number of attending voting shareholders or their representatives.

An Extraordinary GMS (an "**EGM**") shall be convened whenever the Supervisory Board or a shareholder or group of shareholders holding at least 5.0 per cent. of the shares deems such a meeting necessary. Pursuant to Georgian law, shareholders who individually or together hold at least 5.0 per cent. of the shares may, not earlier than one month from the last GMS, request that the Supervisory Board convene an EGM. The Supervisory Board shall convene such meeting no later than 90 days following the receipt of such request.

The GMS is presided over by the Chairman of the Supervisory Board or, in his absence, by the Vice-Chairman or any other member of the Supervisory Board. In the absence of the members of the Supervisory Board, the GMS is presided over by the Chief Executive Officer. If none of the aforementioned persons are present, the chairman shall be selected by the GMS by a simple majority of votes.

All holders of common shares registered with the share registrar as at the record date (to be determined by the Supervisory Board in accordance with applicable laws) of the GMS shall have the right to attend and vote at the meeting. Shareholders may be represented at the GMS by a proxy, if issued in accordance with the Charter.

Under Georgian law, a single shareholder holding more than 75 per cent. of the Company's voting shares would be entitled to pass a resolution without convening a GMS. However, such entitlement has been disapplied in the Company's Charter.

Under Georgian law and the Charter, the shareholders are authorised to pass resolutions on the following issues at a GMS:

- approving amendments to the Charter (including, without limitation, the Company's authorised capital and the Company's legal name);
- approving mergers, de-mergers or transformations, or the Company's liquidation;
- fully or partially cancelling pre-emptive rights upon an increase of authorised capital;
- approving or rejecting Supervisory Board and Board of Directors' proposals regarding the utilisation of profits, or if these bodies cannot provide a joint proposal, making a decision about the utilisation of net profits;
- electing and dismissing Supervisory Board members;
- establishing a code of conduct for Supervisory Board members;
- approving reports of the Supervisory Board and Board of Directors;
- deciding on the compensation of Supervisory Board members;
- deciding on the participation in litigation against members of the Supervisory Board and Board of Directors, including the appointment of a representative in such litigation;
- deciding on the acquisition (if such transaction falls outside the scope of routine economic activity of the Company), alienation, exchange, write-off (or such related transactions) or other encumbrance of the Company's properties, the value of which is more than two per cent. of the authorised capital of the Company;
- making investments, the value of which separately, or in the aggregate, exceeds one per cent. of the authorised capital of the Company;
- approving the Company's annual accounts;
- deciding on other issues provided by law;
- electing the auditors;

- establishing and liquidating the Company's subsidiaries and branches;
- issuing or terminating proxies;
- appointing and dismissing trade proxies (*procuras*) and trade representatives (*procurists*);
- approving the appointment and dismissal of members of the Board of Directors;
- borrowing funds in excess of one per cent. of the Company's authorised capital, as at the end of the previous calendar month; and
- securing the credit and loans taken by the Company or any other person and issuing guarantees or other kinds of collateral, the value of which exceeds one per cent. of the authorised capital of the Company.

According to the Charter, decisions on all other issues are made by the Supervisory Board and the Board of Directors within their respective capacities. Resolutions in relation to the above require holders of more than 50 per cent. of the voting shares attending or represented at the GMS to vote in favour to be passed, save for those matters which require the votes of 75 per cent. of the shareholders, which include the approval and amendments of the Company's Charter, mergers, demergers or transformations, the Company's liquidation and the full or partial cancellation or pre-emptive rights upon an increase of authorised capital.

Supervisory Board

In accordance with the Charter, it is the responsibility of the Supervisory Board to supervise the activities of the Board of Directors.

The tasks and competencies of the Supervisory Board include, but are not limited to:

- supervising the activities of each of the members of the Board of Directors;
- appointing and discharging the Chief Executive Officer and other members of the Board of Directors, subject to approval of the candidates by the GMS in accordance with the Charter, and devising a code of conduct for the members of the Board of Directors;
- approving and amending the Company's policies and other regulatory documents;
- inspecting the Company's books and property, including, without limitation, inspecting the conditions of the Company's cash securities and goods personally or through its members or invited experts;
- requesting reports on the Company's activities from the Board of Directors (including dealings with its associated companies and subsidiaries) and reviewing the information provided by the internal audit department or as a result of external inspections;
- convening an EGM, if necessary and for the benefit of the Company;
- reviewing annual reports and proposals of the Board of Directors relating to the distribution of profits;
- approving the Company's annual budget; and
- making decisions in other cases provided by applicable laws.

The Supervisory Board has created an audit committee, a nomination committee and a remuneration committee in accordance with its charter. The Supervisory Board may decide to create other committees, the composition and tasks of which will be determined by the Supervisory Board through the adoption of terms of reference. Committees report their conclusions and recommendations to the Supervisory Board.

The Supervisory Board consists of ten members, including two executive members and two independent members. Members of the Supervisory Board may be appointed and dismissed at a GMS. Unless otherwise specified at a GMS, each member of the Supervisory Board is elected for a period of one year. There is, however, no statutory limit as to the number of occasions on which such appointment may be renewed. The Supervisory Board, as well as each holder of voting shares, is entitled to propose nominees for election to the Supervisory Board. A member of the Board of

Directors may also serve as a member of the Supervisory Board simultaneously; however, members of the Board of Directors may not hold a majority of the seats on the Supervisory Board. Meetings of the Supervisory Board are held at least once per quarter. Each member of the Supervisory Board has one vote and resolutions are passed by a simple majority of votes and in the case of an equality of votes, the Chairman of the Supervisory Board meeting shall have a casting vote.

The Supervisory Board shall make determinations as to the independence of the members of the Supervisory Board and shall state its reasoning if this determination is made notwithstanding certain factors regarding the independence of members listed in the Charter.

As at the date of this Prospectus, the Company's Supervisory Board consists of the following members:

Name	Age	First Appointed	Current Position
Giorgi Bezarashvili........................	40	2009	Chairman of the Supervisory Board
Mikheil Gogishvili.........................	45	2010	Deputy Chairman of the Supervisory Board
Irakli Ezugbaia	34	2011	Member of the Supervisory Board, Chief Executive Officer
Giorgi Gagnidze	32	2011	Member of the Supervisory Board, Chief Financial Officer
Vladimer Gegelashvili..................	33	2010	Member of the Supervisory Board
Pridon Rukhaia.............................	54	2008	Member of the Supervisory Board
Megi Gotsiridze............................	42	2008	Member of the Supervisory Board
Giorgi Ukleba...............................	41	2008	Member of the Supervisory Board
Clifford S. Isaak	55	2011	Member of the Supervisory Board (independent member)
Levan Surguladze.........................	51	2011	Member of the Supervisory Board (independent member)

Giorgi Bezarashvili. Mr. Bezarashvili was born in 1971 and qualified as a Civil Engineer (Water-Supply and Drainage) from the Technical University of Georgia in 1994. In 1998, he graduated from the College of Government Officials with a qualification in Constitutional Law and Legislative Activity. He began his career in 1988 as a technician with the Project Institute Sakagromrecvmsheni. In 1994, Mr. Bezarashvili worked as a Provision Chief at the Svetitskhoveli Firm. From 1994 to 2002, he worked as a Master of Network for Municipal Production at Tbilckalkanali. In 2002, he worked as a mechanical engineer for Tbiltskalkanali LLC Control Dispatching Service. From 2002 to 2004, he worked as Deputy Chief of the Water-Supply Operation Service at Tbiltskalkanali LLC. Between 2004 and 2008, Mr. Bezarashvili served as a Member of the Georgian Parliament and as Vice-President of the Committee of Natural Resources and Environment. From 2008 to 2009 he served as Chairman of the Supervisory Board of the Tbilisi International Airport. In 2009, Mr. Bezarashvili was appointed to his current position as Chairman of the Supervisory Board.

Mikheil Gogishvili. Mr. Gogishvili was born in 1966 and graduated from the Faculty of International Law and International Relations of the Tbilisi State University. In 1993, he began his career as a specialist at the Legal Department of the Apparatus of the Parliament of Georgia. In 1995, he served as State Adviser to the Head of the State Legal Department. From 1995 to 1999, he served as State Adviser to the President of Georgia in relation to the Parliament Concerning Legislative State Affairs with the Chancellery of Georgia. From 1999 to 2000, Mr. Gogishvili served as a Judge of the Chamber of Administrative Affairs at the Tbilisi District Court. In 2000, he was appointed as a Judge at the Supreme Court of Georgia (Chamber of Civil, Enterprise, and Insolvency Affairs). In June 2005, he was appointed Deputy Head of the Supreme Court of Georgia and Head of the Civil Law Chamber. In 2010, he was appointed as a member of the Supervisory Board, and, in September 2011, he was appointed Deputy Chairman of the Supervisory Board.

Irakli Ezugbaia. Mr. Ezugbaia was born in 1978 and graduated from the Caucasus School of Business with a Master of Business Administration in Finance in 2006. He graduated from the Georgian Technical University in 2002 with a Master of Economics in International Economic Relations. In 2001, he completed the Management Development Programme at the Caucasus School of Business. In 1997, he completed the Accounting and Taxation system training at the Institute of Social and Economic Research. He began his career in 1997 as an economist-consultant with the non-governmental organisation "Alliance of Farmers". From 1998 to 2000, he was a senior consultant for the Chief of Relations of the Department of West Countries at the Centre of International Affairs. From 2000 to 2001, he worked as Financial Administrator with JSC "AES-Telasi". From 2001 to 2003, he worked as a Digomi Business-Center Manager with JSC "AES-Telasi". In 2005, Mr. Ezugbaia was the Adviser to the Prime Minister of Georgia. In 2005, he was appointed as Chief Financial Officer of the Company and to his current positions as Chief Executive Officer and member of the Board of Directors of the Issuer. Mr. Ezugbaia is currently undertaking a course in major programme management and financial strategy at the Said Business School, University of Oxford. Mr Ezugbaia was appointed an Executive Director of the PF upon its establishment in June 2011. In October 2011, he resigned from this position, although he still serves as Adviser to the Executive Director of the PF. In 2011, Mr. Ezugbaia was appointed as a member of the Supervisory Board. In May 2012, Mr. Ezugbaia was appointed as a director of JSC Nenskra, a subsidiary of the PF.

Giorgi Gagnidze. Mr. Gagnidze was born in 1979 and graduated from the Faculty of Management and Microeconomics of the Iv. Javakhishvili State University of Tbilisi and from the Caucasus School of Business in Tbilisi with a major in finance and accounting. In 2001, he began his career as a region business analyst with JSC "AES-Telasi". In 2001 and 2002, he worked at JSC Bank of Georgia and in 2002 and 2003 he worked as the Financial Conduct and International Relations Director of Advertising Company Imperial. From 2003 to 2005, he served as a Finance Officer and then as Senior Finance Officer of JSC "AES-Telasi". Mr. Gagnidze joined the Company in 2005 as the Deputy Finance Director, and has been the Chief Financial Officer since 2006. In 2011, he was appointed as member of the Supervisory Board.

Vladimer Gegelashvili. Mr. Gegelashvili was born in 1978 and received a BBA in international economic relations from the Gori State University in 2000. He undertook further studies in law between 2000 and 2003 at Iv. Javakhishvili State University of Tbilisi. He began his career in 2003 as the chairman of the Gori Regional Department of Youth Issues, State Department of Georgia. From 2004 to 2007, he served as a member of the Georgian Parliament. In 2007 and 2008, he served as an attorney in the regional administration of Shida-kartli. From 2004 to 2008, Mr. Gegelashvili served as Deputy Minister of the Ministry of Environmental Protection and Natural Resources. In 2010, he was appointed as a member of the Supervisory Board.

Megi Gotsiridze. Ms. Gotsiridze was born in 1970 and graduated from the Department of Electrochemistry Technology of the Georgian Technical University in 1988. She began her career in 1987 as an assistant kindergarten tutor. From 1993 to 2001, she worked as a laboratory assistant with the Department of Inorganic Chemistry at the Georgian Technical University. From 1999 to 2001, she was a Director of "Qedani" Ltd. In 2002, she worked for the Red Cross Organisation of Georgia. From 2002 to 2004, she was Chairman of the non-governmental organisation "Gza Momavlisa". In 2004, she served as Head of the Pension Fund of the Isani-Samgori region of the United State Fund of Social Insurance of Georgia. From 2004 to 2008, Ms. Gotsiridze served as a member of the Parliament of Georgia. In 2008, she was appointed as a member of the Supervisory Board.

Pridon Rukhaia. Mr. Rukhaia was born in 1958 and graduated from the Georgian Polytechnical Institute in 1976. From 1978 to 1979, he worked at the Preparatory Department of the Georgian Polytechnical Institute. From 1979 to 1984, he worked in the Department of Geology at the Georgian Polytechnical Institute. Mr. Rukhaia started his career in 1986 as an assistant at the Georgian Polytechnical Institute. Between 1991 and 1995, he was a senior teacher at the Georgian Polytechnical Institute. From 1995 to 1996, he worked as an inspector with the Transport Police Department of the Ministry of Internal Affairs of Georgia and from 1996 to 2000, he was the Head of the Transport Police Department. In 2000 and 2002, he worked as an inspector for the Anti-Corruption and Economic Crime Department of the Ministry of Internal Affairs of Georgia. In 2001 and 2002, he was Head of Customs at "Poti". From 2002 to 2003, he was Head of Regional Customs at "Dasavleti". In 2008, Mr. Rukhaia was appointed as a member of the Supervisory Board.

Giorgi Ukleba. Mr. Ukleba was born in 1971 and qualified as Technical Engineer from the Kutaisi Technical University in 1989. He graduated from the Tbilisi Political Academy with a degree in Political Science in 2000. He began his career in 1987 as an Administrator for the Railway Club. From 1997 to 2001, he worked for the non-governmental organisation "The Club of Young Political Scientists". Between 1999 and 2000, he worked as Head of Section at the JSC "SakKvesadgurMsheni". Since 2002, he has served as a member of the United National Movement. From 2004 to 2008, he served as a member of Parliament of Georgia. In 2008, he was appointed as a member of the Supervisory Board.

Clifford S. Isaak. Mr. Isaak was born in 1956 and graduated from Red River College, Winnipeg, Canada with a degree in Business Administration in 1978 and received a Certified General Accounting Designation in Canada in 1982. In 1981, he began his career as an accountant with a local practice in Saskatchewan, Canada, purchasing the practice in 1983 and subsequently selling it to Coopers & Lybrand, Saskatoon in 1988. He served as Vice-President of Business Administration at Briercrest Schools from 1988 to 1992, and subsequently was a Financial and Management Consultant with Isaak International from 1992-1994. From 1994 to 1995, he was a Senior Consultant with Ernst & Young and was then the Chief Financial Officer of Kyrgyz Agribusiness Company from 1995 to 1997. Mr. Isaak was the Chief of Party for a USAID accounting reform project in Kyrgyzstan from 1997 to 1999 and he subsequently worked at the World Bank as a Senior Financial Management Specialist from 1999 to 2002. Mr. Isaak worked for PricewaterhouseCoopers from 2004 to 2009, first as a Managing Director and finally as the Managing Partner, Caucasus Region. At PricewaterhouseCoopers, Mr. Isaak was responsible for Armenia, Azerbaijan and Georgia. He also oversaw the opening of a new office in Ulanbaatar, Mongolia and worked on the opening of a new office in Ashgabat, Turkmenistan. Since 2009, he has run his own consulting and advisory business in Tbilisi. In 2011, he was appointed as an independent member of the Supervisory Board.

Levan Surguladze. Mr. Surguladze was born in 1958 and received a B.S. and M.S. in physics from Moscow State University. Mr. Surguladze also received a Ph.D. in physics from the National Academy of Sciences, Moscow and an M.B.A. in finance and financial engineering from the Graduate School of Business, University of Alabama. In 1990, he began his career as a Research Associate at the Moscow Institute for Nuclear Research, and in 1991 and 1992, he was a visiting scientist at several universities and scientific institutes in Europe and the United States. From 1995 to 1999, he was a research associate and senior research associate at two universities in the United States. From 1999 to 2000, Mr. Surguladze was a Trade Risk Manager for the American Stock Exchange and in 2000 to 2001 he was a Senior Vice President/Consultant for Deutsche Bank, London in their global credit derivatives department. From 2001 to 2002, he was a Senior Vice President/Consultant, Risk Finance for Barclays Capital, New York. From 2002 to 2007, he was the Director, Risk Control of UBS Investment Bank, New York. Since 2007, he has been the Managing Director of CFS Finance. In 2009, he was appointed as a member of the board of the Financial Supervision Agency of Georgia until its liquidation in December 2009. In 2011, he was appointed as an independent member of the Supervisory Board.

The business address of each of the members of the Supervisory Board is the registered office of the Company at 15, Tamar Mepe Avenue, Tbilisi 0112, Georgia.

Board of Directors

The Board of Directors is an executive body, which is responsible for the day-to-day management of the Company (with the exception of the functions reserved to the GMS and the Supervisory Board), and, pursuant to the Charter, consists of the Chief Executive Officer and at least three additional members. The members of the Board of Directors are appointed and dismissed by the Supervisory Board with the prior approval of the GMS. The Supervisory Board approves the remuneration and other conditions of employment for each member of the Board of Directors. Certain resolutions of the Board of Directors are subject to the approval of the Supervisory Board.

Responsibilities of the Board of Directors include:

- conducting and carrying out the Company’s current activities;
- presenting the draft business plan of the Company for the current year to the Supervisory Board for approval, within one month of the end of the fiscal year;
- supervising the functioning of the Company’s affiliates and subsidiaries and ensuring that the managers fulfil their tasks and functions;
- reviewing the information provided by the Company’s internal audit department or received as a result of external inspections, reviewing reports submitted by the managers of the Company’s subsidiaries and affiliates, and making appropriate decisions based on such information;
- ensuring the fulfilment of the resolutions made by the GMS and the Supervisory Board;
- developing policies, office rules and any other regulations, which are approved by the Supervisory Board and ensuring compliance with such policies, rules and regulations;
- deciding on the selection, dismissal, training and remuneration of staff;
- dealing with any other issues assigned to the Board of Directors (or its individual members) by the Supervisory Board or the GMS; and
- fulfilling the requirements set forth in the Charter and applicable laws.

In addition, the following activities may be carried out by the Board of Directors, provided that the approval of the Supervisory Board has been obtained:

- acquiring (if such transaction falls outside the scope of the routine economic activity of the Company) alienating, writing-off or encumbering real estate and property ownership rights, if the value of such transaction does not exceed two per cent. of the Company's authorised capital;

- making investments, which alone, or in the aggregate, do not exceed one per cent. of the Company's authorised capital;

- borrowing funds or credit in an amount up to one per cent. of the Company's authorised capital;

- providing collateral, guarantee(s) or any other security to support borrowing by the Company or any other person, the value of which does not exceed one per cent. of the Company's authorised capital;

- launching new activities or terminating or suspending existing activities;

- determining general principles of business strategy and the business plan of the Company and the development and approval of the annual budget and long-term liabilities;

- determining the remuneration or additional benefits of the Company's senior management (i.e., the Chief Executive Officer and other members of the Board of Directors, as well as any other top-level managers so selected by the Supervisory Board); and

- other activities that may be defined by applicable laws.

The Board of Directors is headed by the Chief Executive Officer. The Chief Executive Officer is responsible for chairing meetings of the Board of Directors, supervising the implementation of decisions of the Board of Directors, the Supervisory Board and the GMS, assigning tasks to the Board of Directors members and to other managers of the Company and issuing relevant orders, instructions and other directives for these purposes.

As at the date of this Prospectus, the Company's Board of Directors consists of the following members:

Name	**Age**	**First Appointed**	**Position with the Company**
Irakli Ezugbaia	34	2005	Chief Executive Officer
David Jinjolia	32	2005	Director of Freight SBU
Temur Bulia	50	2007	Director of Passenger SBU
Giorgi Gurgenidze	30	2007	Director of Infrastructure SBU

Irakli Ezugbaia. See "—*Supervisory Board*".

David Jinjolia. Mr. Jinjolia was born in 1980 and graduated with a degree in International Economics from the Georgian Technical University in 2003. He graduated from the Tbilisi State University in 2001 with a BBA in Labour Force Management. In 2000, he pursued U.S. Common and Contract Law studies as part of the Civil Education Project of the Central European University. Mr. Jinjolia graduated from the Caucasus School of Business in 2001 with a BBA in Finance and Accounting. In 1997, he began his career working as Manager of Employment and Vice-President of the Youth Fund Center of Employment. From 1999 to 2000, he worked as Marketing Manager of "Personal Service" Ltd. From 2000 to 2002, he worked as Regional Finance Manager of JSC "AES-Telasi". In 2002, he was Head of Regional Commission of Claims and Dispatches with JSC "AES-Telasi". From 2002 to 2003, Mr. Jinjolia was the Planning and Institutional Development Project Manager of JSC "TbilUniversalBank". In 2003, he worked as the Planning and Analyses Group Leader with JSC "AES-Telasi". In 2003, he was Revenue Department Manager for JSC "AES-Telasi". From 2003 to 2004, Mr. Jinjolia worked as Head of the Financial Department of JSC "AES-Telasi". In 2004, he worked as Deputy Director in the Corporate Solution Department of "United Global Technologies" Ltd. From 2005 to 2006, he served as adviser to the Minister of Economics and Privatisation of Georgia. In 2005, he was Deputy General Director and the General Director of JSC "Tbilgazi". In 2005, he was appointed to his current position as Director of the Freight SBU of the Company and as a member of the Board of Directors.

Temur Bulia. Mr. Bulia was born in 1961 and graduated from the Georgian Technical University in 1983, as an engineer in hydro-technical construction. In 2000, he graduated as an economist from the Finance and Credit Faculty of the Economic-Humanitarian Institute of Georgia. From 1989 to 1996, he worked as Deputy General Director and Technical Director for the Research-and-Production Community "Complex". Between 1996 and 1999, he served as Deputy Public Attorney of Samtskhe-Javakheti, Manager of socio-economic development programmes and Chairman of the Permanent Committee on Georgian-Turkish Border Issues. From 1999 to 2004, Mr. Bulia served as Deputy Director of the Examination and Utilisation Department, Counselor of State and Head of the Accounting Documentations Department at the Ministry of Finance of Georgia. From 2005 to 2007, he served as Deputy Director, Head of the Transportation Management and Operations Department of the Passenger Operations Branch of the Company. In 2007, he was appointed to his current position as Director of the Passenger SBU of the Company and as a member of the Board of Directors.

Giorgi Gurgenidze. Mr. Gurgenidze was born in 1982 and graduated from the Tbilisi State University, having specialised in international law and received his qualification as a lawyer in 2004. In 2005 he graduated from the Georgian Institute of Public Affairs, School of Public Administration with a Masters in Public Administration. He began his career in 2002 by working as an assistant to a judge at the Supreme Court of Georgia. From 2005 to 2006, he worked as a senior specialist in the Department of Legal Affairs of the Company. In 2006, he was appointed Head of the Department of Court and Law Enforcement Affairs of the Company. From 2006 to 2007, he was appointed the Head of the Procurement Agency of the Company. In 2007, he served as an adviser to the Director General of the Company. In 2007, Mr. Gurgenidze was appointed Deputy and Acting Director of Infrastructure of the Company. In 2007, he was appointed to his current position as Director of the Infrastructure SBU of the Company and as a member of the Board of Directors.

The business address of each of the members of the Board of Directors is the registered office of the Company at 15, Tamar Mepe Avenue, Tbilisi 0112, Georgia.

Senior Management

The senior management of the Company is comprised of the members of the Board of Directors and the Chief Financial Officer, Giorgi Gagnidze, who is a member of the Supervisory Board.

Corporate Governance

Georgia has not adopted a code of corporate governance and, therefore, the Company is not subject to the requirements of any national corporate governance rules. Furthermore, as a company incorporated in Georgia, the Company is not subject to the U.K. Corporate Governance Code issued by the Financial Reporting Council. See "*Risk Factors—Risks related to the Company's Business—The Company is not subject to mandatory corporate governance requirements*".

As a matter of best practice, however, the Company has adopted and intends to comply with certain corporate governance structures and procedures. In August 2011, two independent members were appointed to the Supervisory Board. The Supervisory Board established an Audit Committee in February 2010 and a Nomination Committee and Remuneration Committee in September 2011. Over the medium term, the Company aims to have half of the Supervisory Board comprised of independent members and all members of the board committees be independent, however it has not set a specific timeframe as it may take time to find candidates that the Company believes will add value to the Company and the board.

Audit Committee

In February 2010, the Supervisory Board established the Audit Committee, which is an advisory body of and reports to the Supervisory Board. In September 2011, the Supervisory Board adopted new terms of reference for the Audit Committee. The members of the Audit Committee are:

Name	Position
Clifford S. Isaak	Chairman of the Audit Committee (independent member)
Mikheil Gogishvili	Member of the Audit Committee
Giorgi Ukleba	Member of the Audit Committee

Pursuant to its terms of reference, the Audit Committee shall comprise three members from among, and selected by, the Supervisory Board on the recommendation of the Nomination Committee and in consultation with the Chairman of the Audit Committee. At least one member of the Audit Committee shall be an independent member of the Supervisory Board and at least one member shall have recent and relevant financial experience. Appointments to the Audit Committee shall be for a period of up to three years, which may be extended by two further three year periods, provided the member still meets all criteria for membership. The Audit Committee is responsible for, among other matters:

- reviewing, monitoring and presenting the financial statements and other public announcements of the Company concerning its financial position, as well as the issuer's financial processes to the Supervisory Board;

- reviewing material transactions and contracts entered between or among the Company, or any subsidiary of the Company, and a related party;

- conducting certain review functions following the completion of the annual audit;

- selecting, monitoring and working with the Company's external auditors;

- reviewing and monitoring the Company's risk management and internal control processes, policies and procedures;

- conducting appointment and monitoring functions in relation to the Company's internal audit department; and

- other matters as contained in the Audit Committee's terms of reference or referred to it by the Supervisory Board.

Nomination Committee

In September 2011, the Supervisory Board established the Nomination Committee, which is an advisory body of and reports to the Supervisory Board. The members of the Nomination Committee are:

Name	Position
Mikheil Gogishvili	Chairman of the Nomination Committee
Pridon Rukhaia	Member of the Nomination Committee
Levan Surguladze	Member of the Nomination Committee (independent member)

- The Nomination Committee shall comprise three members from among, and selected by, the Supervisory Board. At least one member of the Nomination Committee shall be an independent member of the Supervisory Board. Appointments to the Nomination Committee shall be for a period of up to three years, which may be extended for two three-year periods, provided the member still meets all criteria for membership. The Nomination Committee is responsible for, among other matters:

- conducting certain functions in relation to the review of the structure and performance of the Supervisory Board and Board of Directors;

- recommending candidates for appointment to the Supervisory Board and Board of Directors when vacancies arise;

- making recommendations to the Supervisory Board in relation to the appointment or reappointment of independent members of the Supervisory Board;

- making recommendations to the Supervisory Board as to retiring members of the Supervisory Board to be proposed for re-election at a GMS;
- recommending candidates for appointment to the Audit and Remuneration Committees to the Supervisory Board, in consultation with the chairmen of such committees; and
- other matters as contained in the Nomination Committee's terms of reference or as referred to it by the Supervisory Board.

Remuneration Committee

In September 2011, the Company established the Remuneration Committee, which is an advisory body of and reports to the Supervisory Board. The members of the Remuneration Committee are:

Name	**Position**
Levan Surguladze	Chairman of the Remuneration Committee (independent member)
Vladimer Gegelashvili	Member of the Remuneration Committee
Megi Gotsiridze	Member of the Remuneration Committee

The Remuneration Committee shall comprise three members from among, and selected by, the Supervisory Board on the recommendation of the Nomination Committee. At least one member of the Remuneration Committee shall be an independent member of the Supervisory Board. Appointments to the Remuneration Committee shall be for a period of up to three years, which may be extended by two further three-year periods, provided the member still meets all criteria for membership. The Remuneration Committee is responsible for, among other matters:

- reviewing, considering and agreeing proposals and providing recommendations in relation to the Company's framework and policy regarding the remuneration of certain members of the Supervisory Board, Board of Directors and other senior management;
- approving the terms of any service agreement to be entered into with any member of the Supervisory Board or Board of Directors, as well as certain terms of employment and employment contracts;
- preparing remuneration reports;
- conducting certain functions in relation to any schemes of performance-related remuneration, share incentive plans, pensions, bonus and other incentive schemes; and
- other matters as contained in the Remuneration Committee's terms of reference or as referred to it by the Supervisory Board.

Other Arrangements

The Company also has its own internal audit department with its own personnel, separate from the Company's financial departments, which reports to the Audit Committee as well as directly to the Board of Directors. In 2010, the Company commissioned an independent consultant to review and provide recommendations in relation to several global internal control processes. The Company has implemented the recommendations arising from this review, other than a small number of recommendations, predominantly relating to procurement processes, considered by Management to be inappropriate. In 2011, the Company commissioned another independent consultant to conduct a review of the Company's financial reporting procedures, which resulted in a number of recommendations being presented to the Company in relation to improvements in its internal controls, which are currently being considered and, if deemed appropriate, implemented by management. See "*Risk Factors—Risks Related to the Company's Business—The Company's accounting systems and internal controls may not be as advanced as those of companies in more developed countries*".

Compensation

The aggregate amount of remuneration paid by the Company to members of its Supervisory Board, Board of Directors and its senior management for services in all capacities provided to the Company and its subsidiaries during the years ended 31 December 2011, 2010 and 2009 was GEL 1.2 million, GEL 1.0 million and GEL 0.9 million, respectively. The increase in 2011 was primarily due to the increase in the number of Supervisory Board members in 2011.

There are no amounts set aside or accrued by the Company or its subsidiaries to provide pension, retirement or other benefits to such persons. See "*Description of the Company's Business—Employees and Pensions*"

Interests of the Members of the Supervisory Board, the Board of Directors and Senior Management

There are no actual or potential conflicts of interest between any duties owed by members of the Supervisory Board, the Board of Directors or the Company's senior management to the Company and their private interests or other duties.

TERMS AND CONDITIONS OF THE NOTES

The following are the terms and conditions in the form in which they will be endorsed on the Notes:

The issue of the Notes was authorised by a resolution of the Board of Directors of JSC Georgian Railway (the "**Issuer**") passed on 12 June 2012, by a resolution of the Supervisory Board of the Issuer passed on 14 June 2012 and by a resolution of the Issuer's shareholders passed on 15 June 2012. A fiscal agency agreement to be dated 5 July 2012 (the "**Fiscal Agency Agreement**") will be entered into in relation to the Notes between the Issuer, Citibank, N.A., London Branch, as fiscal agent and a paying and transfer agent and Citigroup Global Markets Deutschland AG, as registrar and a paying and transfer agent. The fiscal agent, the paying and transfer agents and the registrar for the time being are referred to below respectively as the "**Fiscal Agent**", the "**Paying and Transfer Agents**" and the "**Registrar**". The expression "**Paying and Transfer Agents**" shall include the Fiscal Agent. The Fiscal Agency Agreement includes the form of the Notes. Copies of the Fiscal Agency Agreement are available for inspection during normal business hours at the specified offices of the Paying and Transfer Agents. The holders of Notes (the "**Noteholders**") are deemed to have notice of all the provisions of the Fiscal Agency Agreement applicable to them.

1. **Form, Denomination, Title and Status**

(a) **Form and denomination**: The Notes are in registered form, serially numbered and in principal amounts of U.S.$200,000 and integral multiples of U.S.$1,000 in excess thereof (each, an "**authorised denomination**").

(b) **Title**: Title to the Notes will pass by transfer and registration as described in *Condition 2*. The holder (as defined below) of any Note will (except as otherwise required by law or as ordered by a court of competent jurisdiction) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it or its theft or loss (or that of the related certificate, as appropriate) or anything written on it or on the certificate in respect of it (other than a duly executed transfer thereof)) and no person will be liable for so treating the holder. For this purpose, "holder" shall mean the person in whose name a Note is registered in the Register (as defined in *Condition 2(a)).*

(c) **Status**: The Notes constitute direct, unconditional, general and (subject to *Condition 3*) unsecured obligations of the Issuer and rank, and shall at all times rank, *pari passu* and without any preference among themselves. The payment obligations of the Issuer under the Notes shall, save for such exceptions as may be provided by applicable legislation and subject to *Condition 3*, at all times rank equally in all respects with all other present and future unsecured obligations of the Issuer.

2. **Registration and Transfer of Notes**

(a) **Registration**: The Issuer will cause a register (the "**Register**") to be kept at the specified office of the Registrar outside the United Kingdom on which will be entered the names and addresses of the holders of the Notes and the particulars of the Notes held by them and of all transfers and redemptions of Notes.

(b) **Transfer**: Notes may, subject to the terms of the Fiscal Agency Agreement and to *Conditions 2(c)* and *2(d)*, be transferred in whole or in part in an authorised denomination by lodging the relevant Note (with the form of application for transfer in respect thereof duly executed and duly stamped where applicable) at the specified office of the Registrar or any Paying and Transfer Agent.

No transfer of a Note will be valid unless and until entered on the Register. A Note may be registered only in the name of, and transferred only to, a named person (or persons, not exceeding four in number).

The Registrar will within seven business days (as defined in *Condition 6(c)*), in the place of the specified office of the Registrar, of any duly made application for the transfer of a Note, deliver a new Note to the transferee (and, in the case of a transfer of part only of a Note, deliver a Note for the untransferred balance to the transferor) at the specified office of the Registrar or (at the risk and, if mailed at the request of the transferee or, as the case may be, the transferor otherwise than by ordinary mail, at the expense of the transferee or, as the case may be, the transferor) mail the Note by uninsured mail to such address as the transferee or, as the case may be, the transferor may request.

(c) **Formalities free of charge**: Any such transfer will be effected without charge subject to (i) the person making such application for transfer paying or procuring the payment of any taxes, duties and other governmental charges in connection therewith, (ii) the Registrar being satisfied with the documents of title and/or identity of the person making the application and (iii) such reasonable regulations as the Issuer may from time to time agree with the Registrar.

(d) **Closed Periods**: Neither the Issuer nor the Registrar will be required to register the transfer of any Note (or part thereof) (i) during the period of 15 calendar days ending on and including the day immediately prior to 11 July 2022 (the "**Final Maturity Date**"); or (ii) during the period of seven calendar days ending on (and including) any Record Date (as defined in *Condition 6(a)*) in respect of any payment of interest on the Notes.

3. **Covenants**

So long as any Note remains outstanding (as defined in the Fiscal Agency Agreement):

(a) **Negative pledge**: The Issuer will not, and will ensure that no Material Subsidiary will, create or permit to subsist any mortgage, charge, pledge, lien or other form of encumbrance or security interest ("**Security Interest**") (other than a Permitted Security Interest) upon the whole or any part of its present or future undertaking, assets or revenues (including any uncalled capital) to secure any Indebtedness, or any guarantee of or indemnity in respect of any Indebtedness, unless, at the same time or prior thereto, the Issuer's obligations under the Notes (i) are secured equally and rateably therewith or benefit from a guarantee or indemnity in substantially identical terms thereto, as the case may be, or (ii) have the benefit of such other security, guarantee, indemnity or other arrangement as shall be approved by an Extraordinary Resolution (as defined in the Fiscal Agency Agreement) of the Noteholders;

(b) **Reorganisation etc**.: The Issuer shall: (i) not enter into any reorganisation (as such term may be construed for the purposes of the laws of Georgia) by any method or procedure for reorganisation contemplated, or as may be contemplated from time to time, by the laws of Georgia); and (ii) ensure that no Material Subsidiary enters into any reorganisation (as such term may be construed for the purposes of the laws of Georgia or any other laws under which any such Material Subsidiary may be incorporated) by any method or procedure for reorganisation contemplated, or as may be contemplated from time to time, by the laws of Georgia or any such other laws), if, in the case of either (i) or (ii) above, any such reorganisation could reasonably be expected to be materially prejudicial to the interests of the Noteholders;

(c) **Financial statements**: (i) On the Issue Date (in respect of the audited consolidated financial statements for the financial year ended 31 December 2011) and within nine months of its most recent financial year-end, the Issuer shall send to the Fiscal Agent a copy of its audited annual consolidated financial statements for each such financial year, together with the report thereon by the Issuer's independent auditors, (ii) within 45 days of the end of each of the first three fiscal quarters of a financial year, the Issuer shall send to the Fiscal Agent a copy of its unaudited interim consolidated financial statements as at, and for the period beginning on the first day of the financial year in which such quarter falls and ending on the last day of such quarter, certified by two directors of the Issuer as presenting fairly the financial position of the Issuer and its consolidated subsidiaries as at the relevant date, and the results of operations and changes in financial position of the Issuer and its consolidated subsidiaries for the relevant period then ended, each prepared and presented in accordance with International Financial Reporting Standards ("**IFRS**") (as issued by the International Accounting Standards Board), consistently applied, and (iii) the Issuer shall procure that the Fiscal Agent delivers a copy of such financial statements, together with, in respect of any audited annual consolidated financial statements, the relevant auditors' report thereon, to any Noteholder promptly upon request by such Noteholder;

(d) **Incurrence of Financial Indebtedness**: The Issuer will not, and will not permit any Subsidiary to, Incur, directly or indirectly, any Financial Indebtedness; *provided, however,* that the Issuer and any Subsidiary will be entitled to Incur Financial Indebtedness if:

(i) after giving effect to such Incurrence and the application of the proceeds thereof, on a *pro forma* basis, no Event of Default would occur or be continuing; and

(ii) the ratio of Net Financial Indebtedness of the Issuer and its Subsidiaries as of the date of such Incurrence (for this purpose "**the date of determination**"), after giving effect to such Incurrence and the application of the proceeds thereof, on a *pro forma* basis, to the aggregate amount of EBITDA for the most recent annual financial period for which consolidated financial statements have been delivered pursuant to *Condition 3(d)* (or, prior to the delivery of the first annual consolidated financial statements following the Issue Date pursuant to Condition 3(c), EBITDA for the 12 month period ended 31 December 2011 each such annual financial period and 12 month period, a "**measurement period**"), does not exceed 3.5 to 1.

For purposes of calculating the ratio described in this *Condition 3(d)*, acquisitions that have been made by the Issuer or any Subsidiary, including through mergers or consolidations and including any related financing transactions (including, without limitation, any acquisition giving rise to the need to make such calculation as a result of the Incurrence of Financial Indebtedness), during (A) the most recent annual financial period for which audited consolidated financial statements have been delivered pursuant to *Condition 3(c)* or (B) subsequent to such annual financial period and on or prior to the date on which the ratio is to be calculated for the purpose of this *Condition 3(d)*, will be given *pro forma* effect as if they had occurred on the first day of the measurement period used in the calculation of EBITDA; *provided, however,* that (x) any such *pro forma* EBITDA in respect of an acquisition may only be so included in the calculation of EBITDA if such *pro forma* EBITDA shall have been derived from financial statements of, or relating to or including, such acquired entity, and (y) such financial statements have been prepared in accordance with IFRS, U.S. GAAP or any body of accounting principles that has been determined by the European Commission to be equivalent to IFRS (without regard to any modification to such principles that may be required after the date of such financial statements in connection with or pursuant to such determination).

(e) **Permitted Incurrence:** *Condition 3(d)* will not prohibit the Incurrence of any of the following items of Financial Indebtedness:

(i) refinancing (including successive refinancing) of Indebtedness of the Issuer or any Subsidiary outstanding on the Issue Date (including the Notes) or permitted to be Incurred under *Condition 3(d) above*; provided that the aggregate principal amount thereof is not thereby increased by more than the fees and expenses incurred or to be incurred by the Issuer or such Subsidiary in connection with such refinancing plus the amount of any premium paid or to be paid in connection with such refinancing;

(ii) inter-company Indebtedness (A) between the Issuer and any Subsidiary and (B) between any Subsidiary and another Subsidiary; provided, however, that any subsequent issuance or transfer of any Capital Stock which results in any such Subsidiary ceasing to be a Subsidiary or any subsequent disposition, pledge or transfer of such Indebtedness (other than to the Issuer or a Subsidiary) shall be deemed, in each case, to constitute the Incurrence of such Indebtedness by the obligor in respect thereof; and

(iii) Indebtedness arising out of interest rate agreements or currency hedging agreements for the benefit of the Issuer or any Subsidiary; provided that such interest rate agreements do not exceed the aggregate principal amount of the related Indebtedness and such currency hedging agreements do not increase the obligations of the Issuer or any Subsidiary other than as a result of fluctuations in interest or foreign currency exchange rates or by reason of fees, indemnities and compensation payable thereunder.

(f) **Limitation on Restricted Payments:**

(i) Subject as provided below, the Issuer will not, directly or indirectly:

(A) declare or pay any dividend, in cash or otherwise, or make any other distribution (whether by way of redemption, acquisition or otherwise) in respect of its share capital; or

(B) voluntarily purchase, redeem or otherwise retire for value any of its share capital or subordinated debt

(any such action, a "**Restricted Payment**").

(ii) Notwithstanding the foregoing, and subject as further provided below, the Issuer may make a Restricted Payment if, at the time of the relevant declaration or payment of a dividend or making of a distribution, as the case may be (A) no Event of Default, or condition, event or act, which, with the lapse of time, the expiry of any grace period or the issue, making or giving of any notice, certification, declaration, demand, determination or request or the taking of any similar action or the fulfilment of any similar condition, would constitute an Event of Default, has occurred or would result from the making of such Restricted Payment and (B) the aggregate amount of such Restricted Payment and all (if any) other Restricted Payments made since the Issue Date would not exceed 50 per cent. of the aggregate amount of the Issuer's consolidated profit and total comprehensive income for each financial year ended since the Issue Date for which financial statements have been delivered pursuant to *Condition 3(c)*, in each case, as determined by reference to the Issuer's audited consolidated financial statements prepared under IFRS for the relevant financial year and calculated on a cumulative basis for all such years.

(iii) Nothing herein shall limit the declaration or payment of any dividend or the making of any other distribution by the Issuer (A) in an aggregate amount not exceeding GEL 350 million in one or more instalments out of the aggregate amount of the Issuer's consolidated profit and total comprehensive income for each financial year ended prior to or on 31 December 2011, in each case, as determined by reference to the Issuer's audited consolidated financial statements prepared under IFRS for the relevant year and calculated on a cumulative basis for all such years; (B) in respect of any preferred stock, which may be issued by the Issuer from time to time; or (C) in respect of any share capital of the Issuer made out of the net cash proceeds of any substantially concurrent sale of, or by issuance of, share capital of the Issuer (other than share capital issued or sold to a Subsidiary or an employee stock ownership plan or to a trust established by the Issuer or any of its Subsidiaries for the benefit of their employees) or a substantially concurrent cash capital contribution to the share capital of the Issuer.

(iv) The Issuer will not permit any Material Subsidiary to declare or pay any dividend, in cash or otherwise or make any other distribution as is described in paragraph (i) above in respect of any class of share capital of such Material Subsidiary unless such dividend or distribution, as the case may be, is made on a pro rata basis to holders of such class of share capital or such dividend is declared or paid or such distribution is made, as the case may be, on a basis that results in the Issuer or another Material Subsidiary receiving a greater amount by way of such dividend or other distribution, as the case may be, than it would have received if the dividend had been paid or distribution made, as the case may be, on a pro rata basis.

(v) For the purpose of this *Condition 3(f)*, the amount of any dividend declared or paid or other distribution made, other than in cash, which is to be taken into account in any calculation required hereunder, shall be the fair market value as determined in good faith by the board of directors of the Issuer of such dividend or distribution, as the case may be, assuming (to the extent applicable in the circumstances of the relevant payment or other distribution) it was the subject of an arm's length transaction between an informed and willing seller under no compulsion to sell and an informed and willing buyer under no compulsion to buy.

The Fiscal Agent shall have no obligation towards, or relationship of agency or trust with, any Noteholder and shall not be responsible or obliged to review the contents of any financial statement referred to in Condition 3(c) above. In addition, the Fiscal Agent shall be under no obligation to enforce any obligation of the Issuer under Condition 3(c), 3(d) or 3(f).

For the purposes of these Conditions:

(i) "**Available Credit Facilities**" means, as at any date of determination, the amount available to be drawn by the Issuer under any committed credit facility available to it as at such date;

(ii) "**Capital Stock**" of any Person means any and all shares, interests (including partnership interests), rights to purchase, warrants, options, participations or other equivalents of or interests in (however designated) equity of such Person, including any Preferred Stock, but excluding any debt securities convertible into such equity;

(iii) "**Cash**" means, as at any date of determination, the amount of cash and cash equivalents of the Issuer at such date;

(iv) "**EBITDA**" means, for any period the profit before income tax for such period minus (i) net finance income, plus (ii) depreciation and amortisation and excluding (iii) impairment reversals/(losses), in each case for such period and on a consolidated basis and, to the extent provided in *Condition 3(d),* calculated in accordance with IFRS;

(v) "**Financial** Indebtedness" means:

(A) moneys borrowed;

(B) any amount raised under any acceptance credit facility;

(C) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument;

(D) the amount of any liability in respect of any lease or hire purchase contract, which would in accordance with IFRS be treated as a finance or capital lease;

(E) receivables sold or discounted (other than any receivables to the extent they are sold on a non-recourse basis);

(F) any amount raised under any other transaction (including any forward sale or purchase agreement) having the commercial effect of borrowing, which is treated as an obligation in accordance with IFRS;

(G) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, standby or documentary letter of credit or any other instrument issued by a bank or financial institution; and

(H) the amount of any liability in respect of any guarantee or indemnity for any of the items referred to in items (A) to (G) inclusive above;

(vi) "**Hedging Obligations**" means, with respect to the Issuer or any Material Subsidiary, the obligations of such entity pursuant to:

(A) any interest rate swap agreement, interest rate cap agreement or interest rate collar agreement or any other agreement or arrangement designed to protect such entity against fluctuations in interest rates; or

(B) any foreign currency futures contract or option agreement or any other agreement or arrangement designed to protect such entity against fluctuations in foreign currency rates;

(vii) "**Incur**" means issue, assume, guarantee, incur or otherwise become liable for; *provided, however*, that any Financial Indebtedness of a Person existing at the time such Person becomes a Subsidiary (whether by merger, consolidation, acquisition or otherwise) shall be deemed to be Incurred by such Person at the time it becomes a Subsidiary. The term "**Incurrence**" when used as a noun shall have the corresponding meaning. Solely for purposes of determining compliance with *Condition 3(d)*:

(A) amortisation of debt discount or the accretion of principal with respect to a non interest-bearing or other discount security;

(B) the payment of regularly scheduled interest in the form of additional Indebtedness of the same instrument or the payment of regularly scheduled dividends on Capital Stock in the form of additional Capital Stock of the same class and with the same terms;

(C) the obligation to pay a premium in respect of Indebtedness arising in connection with the issuance of a notice of redemption or the making of a mandatory offer to purchase such Indebtedness; and

(D) any additional Financial Indebtedness, not covered by (A) to C) (inclusive) above, not to exceed U.S.$15,000,000 at any time outstanding,

will not be deemed to be the Incurrence of Financial Indebtedness;

(viii) "**Indebtedness**" means any present or future indebtedness for moneys borrowed or raised (whether or not evidenced by bonds, debentures, notes or other similar instruments);

(ix) "**Issue Date**" means 5 July 2012;

(x) "**Material Subsidiary**" means, at any time, any Subsidiary:

(A) whose total assets exceed 5 per cent. of the consolidated total assets of the Issuer; or

(B) whose total revenues exceed 5 per cent. of the consolidated total revenues of the Issuer;.

For these purposes:

(C) all calculations shall be determined in accordance with IFRS in the preparation of:

(x) the then latest annual audited consolidated financial statements of the relevant Subsidiary (in the case of a Subsidiary preparing consolidated financial statements) or the then latest annual audited non-consolidated financial statements of the relevant Subsidiary (in the case of a Subsidiary preparing non-consolidated financial statements); and

(y) the then latest annual audited consolidated financial statements of the Issuer;

(D) upon a Material Subsidiary transferring all or substantially all of its assets or business to another Subsidiary, the transferor shall cease to be a Material Subsidiary on the effective date of such transfer and thereupon the transferee shall be deemed to be a Material Subsidiary until the date of its next annual audited consolidated financial statements or, as the case may be, annual audited non-consolidated financial statements, after which whether it is or is not a Material Subsidiary shall be determined in accordance with paragraphs (A) and (B) above; and

(E) subject to paragraph (D) above, if, as a result of any transfer, reconstruction, amalgamation, reorganisation, merger or consolidation, a company, which satisfied either of the tests set forth in paragraphs (A) or (B) above immediately before such transfer, reconstruction, amalgamation, reorganisation, merger or consolidation, no longer satisfies either such test immediately after such transfer, reconstruction, amalgamation, reorganisation, merger or consolidation, such company shall immediately cease to be a Material Subsidiary;

(xi) "**Net Financial Indebtedness**" means, as at any date of determination and with respect to any Person, the aggregate amount of Financial Indebtedness less (A) Cash and (B) Available Credit Facilities, in each case of such Person and as of such date;

(xii) "**Permitted Security Interest**" means:

(A) any Security Interest outstanding as of the Issue Date;

(B) any Security Interest granted in favour of the Issuer by any Material Subsidiary;

(C) any Security Interest arising by operation of law which has not been foreclosed or otherwise enforced against the assets to which it applies;

(D) any Security Interest upon assets created for the purpose of financing the acquisition of such assets;

(E) any Security Interest existing on assets at the time of their acquisition or securing Indebtedness of a person existing at the time that such person is merged into or consolidated with the Issuer or becomes a Material Subsidiary, provided that such Security Interest (x) was not created in contemplation of such acquisition, merger or consolidation or event and (y) in the case of a merger or consolidation, does not extend to any assets or property of the Issuer or any Material Subsidiary, as the case may be (other than those of the person acquired and its subsidiaries (if any));

(F) any Security Interest created for the purpose of any Project Financing provided that such Security Interest is upon (x) assets which are the subject of such Project Financing and (y) revenues or claims which arise from the operation, failure to meet specifications, exploitation, sale or loss of, or failure to complete, or damage to, such assets;

(G) any Security Interest granted pursuant to Hedging Obligations of the Issuer or a Material Subsidiary;

(H) any right of set-off, a right to combine accounts or any analogous right, which any bank or other financial institution may have relating to any credit balance of the Issuer or any Material Subsidiary;

(I) any Security Interest incurred, or pledge and deposit in connection with workers' compensation, unemployment insurance and other social security benefits, and leases, appeal bonds and other obligations of substantially similar nature in the ordinary course of business;

(J) any Security Interest for ad valorem, income or property taxes or assessments and similar charges, which either is not delinquent or is being contested in good faith by appropriate proceedings for which the Issuer has set aside on its books reserves to the extent required by IFRS;

(K) any easement, right of way, restriction (including zoning restriction), reservation, permit, servitude, minor defect or irregularity in title and other similar charge or encumbrance, and any Security Interest arising under leases or subleases granted to others, in each case not interfering in any material respect with the business of the Issuer or any Material Subsidiary and existing, arising or incurred in the ordinary course of business;

(L) any Security Interest not otherwise permitted by the preceding paragraphs (A) to (K) (inclusive), provided that the aggregate principal amount of the Indebtedness secured by such Security Interest does not at any time exceed the greater of U.S.$25,000,000 or 2 per cent. of the consolidated total assets of the Issuer, as determined by reference to the audited consolidated balance sheet of the Issuer prepared in accordance with IFRS as at the end of the most recent financial year of the Issuer; or

(M) the renewal or extension of any Security Interest described in the preceding paragraphs (A) to (L) (inclusive), provided that (x) the principal amount of the Indebtedness secured thereby is not increased, (y) such renewal or extension shall be no more restrictive than the original Security Interest and (z) the Security Interest has not been extended to any additional assets;

(xiii) "**Person**" means any individual, company, corporation, firm, partnership, joint venture, association, unincorporated organisation, trust or other judicial entity, including, without limitation, any state or agency of a state or other entity, whether or not having separate legal personality;

(xiv) "**Preferred Stock**" of any Person, means Capital Stock of any class or classes (however designated) which is preferred as to the payment of dividends or distributions, or as to the distribution of assets upon any voluntary or involuntary liquidation or dissolution of such Person, over shares of any other class of Capital Stock of such Person;

(xv) "**Project Financing**" means any arrangement for the provision of funds which are to be used solely to finance the acquisition, construction, development or exploitation of any assets pursuant to which the persons providing such funds agree that the principal source of repayment of such funds will be the project and the revenues (including insurance proceeds) generated by such project; and

(xvi) **Subsidiary**" means any entity whose financial statements at any time are required by law or in accordance with IFRS to be fully consolidated with those of the Issuer.

4. Interest

Each Note bears interest from and including the Issue Date at the rate of 7.75 per cent. per annum payable semi-annually in arrear in equal instalments of U.S.$38.75 per U.S.$1,000 in principal amount of the Notes on 11 January and 11 July in each year (each an "**Interest Payment Date**"), except that the first payment of interest, to be made on 11 January 2013, will be in respect of the period from and including the Issue Date to but excluding 11 January 2013 and will be U.S.$40.04 per U.S.$1,000 in principal amount of the Notes. Each Note will cease to bear interest from and including the due date for redemption thereof unless, upon due presentation, payment of principal is improperly withheld or refused. In such event it shall continue to bear interest at such rate (both before and after judgment) up to but excluding whichever is the earlier of (i) the day on which all sums due in respect of such Note up to that day are received by or on behalf of the relevant holder and (ii) the day which falls seven days after the Fiscal Agent has notified Noteholders of receipt of all sums due in respect of all the Notes up to that seventh day (except to the extent that there is failure in the subsequent payment to the relevant Noteholders under these Conditions).

If interest is required to be calculated for a period of less than an Interest Period (as defined below), it will be calculated on the basis of a 360-day year consisting of 12 months of 30 days each and, in the case of an incomplete month, the actual number of days elapsed. The period beginning on and including the first Interest Payment Date and ending on but excluding the second Interest Payment Date and each successive period beginning on and including an Interest Payment Date and ending on but excluding the next succeeding Interest Payment Date is called an "**Interest Period**".

5. Redemption and Purchase

(a) **Redemption**: Unless previously redeemed or purchased and cancelled, the Notes will be redeemed at their principal amount on the Final Maturity Date, together (if applicable) with interest accrued and unpaid to but excluding the Final Maturity Date.

(b) **Redemption at the Option of Noteholders (Put Option)**: If a Change of Control Event (as defined below) occurs, the Issuer shall, at the option of the holder of any Note, upon the holder of such Note giving notice to the Issuer as provided in *Condition 5(c)* at any time during the Redemption Period, redeem such Note on the Redemption Date at its principal amount together (if applicable) with interest accrued and unpaid to but excluding the Redemption Date.

(c) **Change of Control Notice**: Immediately upon the Issuer becoming aware that a Change of Control Event has occurred, the Issuer shall give notice (a "**Change of Control Notice**") to the Noteholders in accordance with *Condition 13* specifying the nature of the Change of Control Event and the procedure for exercising the put option contained in *Condition 5(b)*.

To exercise the put option pursuant to *Condition 5(b)*, a holder must deposit the certificate representing the Note(s) to be redeemed with the Registrar or any Paying and Transfer Agent at its specified office, together with a duly completed option exercise notice ("**Exercise Notice**") in the form obtainable from any Paying and Transfer Agent or the Registrar within the Redemption Period. An Exercise Notice, once given, shall be irrevocable.

If 90 per cent. or more in principal amount of the Notes then outstanding has been redeemed pursuant to *Condition 5(b)*, the Issuer may, on not less than 30 or more than 60 days' notice to the Noteholders given within 30 days after the Redemption Date, redeem, at its option, the remaining Notes as a whole at their principal amount, together with interest accrued and unpaid to but excluding the date of such redemption. Such notice to the Noteholders shall specify the date fixed for redemption, the redemption price and the manner in which redemption will be effected.

For the purpose of this *Condition 5*:

(i) a "**Change of Control Event**" will occur if at any time Georgia ceases to own, directly or indirectly, more than 50 per cent. of the issued share capital of the Issuer or otherwise ceases to control, directly or indirectly, the Issuer. For the purpose of this Condition, Georgia will be deemed to "control" the Issuer if (whether directly or indirectly and whether by the ownership of share capital, the possession of voting power, contract, trust or otherwise) it or its government (or any entity controlled by its government) has the power to appoint and/or remove the majority of the members of the board of directors or other governing body of the Issuer or otherwise controls, or has the power to control, the affairs and policies of the Issuer;

(ii) "**Redemption Date**" means, in respect of any Note, the date which falls 14 days after the date on which the relevant holder exercises its option in accordance with this *Condition 5*; and

(iii) "**Redemption Period**" means the period from and including the date on which a Change of Control Event occurs (whether or not the Issuer has given a Change of Control Notice in respect of such event) to and including the date falling 60 days after the date on which such Change of Control Notice is given, provided that if no Change of Control Notice is given, the Redemption Period shall not terminate.

(d) **Purchase**: The Issuer or any Subsidiary may at any time purchase Notes in the open market or otherwise at any price. Any Notes so purchased, while held by or on behalf of the Issuer or any Subsidiary, shall not entitle the holder to vote at any meeting of Noteholders and shall not be deemed to be outstanding for the purposes of calculating quorums at meetings of Noteholders or for any other purpose pursuant to *Conditions 8* or *11*.

(e) **Cancellation**: All Notes purchased by or on behalf of the Issuer or any Subsidiary may be cancelled or held and resold, provided that any Notes so purchased, while held by or on behalf of the Issuer or any Subsidiary, shall not entitle the holder to vote at any meeting of the Noteholders. Any Notes so purchased and cancelled may not be re-issued or resold.

6. Payments

(a) **Method of payment**: Payment of principal in respect of the Notes will be made to the persons shown in the Register at the close of business on the Record Date and subject to the surrender of the Notes at the specified office of any Paying and Transfer Agent. Payments of interest will be made to the persons shown in the Register at close of business on the relevant Record Date. For this purpose, "**Record Date**" means the seventh business day, in the place of the specified office of the Registrar, before the due date for the relevant payment. Each such payment will be made by transfer to a U.S. dollar account maintained by the payee with a bank in outside the United States.

(b) **Payments subject to fiscal laws**: All payments are subject in all cases to any applicable fiscal or other laws and regulations, but without prejudice to the provisions of *Condition 7*. No commissions or expenses shall be charged to the Noteholders in respect of such payments.

(c) **Delay in payment**: Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due (i) as a result of the due date not being a business day or (ii) if the holder is late in surrendering (where so required) the relevant Note(s).

(d) **Business day**: In these Conditions "**business day**" means a day on which commercial banks and foreign exchange markets are open in the relevant city and (where such surrender is required by these Conditions) in the place of the specified office of the relevant Paying and Transfer Agent to whom the relevant Note is surrendered.

(e) **Paying and Transfer Agents**: The initial Registrar and Paying and Transfer Agents and their initial specified offices are listed below. The Issuer reserves the right at any time to vary or terminate the appointment of any Paying and Transfer Agent and/or the Registrar and appoint additional or other Paying and Transfer Agents, provided that it will maintain (i) a Registrar and a Fiscal Agent, (ii) Paying and Transfer Agents having specified offices in at least two major European cities and (iii) a Paying and Transfer Agent with a specified office in a European Union member state that will not be obliged to withhold or deduct tax pursuant to any law implementing European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000, to the extent such a Paying and Transfer Agent is not already maintained pursuant to (ii) above.

7. Taxation

All payments of principal and interest by or on behalf of the Issuer in respect of the Notes shall be made free and clear of, and without withholding or deduction for, any taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or within Georgia or any political subdivision thereof or any authority therein or thereof having power to tax, unless such withholding or deduction is required by law. In that event, the Issuer shall pay such additional amounts as will result in receipt by the Noteholders of such amounts as would have been received by them had no such withholding or deduction been required, except that no such additional amounts shall be payable in respect of any Note:

(a) **Other connection:** to a holder, or to a third party on behalf of a holder, who is liable to such taxes, duties, assessments or governmental charges in respect of such Note by reason of his having some connection with Georgia other than the mere holding of the Note; or

(b) **Provision of information:** to or on behalf of a holder who is able to avoid such taxes, duties, assessments or governmental charges in respect of such Note by providing information concerning the nationality, residence or identity of the holder or by making a declaration of non-residence or other claim for exemption to the relevant tax authority; or

(c) **Surrendered for payment more than 30 days after the Relevant Date:** surrendered for payment more than 30 days after the Relevant Date except to the extent that the holder of it would have been entitled to such additional amounts on surrender of such Note for payment on the last day of such period of 30 days; or

(d) **Payment to individuals:** where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or

(e) **Payment by another Paying and Transfer Agent:** by or on behalf of a Noteholder who would have been able to avoid such withholding or deduction by surrendering the relevant Note to another Paying and Transfer Agent in a Member State of the European Union.

In these Conditions "**Relevant Date**" means whichever is the later of (i) the date on which such payment first becomes due and (ii) if the full amount payable has not been received by the Fiscal Agent as provided in the Fiscal Agency Agreement on or prior to such due date, the date on which, the full amount having been so received, notice to that effect shall have been given to the Noteholders. Any reference in these Conditions to principal and/or interest shall be deemed to include any additional amounts which may be payable under this *Condition 7*.

8. **Events of Default**

If any of the following events (each an "**Event of Default**") occurs and is continuing:

(a) **Non-payment**: the Issuer fails to pay any amount of interest or principal on any of the Notes when due and such failure continues for a period of 10 days (in the case of interest) or 7 days (in the case of principal); or

(b) **Breach of other obligations**: the Issuer does not perform or comply in any material respect with any one or more of its other obligations in the Notes which default is incapable of remedy or if capable of remedy, is not remedied within 30 days after notice of such default shall have been given to the Issuer (with a copy to the Fiscal Agent at its specified office) by any Noteholder; or

(c) **Cross-acceleration**: (i) any Indebtedness of the Issuer or any Subsidiary becomes due and payable prior to its stated maturity by reason of any actual or potential default, event of default or the like (howsoever described), or (ii) any Indebtedness of the Issuer or any Subsidiary is not paid when due or, as the case may be, within any originally applicable grace period, or (iii) the Issuer or any Subsidiary fails to pay when due any amount payable by it under any present or future guarantee for, or indemnity in respect of, any Indebtedness of any other person, *provided that* the aggregate amount of any Indebtedness, guarantees and indemnities in respect of which one or more of the events mentioned above in this paragraph (c) have occurred equals or exceeds U.S.$25,000,000 or its equivalent (on the basis of the middle spot rate for the relevant currency against the U.S. dollar as quoted by any leading bank on the day on which this paragraph operates); or

(d) **Enforcement Proceedings:** a distress, attachment, execution or other legal process is levied, enforced or sued out on or against all or any material part of the property, assets or revenues of the Issuer or any Material Subsidiary and is not discharged or stayed within 60 days; or

(e) **Security Enforced:** any mortgage, charge, pledge, lien or other encumbrance, present or future, created or assumed by the Issuer or any Material Subsidiary over all or any material part of the property, assets or revenues of the Issuer or such Material Subsidiary, as the case may be, becomes enforceable and any step is taken to enforce it (including the taking of possession or the appointment of a receiver, manager or other similar person) and is not discharged within 60 days; or

(f) **Insolvency:** the Issuer or any Material Subsidiary is (or is, or could be, deemed by law or a court to be) insolvent or bankrupt or unable to pay its debts, stops, suspends or threatens to stop or suspend payment of all or a material part of its debts, proposes or makes any agreement for the deferral, rescheduling or other readjustment of all or a material part of its debts or proposes or makes a general assignment or an arrangement or composition with or for the benefit of the relevant creditors in respect of all or a material part of its debts; or a moratorium is agreed or declared in respect of or affecting all or a material part of the debts of the Issuer or any Material Subsidiary; or

(g) **Winding-up:** an order is made or an effective resolution passed for the winding-up or dissolution of the Issuer or any Material Subsidiary, or the Issuer ceases or threatens to cease to carry on all or substantially all of its business or operations, except for the purpose of and followed by a reconstruction, amalgamation, reorganisation, merger or consolidation (i) on terms approved by an Extraordinary Resolution of the Noteholders, or (ii) in the case of a Material Subsidiary, whereby the undertaking and assets of the Material Subsidiary are transferred to or otherwise vested in the Issuer or another Subsidiary; or

(h) **Performance prevented:** it is or will become unlawful for the Issuer to perform or comply with any of its material obligations under or in respect of the Notes or the Fiscal Agency Agreement or any of such obligations shall be or become unenforceable or invalid; or

(i) **Consents etc.:** any regulation, decree, consent, approval, licence or other authority necessary to enable the Issuer to perform its material obligations under the Notes or the Fiscal Agency Agreement or for the validity or enforceability thereof expires or is withheld, revoked or terminated or otherwise ceases to remain in full force and effect or is modified in a manner which adversely affects any right or claim of any of the Noteholders in respect of any payment due to them pursuant to these Conditions; or

(j) **Analogous Events:** any event occurs which under the laws of any relevant jurisdiction has an analogous effect to any of the events referred to in any of the foregoing paragraphs of this *Condition 8*,

then the holders of at least 25 per cent. in aggregate principal amount of the outstanding Notes may, by notice in writing to the Issuer at its registered office (with a copy to the Fiscal Agent), declare all the Notes to be, and whereupon they shall become, immediately due and payable at their principal amount together with accrued interest without further action or formality. Notice of any such declaration shall promptly be given to all other Noteholders by the Fiscal Agent (acting on behalf of the Issuer) in accordance with *Condition 13*.

9. Prescription

Claims in respect of principal and interest shall be prescribed and will become void unless made within a period of 10 years in the case of principal and five years in the case of interest from the appropriate Relevant Date.

10. Replacement of Notes

If any Note is lost, stolen, mutilated, defaced or destroyed it may be replaced at the specified office of the Fiscal Agent, subject to all applicable laws and stock exchange or other relevant authority requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may reasonably require. Mutilated or defaced Notes must be surrendered before replacements will be issued.

11. Meetings of Noteholders, Written Resolutions

(a) **Meetings of Noteholders**: The Fiscal Agency Agreement contains provisions for convening meetings of Noteholders to consider matters relating to the Notes, including (subject to *Condition 11(c)* below) the modification of any provision of these Conditions or the provisions of the Fiscal Agency Agreement. Such a meeting may be convened by the Issuer or the Fiscal Agent in its discretion and shall be convened by the Issuer or the Fiscal Agent at any time upon the request in writing of holders of at least 10 per cent. of the aggregate principal amount of the outstanding Notes. For the avoidance of doubt, notwithstanding any provision contained in these Conditions, the Notes or in the Fiscal Agency Agreement, no modification or amendment of these Conditions, the Notes or the Fiscal Agency Agreement may be made without the prior written consent of the Issuer.

(b) **Quorum**: The quorum for any meeting convened to consider an Extraordinary Resolution will be two or more persons holding or representing a clear majority in principal amount of the Notes for the time being outstanding or for any adjourned meeting, two or more persons being or representing Noteholders whatever the principal amount of the Notes held or represented, unless the business of such meeting includes consideration of proposals, inter alia, (i) to modify the maturity of the Notes or the dates on which interest is payable in respect of the Notes, (ii) to reduce or cancel the principal amount of or interest on or to vary the method of calculating the rate of interest on, the Notes, (iii) to change the currency of payment of the Notes, or (iv) to modify the provisions concerning the quorum required at any meeting of Noteholders or the majority required to pass an Extraordinary Resolution, in which case the necessary quorum will be two or more persons holding or representing not less than 75 per cent., or at any adjourned meeting not less than 25 per cent., in principal amount of the Notes for the time being outstanding. Any Extraordinary Resolution duly passed shall be binding on Noteholders (whether or not they were present at the meeting at which such resolution was passed).

(c) **Written Resolutions:** The Fiscal Agency Agreement provides that a resolution in writing signed by or on behalf of the holders of not less than 75 per cent. in principal amount of the Notes outstanding shall for all purposes be as valid and effective as an Extraordinary Resolution passed at a meeting of Noteholders duly convened and held. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders. Notwithstanding any provision contained in these Conditions or in the Fiscal Agency Agreement, no modification or amendment of these Conditions or the Fiscal Agency Agreement may be made without the prior written consent of the Issuer.

(d) **Modification of these Conditions and the Fiscal Agency Agreement:** The Notes, these Conditions and the provisions of the Fiscal Agency Agreement may be amended without the consent of the Noteholders to correct a manifest error or to make any other modification of a minor or technical nature; provided that, for the avoidance of doubt, no modification or amendment of the Notes, these Conditions and the provisions of the Fiscal Agency Agreement may be made without the prior written consent of the Issuer and the Issuer shall only permit any modification of, or any waiver or authorisation of any breach or proposed breach of or any failure to comply with, these Conditions, the Notes or the Fiscal Agency Agreement, if to do so could not reasonably be expected to be materially prejudicial to the interests of the Noteholders.

12. **Further Issues**

The Issuer may from time to time without the consent of the Noteholders create and issue further securities either having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding securities of any series (including the Notes) or upon such terms as the Issuer may determine at the time of their issue. References in these Conditions to the Notes include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the Notes.

*Any such further securities, even if they are treated for non-tax purposes as part of the same series as the Notes, in some cases may be treated as a separate series for U.S. federal income tax purposes. In such a case, the further securities may be considered to have been issued with original issue discount ("**OID**") even if the Notes had no OID. These differences may affect the market value of the Notes if the further securities are not otherwise distinguishable from the Notes.*

13. **Notices**

All notices to Noteholders shall be mailed to them at their respective addresses appearing in the Register and shall be deemed to have been given on the fourth weekday (excluding Saturday and Sunday) after the date of mailing.

14. **Currency Indemnity**

United States dollars (the "**Contractual Currency**") is the sole currency of account and payment for all sums payable by the Issuer under or in connection with the Notes, including damages. Any amount received or recovered in a currency other than the Contractual Currency (whether as a result of, or of the enforcement of, a judgment or order of a court of any jurisdiction or otherwise) by any Noteholder in respect of any sum expressed to be due to it from the Issuer shall only constitute a discharge to the Issuer to the extent of the Contractual Currency amount which the recipient is able to purchase with the amount so received or recovered in that other currency on the date of that receipt or recovery (or, if it is not practicable to make that purchase on that date, on the first date on which it is practicable to do so). If that Contractual Currency amount is less than the Contractual Currency amount expressed to be due to the recipient under any Note, the Issuer shall indemnify such recipient against any loss sustained by it as a result. In any event, the Issuer shall indemnify the recipient against the cost of making any such purchase. For the purposes of this Condition, it will be sufficient for the Noteholder to demonstrate that it would have suffered a loss had an actual purchase been made. These indemnities constitute a separate and independent obligation from the Issuer's other obligations, shall give rise to a separate and independent cause of action, shall apply irrespective of any indulgence granted by any Noteholder and shall continue in full force and effect despite any other judgment, order, claim or proof for a liquidated amount in respect of any sum due under any Note or any other judgment or order, until paid in full.

15. **Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the Notes under the Contracts (Rights of Third Parties) Act 1999.

16. **Governing Law**

(a) **Governing law**: The Fiscal Agency Agreement and the Notes are governed by, and shall be construed in accordance with, English law.

(b) **Jurisdiction**: The Issuer irrevocably agrees for the benefit of the Noteholders that the courts of England are to have jurisdiction to settle any disputes which may arise out of or in connection with the

Fiscal Agency Agreement or the Notes and that accordingly any suit, action or proceedings arising out of or in connection therewith (together referred to as "**Proceedings**") may be brought in the courts of England.

(c) **No objection to Proceedings**: The Issuer irrevocably and unconditionally waives and agrees not to raise any objection which it may have now or subsequently to the laying of the venue of any Proceedings in the courts of England and any claim that any Proceedings have been brought in an inconvenient forum and further irrevocably and unconditionally agrees that a final non-appealable judgment in any Proceedings brought in the courts of England shall be conclusive and binding upon the Issuer and may, subject to the proviso in paragraph (f) below, be enforced in the courts of any other jurisdiction to which the Issuer is or may be subject. Nothing in this Condition shall limit any right to take Proceedings against the Issuer in any other court of competent jurisdiction, nor shall the taking of Proceedings in one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction, whether concurrently or not.

(d) **Agent for service of process**: The Issuer irrevocably appoints Law Debenture Corporate Services Limited of Fifth Floor, 100 Wood Street, London EC2V 7EX as its agent in England to receive service of process in any Proceedings in England. If for any reason such agent shall cease to be such agent for service of process, the Issuer shall appoint a new agent for service of process in England and deliver to the Fiscal Agent a copy of the new agent's acceptance of that appointment within 30 days.

(e) **Arbitration**: The Issuer irrevocably and unconditionally agrees that any disputes which may arise out of or in connection with the Notes (including any questions regarding their existence, validity or termination) may be referred to and finally resolved by arbitration under the Rules of the LCIA (formerly the London Court of International Arbitration). The place of such arbitration shall be London and the language English.

(f) **Waiver of immunity**: To the extent that the Issuer or any of its assets has (on the date of issue of the Notes), or thereafter may acquire, any right to immunity from set-off, legal proceedings, attachment prior to judgement, other attachment or execution of judgement on the grounds of sovereignty or otherwise, the Issuer, if and to the extent permitted by applicable laws, hereby irrevocably waives any such right to immunity and any similar defence, and irrevocably consents to the giving of any relief or the issue of any process, including, without limitation, the making, enforcement or execution against any property whatsoever of any order, award or judgment made or given in connection with any Proceedings.

PROVISIONS RELATING TO THE NOTES WHILST IN GLOBAL FORM

The Global Notes

The Notes will be evidenced on issue, in the case of Unrestricted Notes, by the Unrestricted Global Note (which will be deposited with, and registered in the name of a nominee for, a common depositary for Euroclear and Clearstream, Luxembourg) and, in the case of Restricted Notes, by the Restricted Global Note (which will be deposited with a custodian for, and registered in the name of Cede & Co. as nominee of, DTC).

Beneficial interests in the Unrestricted Global Note may be held only through Euroclear or Clearstream, Luxembourg at any time. See "*Clearing and Settlement—Book-Entry Ownership*". By acquisition of a beneficial interest in an Unrestricted Global Note, the purchaser thereof will be deemed to represent, among other things, that it is not located in the United States.

Beneficial interests in the Restricted Global Note may only be held through DTC at any time. See "*Clearing and Settlement—Book-Entry Ownership*". By acquisition of a beneficial interest in the Restricted Global Note, the purchaser thereof will be deemed to represent, among other things, that it is a QIB and that, if in the future it decides to transfer such beneficial interest, it will transfer such interest in accordance with the procedures and restrictions contained in the Fiscal Agency Agreement. See "*Transfer Restrictions*".

Beneficial interests in each Global Note will be subject to certain restrictions on transfer set forth therein and in the Fiscal Agency Agreement, and with respect to Restricted Notes, as set forth in Rule 144A, and the Restricted Global Note will bear the legend set forth thereon regarding such restrictions set forth under "*Transfer Restrictions*". A beneficial interest in the Unrestricted Global Note may be transferred to a person who takes delivery in the form of an interest in the Restricted Global Note in denominations greater than or equal to the minimum denominations applicable to interests in the Restricted Global Note and only upon receipt by the Registrar of a written certification (in the form provided in the Fiscal Agency Agreement) to the effect that the transferor reasonably believes that the transferee is a QIB and that such transaction is in accordance with any applicable securities laws of any state of the United States or any other jurisdiction. Beneficial interests in the Restricted Global Note may be transferred to a person who takes delivery in the form of an interest in the Unrestricted Global Note and in accordance with Regulation S.

A beneficial interest in the Unrestricted Global Note that is transferred to a person who takes delivery in the form of an interest in the Restricted Global Note will, upon transfer, cease to be an interest in the Unrestricted Global Note and become an interest in the Restricted Global Note, and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in the Restricted Global Note for as long as it remains such an interest. A beneficial interest in the Restricted Global Note that is transferred to a person who takes delivery in the form of an interest in the Unrestricted Global Note will, upon transfer, cease to be an interest in the Restricted Global Note and become an interest in the Unrestricted Global Note and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in the Unrestricted Global Note for so long as it remains such an interest. No service charge will be made for any registration of transfer or exchange of Notes, but the Registrar may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith. Except in the limited circumstances described below, owners of beneficial interests in Global Notes will not be entitled to receive physical delivery of the definitive registered certificates ("**Note Certificates**"). No Notes will be issued in bearer form.

Legends

The holder of a Note Certificate may transfer the Notes evidenced thereby in whole or in part in the applicable minimum denomination by surrendering it at the specified office of the Registrar or any Paying and Transfer Agent, together with the completed form of transfer thereon. Upon the transfer, exchange or replacement of a Restricted Note Certificate bearing the legend referred to under "*Transfer Restrictions*", or upon specific request for removal of the legend on a Restricted Note Certificate, the Company will deliver only Restricted Note Certificates that bear such legend, or will refuse to remove such legend, as the case may be, unless there is delivered to the Company and the Registrar such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by the Company that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

Amendments to Terms and Conditions of the Notes

The Global Notes contain provisions that apply to the Notes that it evidences, some of which modify the effect of the Terms and Conditions of the Notes. The following is a summary of those provisions.

Payments

Payments of principal and interest in respect of Notes evidenced by a Global Note will be made to the person who appears in the Register at the close of business on the Clearing System Business Day immediately prior to the date for payment as holder of the Notes against presentation for endorsement by the Fiscal Agent and, if no further payment falls to be made in respect of the relevant Notes, surrender of such Global Note to or to the order of the Fiscal Agent or such other Paying and Transfer Agent as shall have been notified to the relevant Noteholders for such purpose. A record of each payment so made will be endorsed in the appropriate schedule to a Global Note, which endorsement will be *prima facie* evidence that such payment has been made in respect of the relevant Notes. "**Clearing System Business Day**" for the purposes of this paragraph means Monday to Friday, inclusive, except 25 December and 1 January.

Notices

So long as any Notes are evidenced by a Global Note and such Global Note is held by or on behalf of a clearing system, notices to Noteholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled account holders in substitution for delivery thereof as required by the Terms and Conditions of the Notes (and such notices will be deemed to have been given on the day following the date of delivery to the relevant clearing system or, if that is not a Clearing System Business Day, on the next succeeding Clearing System Business Day).

Meetings

The holder of a Global Note will be treated as being two persons for the purposes of any quorum requirements of, or the right to demand a poll at, a meeting of Noteholders and in any such meeting as having one vote in respect of each integral U.S.$1,000 in principal amount of Notes.

Cancellation

Cancellation of any Note required by the Terms and Conditions of the Notes to be cancelled will be effected by reduction in the principal amount of the relevant Global Note.

Prescription

Claims against the Company in respect of principal and interest on the Notes whilst the relevant Notes are represented by a Global Note will become void unless it is presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) from the appropriate Relevant Date (as defined in Condition 7 (*Taxation*) of the Notes).

Default

Each Global Note provides that the holder may cause the Global Note or a portion of it to become due and payable in the circumstances described in Condition 8 (*Events of Default*) of the Notes by stating in the notice to the Fiscal Agent the principal amount of Notes which is being declared due and payable. If principal in respect of any Note is not paid when due and payable, the holder of the Global Note may elect that the Global Note becomes void as to a specified portion and that the persons entitled to such portion, as accountholders with a clearing system, acquire direct enforcement rights against the Company under further provisions of the Global Note executed by the Company as a deed poll.

Put Option

The Noteholders' put option in Condition 5(b) (*Redemption at the Option of Noteholders (Put Option)*) of the Notes may be exercised by the holder of the relevant Global Note, giving notice to the Fiscal Agent of the principal amount of Notes in respect of which the option is exercised and presenting the relevant Global Note for endorsement of exercise within the time limits and in the circumstances specified in Condition 5(b) (*Redemption at the Option of Noteholders (Put Option)*).

Exchange for Note Certificates

Exchange

The Unrestricted Global Note will be exchangeable, free of charge to the holder, in whole but not in part, for Note Certificates if: (i) it is held by or on behalf of a clearing system and such clearing system is closed for business for a continuous period of 14 calendar days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so, by the holder giving notice to the Registrar or (ii) if the Company would suffer a material disadvantage in respect of the Notes as a result of a change in the laws or regulations (taxation or otherwise) of any jurisdiction referred to in Condition 7 (*Taxation*) of the Notes which would not be suffered were the Notes in definitive form, by the Company giving notice to the Registrar and the Noteholders, in each case of its intention to exchange interests in the Unrestricted Global Note for Note Certificates on or after the Exchange Date (as defined below) specified in the notice.

The Restricted Global Note will be exchangeable, free of charge to the holder, in whole but not in part, for Note Certificates if (i) DTC or its successor depositary notifies the Company that it is no longer willing or able to discharge properly its responsibilities as depositary with respect to the Restricted Global Note or ceases to be a "clearing agency" registered under the Exchange Act, or is at any time unable to act as such, and the Company is unable to locate a qualified successor within 90 days of receiving notice of such ineligibility on the part of such depositary or (ii) the Company would suffer a material disadvantage in respect of the Notes as a result of a change in the laws or regulations (taxation or otherwise) of any jurisdiction referred to in Condition 7 (*Taxation*) of the Notes which would not be suffered were the Notes in definitive form, by the Company giving notice to the Registrar and the Noteholders, in each case, of its intention to exchange interests in the Restricted Global Note for Note Certificates on or after the Exchange Date (as defined below) specified in the notice.

"**Exchange Date**" means a day falling not later than 60 calendar days after that on which the notice requiring exchange is given and on which banks are open for business in the city in which the specified office of the Registrar or the relevant Paying and Transfer Agent is located.

The Registrar will not register the transfer of, or exchange of interests in, a Global Note for Note Certificates for a period of 15 calendar days ending on the date for any payment of principal or interest in respect of the Notes.

Delivery

If any of the events described in "*—Exchange*" above occurs, the relevant Global Note shall be exchangeable in full but not in part for Note Certificates and the Company will, free of charge to the Noteholders (but against such indemnity as the Registrar or any relevant Paying and Transfer Agent may require in respect of any tax or other duty of whatever nature which may be levied or imposed in connection with such exchange), cause sufficient Note Certificates to be executed and delivered to the Registrar for completion and despatch to the relevant Noteholders. A person having an interest in the relevant Global Note must provide the Registrar with (a) a written order containing instructions and such other information as the Company and the Registrar may require to complete, execute and deliver such Note Certificates and (b) in the case of the Restricted Global Note only, a fully completed, signed certification substantially to the effect that the exchanging holder is not transferring its interest at the time of such exchange or, in the case of simultaneous sale pursuant to Rule 144A, a certification that the transfer is being made in compliance with the provisions of Rule 144A to a QIB. Except as otherwise permitted, Note Certificates issued in exchange for an interest in the Restricted Global Note shall bear the legend applicable to transfers pursuant to Rule 144A, as set out under "*Transfer Restrictions*".

CLEARING AND SETTLEMENT

*The information set out below is subject to any change in or reinterpretation of the rules, regulations and procedures of DTC, Euroclear or Clearstream, Luxembourg (together, the "**Clearing Systems**") currently in effect. Investors wishing to use the facilities of any of the Clearing Systems are advised to confirm the continued applicability of the rules, regulations and procedures of the relevant Clearing System. None of the Company nor any other party to the Fiscal Agency Agreement will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Notes held through the facilities of any Clearing System or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.*

The Clearing Systems

Custodial and depositary links are to be established between DTC, Euroclear and Clearstream, Luxembourg to facilitate the initial issue of the Notes and cross-market transfers of the Notes associated with secondary market trading. See "—*Book-Entry Ownership*" and "*—Settlement and Transfer of Notes*" below.

Investors may hold their interests in a Global Note directly through DTC, Euroclear or Clearstream, Luxembourg if they are accountholders ("**Direct Participants**") or indirectly ("**Indirect Participants**" and, together with Direct Participants, "**Participants**") through organisations which are accountholders therein.

Euroclear and Clearstream, Luxembourg

Euroclear and Clearstream, Luxembourg each hold securities for their customers and facilitate the clearance and settlement of securities transactions through electronic book-entry transfer between their respective accountholders. Indirect access to Euroclear and Clearstream, Luxembourg is available to other institutions which clear through or maintain a custodial relationship with an accountholder of either system. Euroclear and Clearstream, Luxembourg provide various services including safekeeping, administration, clearance and settlement of internationally-traded securities and securities lending and borrowing. Euroclear and Clearstream, Luxembourg also deal with domestic securities markets in several countries through established depositary and custodial relationships. Euroclear and Clearstream, Luxembourg have established an electronic bridge between their two systems across which their respective customers may settle trades with each other.

The Depository Trust Company

DTC has advised the Company as follows: DTC is a limited purpose trust company organised under the laws of the State of New York, a "banking organisation" under the laws of the State of New York, a member of the United States Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial code and a "clearing agency" registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities for its Participants and facilitate the clearance and settlement of securities transactions between Participants through electronic computerised book-entry changes in accounts of its Participants, thereby eliminating the need for physical movement of certificates. Participants include securities brokers and dealers, banks, trust companies, clearing corporations and certain other organisations. Indirect access to DTC is available to others, such as banks, securities brokers, dealers and trust companies that clear through or maintain a custodial relationship with a DTC Direct Participant, either directly or indirectly.

Investors may hold their interests in the Restricted Global Note directly through DTC if they are Direct Participants in the DTC system, or as Indirect Participants through organisations which are Direct Participants in such system.

Under the rules, regulations and procedures creating and affecting DTC and its operations (the "**Rules**"), DTC makes book-entry transfers of Restricted Notes represented by the Restricted Global Note among Direct Participants on whose behalf it acts with respect to Restricted Notes and receives and transmits distributions of principal and interest on Restricted Notes. The Rules are on file with the Securities and Exchange Commission. Direct Participants and Independent Participants with which beneficial owners of Restricted Notes have accounts with respect to the Restricted Notes similarly are required to make book-entry transfers and receive and transmit such payments on behalf of their beneficial owners. Accordingly, although beneficial owners who hold Restricted Notes through Direct Participants or Indirect Participants will not possess Restricted Notes, the Rules, by virtue of the requirements described above, provide a mechanism by which Participants will receive payments and will be able to transfer their interest in respect of the Restricted Notes.

DTC has advised the Company that it will take any action permitted to be taken by a holder of Notes only at the direction of one or more Direct Participants and only in respect of such portion of the aggregate principal amount of the Restricted Global Note as to which such Participant or Participants has or have given such direction. However, in the circumstances described under "*Provisions Relating to the Notes whilst in Global Form—Exchange for Note Certificates*", DTC will cause its custodian to surrender the Restricted Global Note for exchange for Note Certificates (which will bear the legend applicable to transfers pursuant to Rule 144A).

Payments through DTC

Payments of principal and interest in respect of a Global Note registered in the name of, or in the name of a nominee for, DTC will be made to the order of such nominee as the registered holder of such Note.

Book-Entry Ownership

Euroclear and Clearstream, Luxembourg

The Unrestricted Global Note evidencing Unrestricted Notes will have an ISIN and a Common Code and will be registered in the name of a nominee for, and deposited with a common depositary on behalf of, Euroclear and Clearstream, Luxembourg.

DTC

The Restricted Global Note evidencing the Restricted Notes will have an ISIN, Common Code and a CUSIP number and will be deposited with the Custodian for, and registered in the name of Cede & Co. as nominee of, DTC. The Custodian and DTC will electronically record the principal amount of the Notes held within the DTC System.

Relationship of Participants with Clearing Systems

Each of the persons shown in the records of DTC, Euroclear or Clearstream, Luxembourg as the holder of a Note evidenced by a Global Note must look solely to DTC, Euroclear or Clearstream, Luxembourg (as the case may be) for its share of each payment made by the Company to the holder of such Global Note and in relation to all other rights arising under such Global Note, subject to and in accordance with the respective rules and procedures of DTC, Euroclear or Clearstream, Luxembourg (as the case may be). The Company expects that, upon receipt of any payment in respect of Notes evidenced by a Global Note, the common depositary by whom such Note is held, or nominee in whose name it is registered, will immediately credit the relevant Participants' or accountholders' accounts in the relevant Clearing System with payments in amounts proportionate to their respective beneficial interests in the principal amount of the relevant Global Note as shown on the records of the relevant Clearing System or its nominee. The Company also expects that payments by Direct Participants in any Clearing System to owners of beneficial interests in any Global Note held through such Direct Participants in any Clearing System will be governed by standing instructions and customary practices. Save as aforesaid, such persons shall have no claim directly against the Company in respect of payments due on the Notes for so long as the Notes are evidenced by such Global Note and the obligations of the Company will be discharged by payment to the registered holder of such Global Note in respect of each amount so paid. None of the Company, the Fiscal Agent or any other Paying and Transfer Agent will have any responsibility or liability for any aspect of the records relating to or payments made on account of ownership interests in any Global Note or for maintaining, supervising or reviewing any records relating to such ownership interests.

Settlement and Transfer of Notes

Subject to the rules and procedures of each applicable Clearing System, purchases of Notes held within a Clearing System must be made by or through Direct Participants, which will receive a credit for such Notes on the Clearing System's records. The ownership interest of each actual purchaser of each such Note (the "**Beneficial Owner**") will in turn be recorded on the Direct and Indirect Participants' records.

Beneficial Owners will not receive written confirmation from any Clearing System of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which such Beneficial Owner entered into the transaction.

Transfers of ownership interests in Notes held within the Clearing System will be effected by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates evidencing their ownership interests in such Notes, unless and until interests in any Global Note held within a Clearing System are exchanged for Note Certificates.

No Clearing System has knowledge of the actual Beneficial Owners of the Notes held within such Clearing System and their records will reflect only the identity of the Direct Participants to whose accounts such Notes are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers. Conveyance of notices and other communications by the Clearing Systems to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

The laws of some jurisdictions may require that certain persons take physical delivery in definitive form of securities. Consequently, the ability to transfer interests in a Global Note to such persons may be limited. As DTC can only act on behalf of Direct Participants, who in turn act on behalf of Indirect Participants, the ability of a person having an interest in a Restricted Global Note to pledge such interest to persons or entities that do not participate in DTC, or otherwise take actions in respect of such interest, may be affected by a lack of a physical certificate in respect of such interest.

Trading between Euroclear and Clearstream, Luxembourg Participants

Secondary market sales of book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg to purchasers of book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be conducted in accordance with the normal rules and operating procedures of Euroclear and Clearstream, Luxembourg and will be settled using the procedures applicable to conventional eurobonds.

Trading between DTC Participants

Secondary market sales of book-entry interests in the Notes between DTC Participants will occur in the ordinary way in accordance with DTC rules and will be settled using the procedures applicable to United States corporate debt obligations in DTC's Same-Day Funds Settlement system in same-day funds, if payment is effected in U.S. Dollars, or free of payment, if payment is not effected in U.S. Dollars. Where payment is not effected in U.S. Dollars, separate payment arrangements outside DTC are required to be made between the DTC participants.

Trading between DTC Seller and Euroclear/Clearstream, Luxembourg Purchaser

When book-entry interests in Notes are to be transferred from the account of a DTC Participant holding a beneficial interest in the Restricted Global Note to the account of a Euroclear or Clearstream, Luxembourg accountholder wishing to purchase a beneficial interest in the Unrestricted Global Note (subject to the certification procedures provided in the Fiscal Agency Agreement), the DTC participant will deliver instructions for delivery to the relevant Euroclear or Clearstream, Luxembourg accountholder to DTC by 12 noon, New York time, on the settlement date. Separate payment arrangements are required to be made between the DTC Participant and the relevant Euroclear or Clearstream, Luxembourg Participant. On the settlement date, the custodian of the Restricted Global Note will instruct the Registrar to (i) decrease the amount of Notes registered in the name of Cede & Co. and evidenced by the Restricted Global Note and (ii) increase the amount of Notes registered in the name of the nominee of the common depositary for Euroclear and Clearstream, Luxembourg and evidenced by the Unrestricted Global Note. Book-entry interests will be delivered free of payment to Euroclear or Clearstream, Luxembourg, as the case may be, for credit to the relevant accountholder on the first business day following the settlement date.

Trading between Euroclear/Clearstream, Luxembourg seller and DTC Purchaser

When book-entry interests in the Notes are to be transferred from the account of a Euroclear or Clearstream, Luxembourg accountholder to the account of a DTC Participant wishing to purchase a beneficial interest in the Restricted Global Note (subject to the certification procedures provided in the Fiscal Agency Agreement), the Euroclear or Clearstream, Luxembourg Participant must send to Euroclear or Clearstream, Luxembourg delivery free of payment instructions by 7:45 p.m., Brussels or Luxembourg time, one business day prior to the settlement date. Euroclear or Clearstream, Luxembourg, as the case may be, will in turn transmit appropriate instructions to the common depositary for Euroclear and Clearstream, Luxembourg and the Registrar to arrange delivery to the DTC Participant on the settlement date, Separate payment arrangements are required to be made between the DTC Participant and the relevant Euroclear or Clearstream, Luxembourg accountholder, as the case may be. On the settlement date, the common depositary for Euroclear and Clearstream, Luxembourg will (a) transmit appropriate instructions to the custodian of the Restricted Global Note who will in turn deliver such book-entry interests in the Notes free of payment to the relevant account of the DTC Participant and (b) instruct the Registrar to (i) decrease the amount of Notes registered in the name of the nominee of the common depositary for Euroclear and Clearstream, Luxembourg and evidenced by the Unrestricted Global Note; and (ii) increase the amount of Notes registered in the name of Cede & Co. and evidenced by the Restricted Global Note, Although DTC, Euroclear and Clearstream, Luxembourg have agreed to the foregoing procedures in order to facilitate transfers of beneficial interests in Global Notes among Participants and accountholders of DTC, Euroclear and Clearstream, Luxembourg, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. None of the Company, the Fiscal Agent or any other Paying and Transfer Agent will have any responsibility for the performance by DTC, Euroclear, Clearstream, Luxembourg or their respective Direct or Indirect Participants of their respective obligations under the rules and procedures governing their operations.

Settlement of Pre-issue Trades

It is expected that delivery of Notes will be made against payment therefor on the Issue Date, which could be more than three business days following the date of pricing. Under Rule 15c6-l under the Exchange Act, trades in the United States secondary market generally are required to settle within three business days (T+3), unless the parties to any such trade expressly agree otherwise.

Accordingly, purchasers who wish to trade Notes in the United States on the date of pricing or the next succeeding business days until three days prior to the Issue Date will be required, by virtue of the fact the Notes initially will settle beyond T+3, to specify an alternate settlement cycle at the time of any such trade to prevent a failed settlement. Settlement procedures in other countries will vary.

Purchasers of Notes may be affected by such local settlement practices and purchasers of Notes between the relevant date of pricing and the Issue Date should consult their own advisers.

SUBSCRIPTION AND SALE

Each of Goldman Sachs International, J.P. Morgan Securities Ltd. and Merrill Lynch International (each, a "**Joint Lead Manager**" and together, the "**Joint Lead Managers**") has, in a subscription agreement dated 27 June 2012 (the "**Subscription Agreement**") and upon the terms and subject to the conditions contained therein, severally agreed to subscribe and pay for the aggregate principal amount of the Notes listed next to its name in the table below at the issue price of 99.998 per cent. of their principal amount.

Joint Lead Manager	**Principal Amount of the Notes**
Goldman Sachs International	U.S.$166,666,667
J.P. Morgan Securities Ltd.	U.S.$166,666,667
Merrill Lynch International	U.S.$166,666,666
Total	**U.S.$500,000,000**

The Company has agreed to pay to the Joint Lead Managers a fee in respect of their agreement to subscribe and pay for the Notes. The Joint Lead Managers are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Notes. The Company has in the Subscription Agreement agreed to indemnify the Joint Lead Managers against certain liabilities incurred in connection with the Notes.

Each of the Joint Lead Managers and its respective affiliates have performed and expect to perform in the future various financial advisory, investment banking and commercial banking services for, and may arrange loans and other non-public market financing for, and enter into derivative transactions with, the Company and its affiliates (including its shareholders) for which they will receive customary fees. If the Joint Lead Managers or their respective affiliates have a lending relationship with the Company, they will routinely hedge their credit exposure consistent with customary risk management policies. Typically, the Joint Lead Managers and their respective affiliates would hedge such exposure by entering into transactions, which consist of either the purchase of credit default swaps or the creation of short positions in the Company's securities, including potentially the Notes. Any such short positions could adversely affect future trading prices of the Notes. The Joint Lead Managers and their respective affiliates may also make investment recommendations or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

In connection with the issue of the Notes, the Stabilising Manager (or any person acting for the Stabilising Manager) may over-allot notes or effect transactions with a view to supporting the market price of the Notes at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the initial allotment of the Notes. Any stabilisation action or over-allotment must be conducted by the Stabilising Manager (or any person acting on behalf of the Stabilising Manager) in accordance with all applicable laws and rules.

United States

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act.

Each Joint Lead Manager has represented that it has not offered or sold, and agreed that it will not offer or sell, any Notes constituting part of its allotment within the United States except in accordance with Rule 903 of Regulation S or Rule 144A under the Securities Act. Each Joint Lead Manager has represented that neither it nor its affiliates (as defined in Rule 405 under the Securities Act), nor any persons acting on its or their behalf, have engaged or will engage in any directed selling efforts with respect to the Notes. Terms used in this paragraph have the meaning given to them by Regulation S under the Securities Act.

Each Joint Lead Manager has represented and agreed that neither it nor any of its affiliates (as defined in Rule 501(b) of Regulation D under the Securities Act ("**Regulation D**")), nor any person acting on its or their behalf, has engaged or will engage in any form of general solicitation or general advertising (within the meaning of Regulation D) in connection with any offer and sale of the Notes in the United States.

The Notes are being offered and sold by the Joint Lead Managers outside the United States in accordance with Regulation S. The Subscription Agreement provides that the Joint Lead Managers may through their respective United

States broker-dealer affiliates resell a portion of the Notes within the United States only to QIBs in reliance on Rule 144A.

In addition, until 40 days after the commencement of the offering of the Notes, an offer or sale of Notes within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A, or another available exemption from registration under the Securities Act.

United Kingdom

Each Joint Lead Manager has represented and agreed that:

i. it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the Financial Services and Markets Act 2000 (the "**FSMA**") received by it in connection with the issue or sale of the Notes in circumstances in which Section 21(1) of the FSMA does not apply to the Company; and

ii. it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

Georgia

Each Joint Lead Manager has represented and agreed that it has complied and will comply with all applicable provisions of Georgian law with respect to anything done by it in relation to the Notes in, from or otherwise involving Georgia.

General

No action has been, or will be, taken by the Company or the Joint Lead Managers that would, or is intended to, permit a public offer of Notes, or possession or distribution of this Prospectus, in any country or jurisdiction where any such action for that purpose is required. Accordingly, each Joint Lead Manager has undertaken that it will comply, to the best of its knowledge and belief and in all material respects, with all applicable securities laws and regulations in each jurisdiction in which it purchases, offers, sells or delivers Notes or has in its possession or distributes this Prospectus.

TRANSFER RESTRICTIONS

Restricted Notes

Each purchaser of Restricted Notes, by accepting delivery of this Prospectus and the Notes, will be deemed to have represented, agreed and acknowledged that:

1. It is (a) a QIB, (b) acting for its own account, or for the account of a QIB, (c) not formed for the purpose of investing in the Company, and (d) aware, and each beneficial owner of such Notes has been advised, that the sale of such Notes to it is being made in reliance on Rule 144A.

2. It understands that the Restricted Notes are being offered only in a transaction not involving any public offering in the United States within the meaning of the Securities Act, and that the Restricted Notes have not been and will not be registered under the Securities Act and may not be offered, sold, pledged or otherwise transferred except (a) in accordance with Rule 144A to a person that it and any person acting on its behalf reasonably believe is a QIB purchasing for its own account or for the account of a QIB or (b) in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act, in each case, in accordance with any applicable securities laws of any state or another jurisdiction of the United States.

3. It acknowledges that the Notes offered and sold hereby in the manner set forth in paragraph 1 are "restricted securities" within the meaning of Rule 144(a)(3) under the Securities Act and are being offered and sold in a transaction not involving any public offering in the United States within the meaning of the Securities Act and that no representation is made as to the availability of the exemption provided by Rule 144 for resales of the Notes.

4. If it is acquiring any Notes for the account of one or more QIBs, it represents that it has sole investment discretion with respect to each such account and that it has full power to make (and does make) the foregoing acknowledgments, representations and agreements on behalf of each such account.

5. It understands that the Company has the right to refuse to honour the transfer of an interest in the Restricted Notes to a United States person whom it reasonably believes is not a QIB.

6. It understands that the Restricted Notes, unless otherwise agreed between the Company and the Fiscal Agent in accordance with applicable law, will bear a legend to substantially the following effect:

   THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933 (THE "**SECURITIES ACT**"), OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES AND MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED EXCEPT (1) IN ACCORDANCE WITH RULE 144A UNDER THE SECURITIES ACT ("**RULE 144A**") TO A PERSON THAT THE HOLDER AND ANY PERSON ACTING ON ITS BEHALF REASONABLY BELIEVE IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A (A "**QIB**") AND THAT IS ACQUIRING THIS NOTE FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF ONE OR MORE QIBS, (2) IN AN OFFSHORE TRANSACTION IN ACCORDANCE WITH RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT OR (3) PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT PROVIDED BY RULE 144 THEREUNDER, IF AVAILABLE, IN EACH CASE, IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES AND THE HOLDER WILL, AND EACH SUBSEQUENT HOLDER IS REQUIRED TO, NOTIFY ANY PURCHASER OF THE RESALE RESTRICTIONS REFERRED TO ABOVE. NO REPRESENTATION CAN BE MADE AS TO THE AVAILABILITY OF ANY EXEMPTION UNDER THE SECURITIES ACT FOR RESALES OF THE NOTES.

7. It acknowledges that the Company, the Registrar, the Joint Lead Managers and their affiliates, and others, will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements and agrees that, if any of the acknowledgements, representations or agreements deemed to have been made by it by its purchase of Restricted Notes is no longer accurate, it shall promptly notify the Company and the Joint Lead Managers. If it is acquiring any Notes as a fiduciary or agent for one or more investor accounts, it represents that it has sole investment discretion with respect to each of those accounts and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each account.

8. It understands that the Restricted Notes will be evidenced by the Restricted Global Note. Before any interest in a Restricted Global Note may be offered, sold, pledged or otherwise transferred to a person who takes delivery in the form of an interest in an Unrestricted Global Note, it will be required to provide a Paying and Transfer Agent with a written certification (in the form provided in the Fiscal Agency Agreement) as to compliance with applicable securities laws.

9. Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A.

Unrestricted Notes

Each purchaser of Unrestricted Notes, by accepting delivery of this Prospectus and the Notes, will have been deemed to have represented, agreed and acknowledged that:

1. It is, or at the time the Unrestricted Notes are purchased will be, the beneficial owner of such Unrestricted Notes and (a) that it is located outside the United States (within the meaning of Regulation S) and (b) it is not an affiliate of the Company or a person acting on behalf of such an affiliate.

2. It understands that the Unrestricted Notes have not been and will not be registered under the Securities Act and may not be offered, sold, pledged or otherwise transferred except (a) in accordance with Rule 144A to a person that it and any person acting on its behalf reasonably believe is a QIB purchasing for its own account or for the account of one or more QIBs or (b) to a non-United States person in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S, in each case, in accordance with any applicable securities laws of any state of the United States.

3. It understands that the Unrestricted Notes will be evidenced by an Unrestricted Global Note. Before any interest in an Unrestricted Global Note may be offered, sold, pledged or otherwise transferred to a person who takes delivery in the form of an interest in the corresponding Restricted Global Note, it will be required to provide a Paying and Transfer Agent with a written certification (in the form provided in the Fiscal Agency Agreement) as to compliance with applicable securities laws.

4. It acknowledges that the Company, the Registrar, the Joint Lead Managers and their affiliates, and others, will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements and agrees that, if any of the acknowledgements, representations or agreements deemed to have been made by it by its purchase of the Unrestricted Notes is no longer accurate, it shall promptly notify the Company and the Joint Lead Managers. If it is acquiring any Notes as a fiduciary or agent for one or more investor accounts, it represents that it has sole investment discretion with respect to each of those accounts and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each account.

TAXATION

The following discussion summarises certain Georgian tax considerations that may be relevant to holders of Notes. It also includes a limited discussion of certain European Union considerations and certain material United States federal income tax considerations. This summary is based on the Company's understanding of laws, regulations, rulings and decisions now in effect and is subject to changes in, and differing interpretations of, tax law and practice, including changes, interpretations and applications that could have a retroactive effect. Certain statements made below as to the possible tax treatment of holders of Notes should be read in this context.

This summary does not describe all of the tax considerations that may be relevant to holders of Notes, particularly holders of Notes subject to special tax rules. Holders of Notes are advised to consult their own professional advisers as to the consequences of purchasing Notes under the tax laws of the country of which they are resident.

Georgian Tax

The analysis below is a general overview of certain tax implications related to the Notes prepared in accordance with Georgian tax legislation. As with other areas of Georgian legislation, tax law and practice in Georgia is not as clearly established as that of more developed jurisdictions. It is possible, therefore, that changes may be made in the law or in the current interpretation of the law or current practice, including changes that could have a retroactive effect. Accordingly, it is possible that payments to be made to the holders of the Notes could become subject to taxation, or that rates currently in effect with respect to such payments could be increased, in ways that cannot be anticipated as at the date of this Prospectus. Each prospective purchaser of Notes should also consider the further tax implications for it under laws and regulations of those countries which will be applicable to its purchase, holding and sale of Notes. See "*Risk Factors—Risks Related to Georgia—The uncertainties of the Georgian tax system could have a material adverse effect on the Company's business.*"

Withholding Tax on Interest

Pursuant to the Tax Code of Georgia, payments of interest on the Notes will be exempt from withholding tax and such payments of interest shall not be included in the gross taxable income of Noteholders (whether they are individuals (physical persons) or legal entities), so long as the Notes are listed on a "recognised stock exchange". For these purposes, the London Stock Exchange is a "recognised stock exchange". However, it is not clear what kind of evidence the tax authorities might require by way of proof that the Notes are listed on the London Stock Exchange.

Enforceability of the Tax Gross-up under the Terms and Conditions of the Notes

Pursuant to Condition 7 *(Taxation)* of the Notes, in the case of a withholding or deduction of any taxes (subject to certain customary exceptions) in respect of any payment on the Notes, the Company is required to increase the amount of the relevant payment by such amount as would result in the receipt by the relevant Noteholder of the amount which would have been received by it had no such withholding or deduction been required. The Tax Code of Georgia neither prohibits nor permits the inclusion of tax gross-up clauses (such as that set out in Condition 7 *(Taxation)*) in agreements or instruments made by Georgian companies. In practice, however, such gross-up provisions are widely respected by the tax authorities in Georgia.

Taxation on Sale of Notes

Taxation on the Sale of Notes by Non-resident Noteholders—General

It is unlikely that the sale of Notes, absent a sale of Notes on the territory of Georgia or to a Georgian tax resident, will trigger any Georgian tax obligations on the part of the Noteholders. However, the Tax Code of Georgia does not provide a clear definition of the place of sale (supply) of the Notes for the purposes of determining profit/income tax exposure and, accordingly, there is a risk that such interpretation may be susceptible to varying interpretations by the tax authorities.

The relative novelty of the introduction of debt securities, such as the Notes, to the Georgian market, as well as ambiguities with respect to the application of the respective provisions of the Tax Code of Georgia, which came into force on 1 January 2011, combined with the absence of established practices, may result in varying interpretations of the respective provisions of the Tax Code of Georgia being adopted by the tax authorities. In addition, the tax authorities have been known to apply such varying interpretations to the respective provisions of the Tax Code of Georgia to cope with the impracticability or unenforceability of certain provisions with respect to non-resident tax payers.

Taxation on Sale of Notes by Non-resident Legal Entities

Legal entities in Georgia are subject to profit tax at the rate of 15 per cent., calculated based on the taxable profit of the relevant entity. Under the Tax Code of Georgia, taxable profit, for these purposes, is defined as the difference between the gross income of the entity and the deductions granted or permitted under the Tax Code of Georgia. The same rate may be applicable to non-resident legal entities if they realise a capital gain on the sale of Notes to Georgian taxpayers and the same rate will be applicable to non-resident legal entities if they realise a capital gain on the sale of Notes to non-resident taxpayers on the territory of Georgia. The capital gain is calculated as the difference between the initial acquisition and subsequent sale prices. If such sale triggers a tax liability, non-residents will be obliged to report and pay tax to the Georgian tax authorities. However, the actual applicability of this taxation regime is subject to considerable impracticability and lack of enforceability, which may, in limited circumstances, lead to the adoption of peculiar and, at times, rather aggressive interpretations by the tax authorities. The applicability of profit tax may be affected by a double tax treaty between Georgia and the country of residence of the seller.

Taxation on Sale of Notes by Non-resident Natural Persons

Natural persons in Georgia are subject to income tax at the rate of 20 per cent. (the income tax rate applicable to natural persons in Georgia is set to gradually decrease over the next few years with the effective income tax rate expected to drop to 18 per cent. in 2013 and 15 per cent. thereafter) on the taxable income. Under the Tax Code of Georgia, taxable income, for these purposes, is defined as the difference between the gross income of the natural person and the deductions granted or permitted under the Tax Code of Georgia. The same rate will be applicable to non-resident individuals when such individuals sell Notes to any legal entity or individual on the territory of Georgia and the same rate may be applicable to non-resident individuals when such individuals sell Notes to a Georgian resident outside of the territory of Georgia. In such cases, income tax will be assessed on the difference between the initial purchase and subsequent sale price. If such sale triggers a tax liability, non-resident natural persons selling Notes will be obliged to report and pay tax to the Georgian tax authorities. The actual applicability of this taxation regime, however, is subject to considerable impracticability and lack of enforceability, which may, in limited circumstances, lead to the adoption of peculiar and, at times, rather aggressive interpretations by the tax authorities. As above, the applicability of income tax may be affected by a double tax treaty between Georgia and the country of residency of the seller.

Taxation of Sale of Notes by Non-resident Noteholders through a Georgian Brokerage Company

If a Noteholder (individual (natural person) or legal entity), which is not registered as a taxpayer for the purposes of the Tax Code of Georgia, sells Notes through a Georgian brokerage company licensed in Georgia, withholding tax will be assessed on the difference between the initial purchase and subsequent sale price. The amount of this withholding tax, in the case of a natural person selling the Notes, will be 20 per cent. and, in case of legal entities selling the Notes, will be 15 per cent., although varying interpretations may exist as to the tax rates applicable to both natural persons and legal entities. Certain exemptions may be available to individual Noteholders if such individuals maintain ownership of such Notes for more than two calendar years, although varying interpretations may preclude the applicability of such exemption.

Taxation on Sale of Notes by Residents of Georgia to Non-resident Legal Entities or Natural Persons

In the event of a sale of Notes by a resident of Georgia to a non-resident natural person or legal entity, no tax burden will fall on the purchaser. A sale of Notes by a Georgian resident taxpayer may be subject to 15 per cent. profit tax (for a legal entity) or 20 per cent. income tax (for an individual), with the tax being calculated based on the difference between the relevant initial acquisition price and the subsequent sale price. There may, however, be some uncertainty relating to the interpretation of the applicable provisions of the Tax Code of Georgia regarding the Notes. An aggressive interpretation of the tax law by local tax authorities may result in the imposition of additional tax obligations. The Georgian tax authorities may adopt the view that such taxes are to be assessed on the full amount of the sale price.

Certain exemptions from the 20 per cent. income tax may be available to an individual Noteholder if such Noteholder has held Notes for more than two calendar years, although varying interpretations may preclude the applicability of this exemption.

Taxation on Sale of Notes by Resident Noteholders through a Georgian Brokerage Company

If a Georgian resident individual Noteholder, who is not registered as a taxpayer for the purposes of the Tax Code of Georgia, sells Notes through a brokerage company registered in Georgia, withholding tax (currently at the rate of 20 per cent., although varying interpretations may exist as to the tax rate applicable) will be assessed on the difference between the initial purchase and subsequent sale price. Certain exemptions may be available to Georgian resident individual Noteholders if such individuals maintain ownership of such Notes for more than two calendar years, although varying interpretations may preclude the applicability of such exemption.

Taxation on Purchase of Notes by Residents of Georgia

Generally, the Tax Code of Georgia does not impose any tax burden on a purchaser of Notes who is a resident of Georgia, whether the purchaser is a legal entity or an individual. The tax authorities may, however, in limited circumstances, attempt to interpret certain provisions of the Tax Code of Georgia in such a way as to ensure that the seller complies with its tax obligations (as outlined above) by assessing the corresponding amount of withholding tax on the purchaser.

Value Added Tax

The Tax Code of Georgia considers the sale of Notes as a financial operation, which is exempt from value-added-tax.

Other Considerations

The Tax Code of Georgia expressly provides for right of the tax authority to re-examine the transaction price indicated by the respective parties, subject to certain procedural requirements.

Certain United States Federal Income Taxation Considerations

TO ENSURE COMPLIANCE WITH TREASURY DEPARTMENT CIRCULAR 230, HOLDERS ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF FEDERAL TAX ISSUES IN THIS OFFERING MEMORANDUM IS NOT INTENDED OR WRITTEN TO BE RELIED UPON, AND CANNOT BE RELIED UPON, BY HOLDERS FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON HOLDERS UNDER THE INTERNAL REVENUE CODE; (B) SUCH DISCUSSION IS INCLUDED HEREIN BY THE COMPANY IN CONNECTION WITH THE PROMOTION OR MARKETING (WITHIN THE MEANING OF CIRCULAR 230) BY THE COMPANY OF THE TRANSACTIONS OR MATTERS ADDRESSED HEREIN; AND (C) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISER.

* * * * *

The following is a summary of certain material United States federal income tax consequences of the acquisition, ownership and disposition of Notes by a U.S. Holder (as defined below). This summary deals only with initial purchasers of Notes at the issue price that are U.S. Holders and that will hold the Notes as capital assets. The discussion does not cover all aspects of United States federal income taxation that may be relevant to, or the actual tax effect that any of the matters described herein will have on, the acquisition, ownership or disposition of Notes by particular investors, and does not address state, local, foreign or other tax laws. This summary also does not discuss all of the tax considerations that may be relevant to certain types of investors subject to special treatment under the United States federal income tax laws (such as, U.S. expatriates, "dual resident" companies, real estate investment trusts, regulated investment companies, grantor trusts, financial institutions, insurance companies, investors liable for the alternative minimum tax, individual retirement accounts and other tax-deferred accounts, tax-exempt organisations, dealers in securities or currencies, investors that will hold the Notes, as part of straddles, hedging transactions or conversion transactions for United States federal income tax purposes or investors whose functional currency is not the U.S. Dollar, U.S. Holders who are residents of Georgia or holders otherwise subject to special tax rules).

As used herein, the term "**U.S. Holder**" means a beneficial owner of Notes that is, for United States federal income tax purposes, (i) an individual citizen or resident of the United States, (ii) a corporation created or organised under the laws of the United States or any state thereof, (iii) an estate the income of which is subject to United States federal income tax without regard to its source or (iv) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more United States persons have the authority to control all substantial decisions of the trust, or the trust has elected to be treated as a domestic trust for United States federal income tax purposes.

The United States federal income tax treatment of a partner in a partnership that holds Notes will depend on the status of the partner and the activities of the partnership. Prospective purchasers that are partnerships should consult their tax advisers concerning the United States federal income tax consequences to their partners of the acquisition, ownership and disposition of Notes by the partnership.

The summary is based on the tax laws of the United States, including the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations thereunder, published rulings and court decisions, all as of the date hereof and all subject to change at any time, possibly with retroactive effect.

THE SUMMARY OF UNITED STATES FEDERAL INCOME TAX CONSEQUENCES SET OUT BELOW IS FOR GENERAL INFORMATION ONLY. ALL PROSPECTIVE PURCHASERS SHOULD CONSULT THEIR TAX ADVISERS AS TO THE PARTICULAR TAX CONSEQUENCES TO THEM OF OWNING THE NOTES, INCLUDING THE APPLICABILITY AND EFFECT OF STATE, LOCAL, FOREIGN AND OTHER TAX LAWS AND POSSIBLE CHANGES IN TAX LAW.

Payments of Interest and Sale of Notes

General

Interest on a Note will be taxable to a U.S. Holder as ordinary income at the time it is received or accrued, depending on the holder's method of accounting for tax purposes. Interest paid by the Company on the Notes constitutes income from sources outside the United States. Prospective purchasers should consult their tax advisers concerning the applicability of the foreign tax credit and source of income rules to income attributable to the Notes.

Sale and Retirement of the Notes

A U.S. Holder will generally recognise gain or loss on the sale or retirement of a Note equal to the difference between the amount realised on the sale or retirement and the tax basis of the Note. A U.S. Holder's tax basis in a Note will generally be its U.S. Dollar cost. The amount realised does not include the amount attributable to accrued but unpaid interest, which will be taxable as interest income to the extent not previously included in income. Gain or loss recognised by a U.S. Holder on the sale or retirement of a Note will be capital gain or loss and will be long-term capital gain or loss if the Note was held by the U.S. Holder for more than one year. The deductibility of capital losses is subject to substantial limitations. Gain or loss realised by a U.S. Holder on the sale or retirement of a Note generally will be United States source. Therefore, a U.S. Holder may have insufficient foreign source income to utilise foreign tax credits attributable to any withholding or other foreign tax imposed on the sale or disposition. Prospective purchasers should consult their tax advisers as to the foreign tax credit implications of the sale or retirement of Notes.

Backup Withholding and Information Reporting

Payments of principal and interest on, and the proceeds of sale or other disposition of Notes by a United States paying agent or other United States intermediary will be reported to the IRS and to the U.S. Holder as may be required under applicable regulations. Backup withholding will be required on payments made within the United States, or by a United States paying agent or other United States intermediary, on Notes held by a U.S. Holder (other than an exempt recipient), if the U.S. Holder fails to furnish its correct taxpayer identification number, fails to report all interest and dividends required to be shown on its United States federal income tax returns, or otherwise fails to comply with, or establish an exemption from, the backup withholding requirements.

Backup withholding tax is not an additional tax. A holder generally will be entitled to credit any amounts withheld under the backup withholding rules against such holder's United States federal income tax liability provided the required information is furnished to the IRS in a timely manner.

Information Reporting Regarding Specified Foreign Financial Assets

The "Hiring Incentives to Restore Employment Act" and temporary and proposed regulations generally require individual U.S. holders ("**specified individuals**") and "specified domestic entities" with an interest in any "specified foreign financial asset" (which may include the Notes) to file an annual report on new IRS Form 8938 with information relating to the asset, including the maximum value thereof, for any taxable year in which the aggregate value of all such assets is greater than $50,000 on the last day of the taxable year or $75,000 at any time during the taxable year. Certain individuals are permitted to have an interest in a higher aggregate value of such assets before being required to file a report. The proposed regulations relating to specified domestic entities apply to taxable years beginning after December 31, 2011. Under the proposed regulations, "specified domestic entities" are domestic entities that are formed or used for the purposes of holding, directly or indirectly, specified foreign financial assets. Generally, specified domestic entities are certain closely held corporations and partnerships that meet passive income or passive asset tests and, with certain exceptions, domestic trusts that have a specified individual as a current beneficiary and exceed the reporting threshold. Specified foreign financial assets include any depository or custodial account held at a foreign financial institution; any debt or equity interest in a foreign financial institution if such interest is not regularly traded on an established securities market; and, if not held at a financial institution, (i) any stock or security issued by a non-U.S. person, (ii) any financial instrument or contract held for investment where the issuer or counterparty is a non-U.S. person, and (iii) any interest in an entity which is a non-U.S. person.

Depending on the aggregate value of your investment in specified foreign financial assets, you may be obligated to file an IRS Form 8938 under this provision if you are an individual U.S. holder. Specified domestic entities are not required to file Form 8938 until the proposed regulations are final. Penalties apply to any failure to file IRS Form 8938. Additionally, in the event a U.S. holder (either a specified individual or specified domestic entity) does not file such form, the statute of limitations on the assessment and collection of U.S. federal income taxes of such U.S. holder for the related tax year may not close before the date which is three years after the date such information is filed. You should consult your own tax advisor as to the possible application to you of this information reporting requirement and related statute of limitations tolling provision.

Legislation Affecting Taxation of Notes Held By or Through Entities Treated as Foreign Financial Institutions

Legislation enacted in 2010 generally imposes a withholding tax of 30 per cent. on certain payments, including on certain non-U.S. source payments made by non-U.S. financial institutions that enter into an agreement with the IRS and satisfy various U.S. information reporting and withholding requirements to non-U.S. financial institutions that do not enter into such agreement. Under proposed regulations, this tax may apply to a portion of interest paid on the Notes on or after January 1, 2017, although under the same proposed regulations (which need to be finalised to become effective) the tax generally would not apply to payments on debt obligations outstanding on January 1, 2013. Non-U.S. Holders should consult their tax advisers regarding the implications of this legislation and the guidance issued thereunder for their investment in the Notes.

3.8 per cent. Medicare Tax On "Net Investment Income"

For taxable years beginning after December 31, 2012, certain U.S. Holders, including individuals, estates, and trusts, will be subject to an additional 3.8 per cent. Medicare tax on unearned income. For individual U.S. Holders, the additional Medicare tax applies to the lesser of (i) "net investment income," or (ii) the excess of "modified adjusted gross income" over U.S. $200,000 (U.S. $250,000 if married and filing jointly or U.S. $125,000 if married and filing separately). "Net investment income" generally equals the taxpayer's gross investment income reduced by the deductions that are allocable to such income. Investment income generally includes passive income such as interest, dividends, annuities, royalties, rents, and capital gains. U.S. Holders are urged to consult their own tax advisors regarding the implications of the additional Medicare tax resulting from an investment in the Notes.

EU Savings Directive

Under EC Council Directive 2003/48/EC on the taxation of savings income, Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State. However, for a transitional period, Luxembourg and Austria may instead (unless during that period they elect otherwise) operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries). A number of non-EU countries and territories including Switzerland have adopted similar measures (a withholding system in the case of Switzerland).

The European Commission has proposed certain amendments to the EU Savings Directive, which may, if implemented, amend or broaden the scope of the requirements described above.

GENERAL INFORMATION

Authorisation

The Company has obtained all necessary consents, approvals and authorisations in Georgia in connection with the issue and performance of the Notes. The issue of the Notes was authorised by resolutions of the Board of Directors of the Company passed on 12 June 2012, by resolutions of the Supervisory Board of the Company passed on 14 June 2012 and by shareholders' resolutions of the Company passed on 15 June 2012. The Company's registration number is 202886010. The Company's telephone number is +995 219 9573.

Listing

It is expected that listing of the Notes on the Official List and admission of the Notes to trading on the Market will be granted on or about 5 July 2012, subject only to the issue of the Global Notes. The Global Notes are expected to be issued on or about 5 July 2012. Prior to official listing and admission to trading, dealings in the Notes will be permitted by the London Stock Exchange in accordance with its rules. The listing of the Notes on the Official List will be expressed as a percentage of their nominal amount (exclusive of accrued interest). Transactions will normally be effected for settlement in U.S. Dollars and for delivery on the third working day after the day of the transaction. The listing expenses in connection with the issue of the Notes are expected to be approximately U.S.$12,000.

No Significant Change

There has been no significant change in the financial or trading position of the Company or the Company and its consolidated subsidiaries taken as a whole, in each case, since 31 March 2012 and no material adverse change in the prospects of the Company and its consolidated subsidiaries taken as a whole, in each case, since 31 December 2011.

Clearing Systems

The Notes have been accepted for clearance through Euroclear, Clearstream, Luxembourg and DTC. The Common Code and ISIN for the Unrestricted Notes and the Common Code, ISIN and CUSIP number for the Restricted Notes are as follows:

Unrestricted Notes

ISIN:	XS0800346362
Common Code:	080034636

Restricted Notes

ISIN:	US37363BAA61
Common Code:	080082215
CUSIP:	37363B AA6

The address of Euroclear is 1 Boulevard du Roi Albert II, B-1210 Brussels, Belgium, The address of Clearstream, Luxembourg is 42 Avenue JF Kennedy, L-1855 Luxembourg. The address of DTC is 55 Water Street, New York, NY 10041, United States.

Indication of Yield

The indication of yield in relation to the Notes is 7.75 per cent. per annum. This yield is calculated at the Issue Date on the basis of the issue price. It is not an indication of future yield.

Litigation

Neither the Company nor its subsidiaries has been involved in any governmental, legal or arbitration proceedings (including such proceedings pending or threatened of which the Company is aware) during the previous twelve months that may have, or have had in the recent past, significant effects on the financial position or profitability of the Company or the Company and its subsidiaries, taken as a whole.

Documents

For the period of 12 months starting on the date on which this Prospectus is made available to the public, copies (and English translations where the documents in question are not in English) of the following documents will be available, during usual business hours on any weekday (Saturdays and public holidays excepted), for inspection at the offices of the Company:

(a) the Charter of the Company;

(b) the Consolidated Financial Statements;

(c) a copy of this Prospectus together with any supplement to this Prospectus or further prospectus; and

(d) the Fiscal Agency Agreement.

This Prospectus will be published on the website of the Regulatory News Service operated by the London Stock Exchange at *www.londonstockexchange.com/exchange/news/market-news/market-news-home.html*.

Auditors

KPMG of 4 Besiki Street, Tbilisi 0108, Georgia have audited, and in each case rendered an unqualified audit report on, the consolidated financial statements of the Company as at and for the respective years ended 31 December 2011 and 31 December 2010. The First Quarter Condensed Consolidated Financial Statements were reviewed by KPMG of 4 Besiki Street, Tbilisi 0108, Georgia.

The review report of KPMG in respect of the First Quarter Condensed Consolidated Financial Statements contains an "emphasis of matter", which draws attention to the fact that the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011, excluding the adjustments described in Note 18 to the First Quarter Condensed Consolidated Financial Statements, were based on the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011 that were approved for issuance by the Company on 15 May 2011. Such statements were neither audited nor reviewed. As part of preparing the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2012, management adjusted the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011. KPMG has reviewed the adjustments made and has stated in its review report that nothing has come to its attention that causes it to believe that such adjustments have not been properly applied.

KPMG is registered as a third country audit entity in accordance with the requirements of article 45 of the Statutory Audit Directive (2006/43/EC) (as implemented in the United Kingdom).

KPMG has given and has not withdrawn its written consent to the inclusion of its independent review report on the Company in relation to the First Quarter Condensed Consolidated Financial Statements (the "**Q1 2012 Review Report**") in the form and context in which it appears and has authorised the contents of the Q1 2012 Report for the purposes of paragraph 5.5.4(R)(2)(f) of the Prospectus Rules paragraph 13.1 of Annex IX and paragraph 7.3 of Annex XIII of the Commission Regulation (EC) 809/2004 (the "**Prospectus Directive Regulation**").

For the purposes of Prospectus Rule 5.5.4R(2)(f), KPMG accepts responsibility for the Q1 2012 Review Report as part this Prospectus and declares that it has taken all reasonable care to ensure that the information contained in the Q1 2012 Review Report is, to the best of its knowledge, in accordance with the facts and contains no omission likely to affect its import.

This declaration is included in this Prospectus in compliance with paragraph 1.2 of Annex IX and paragraph 1.2 of Annex XIII of the Prospectus Directive Regulation.

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The Audited Consolidated Financial Statements in this Prospectus are those of Georgian Railway LLC, the predecessor company to the Company. On 12 April 2012, Georgian Railway LLC changed its corporate form from a limited liability company to a joint stock company and was re-registered under the name "JSC Georgian Railway", in accordance with the *Law on Entrepreneurs*.

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Georgian Railway JSC
(formerly Georgian Railway LLC)

Condensed Consolidated Interim Financial Statements for the three-month periods ended 31 March 2012 and 2011

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Independent Auditors' Report on Review of Condensed Consolidated Interim Financial Statements

To the Management Board
Georgian Railway JSC (formerly Georgian Railway LLC)

Introduction

We have reviewed the accompanying condensed consolidated interim statements of financial position of Georgian Railway JSC (formerly Georgian Railway LLC) (the "Company") and its subsidiaries (the "Group") as at 31 March 2012 and 31 March 2011, and the related condensed consolidated interim statements of comprehensive income, changes in equity and cash flows for the three-month periods ended 31 March 2012 and 31 March 2011, and notes to the condensed consolidated interim financial statements. Management is responsible for the preparation and presentation of these condensed consolidated interim financial statements in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on these condensed consolidated interim financial statements based on our reviews.

Scope of reviews

We conducted our reviews in accordance with the International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of condensed consolidated interim financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our reviews, nothing has come to our attention that causes us to believe that the condensed consolidated interim financial statements as at 31 March 2012 and 31 March 2011, and for the three-month periods ended 31 March 2012 and 31 March 2011 are not prepared, in all material respects, in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*.

Emphasis of Matter

We draw attention to the fact that the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011, excluding the adjustments described in note 18, are based on the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011 that were approved for issuance on 15 May 2011. Such statements were neither audited nor reviewed. As part of preparing the current period condensed consolidated interim financial statements Management has adjusted the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011. We have reviewed the adjustments made and nothing has come to our attention that causes us to believe that these adjustments have not been properly applied.

Tbilisi branch of KPMG CIS Limited

Tbilisi Branch of KPMG CIS Limited
14 May 2012

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'000 GEL	Note	31 March 2012	31 December 2011	31 March 2011	31 December 2010
		Unaudited		Unaudited Restated	
ASSETS					
Non-current assets					
Property, plant and equipment	11	1,979,521	1,913,195	1,727,045	1,725,633
Investment property	11	-	6,838	9,926	9,926
Other non-current assets	11	227,795	276,039	174,014	136,375
Total non-current assets		**2,207,316**	**2,196,072**	**1,910,985**	**1,871,934**
Current assets					
Non-current assets held for distribution	11	33,033	-	-	-
Inventories		23,053	23,737	19,700	17,992
Current tax assets		-	511	-	-
Trade and other receivables		31,821	27,355	23,398	26,913
Prepayments and other current assets	12	57,387	27,714	53,381	42,665
Cash and cash equivalents	14	42,110	64,516	258,325	335,855
Bank deposits		87,196	76,449	36,896	38,021
Total current assets		**274,600**	**220,282**	**391,700**	**461,446**
Total assets		**2,481,916**	**2,416,354**	**2,302,685**	**2,333,380**
EQUITY AND LIABILITIES					
Equity					
Charter capital		990,545	1,000,463	985,869	985,376
Non-cash owner contribution reserve		38,031	38,043	35,404	35,404
Retained earnings		768,606	763,502	631,273	612,261
Total equity	13	**1,797,182**	**1,802,008**	**1,652,546**	**1,633,041**
Non-current liabilities					
Loans and borrowings	14	411,756	414,063	422,089	438,383
Trade and other payables		45	45	45	45
Deferred tax liabilities		59,550	60,925	66,548	66,521
Total non-current liabilities		**471,351**	**475,033**	**488,682**	**504,949**
Current liabilities					
Loans and borrowings	14	8,320	18,607	7,744	19,259
Trade and other payables	15	81,195	45,954	48,761	61,886
Liabilities to owner	16	22,291	13,188	26,543	29,241
Provisions		19,834	20,273	20,606	21,597
Other taxes payable		33,389	26,867	30,642	27,236
Other current liabilities		12,868	14,424	15,315	15,018
Dividends payable		28,000	-	-	-
Current tax liabilities		7,486	-	11,846	21,153
Total current liabilities		**213,383**	**139,313**	**161,457**	**195,390**
Total liabilities		**684,734**	**614,346**	**650,139**	**700,339**
Total equity and liabilities		**2,481,916**	**2,416,354**	**2,302,685**	**2,333,380**

The condensed consolidated interim statements of financial position are to be read in conjunction with the notes to, and forming part of, the condensed consolidated interim financial statements set out on pages 8 to 18.

'000 GEL	Note	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Unaudited	**Unaudited Restated**
Revenue	6	105,798	103,396
Other income		5,717	3,989
Employee benefits expense		(23,846)	(26,310)
Depreciation and amortization expense		(24,765)	(23,034)
Electricity and materials used	7	(12,346)	(12,669)
Other expenses	8	(14,703)	(20,464)
Results from operating activities		**35,855**	**24,908**
Finance income	9	10,425	10,869
Finance costs	9	(6,559)	(1,515)
Net finance income		**3,866**	**9,354**
Profit before income tax		**39,721**	**34,262**
Income tax expense	10	(6,617)	(5,719)
Profit and total comprehensive income for the period		**33,104**	**28,543**

These condensed consolidated interim financial statements were approved by the Management Board on 14 May 2012 and were signed on its behalf by:

Irakli Ezugbaia
General Director

Amiran Tevzadze
Acting Chief Accountant

The condensed consolidated interim statements of comprehensive income are to be read in conjunction with the notes to, and forming part of, the condensed consolidated interim financial statements set out on pages 8 to 18.

'000 GEL	Charter capital	Non-cash owner contribution reserve	Retained earnings	Total equity
Balance at 1 January 2011	**985,376**	**35,404**	**612,261**	**1,633,041**
Total comprehensive income for the period				
Profit and total comprehensive income for the period (unaudited, restated)	-	-	28,543	28,543
Transactions with owners, recorded directly in equity				
Non-cash contributions by and distributions to owners (unaudited, restated)	493	-	(9,531)	(9,038)
Balance at 31 March 2011 (unaudited, restated)	**985,869**	**35,404**	**631,273**	**1,652,546**
Balance at 1 January 2012	**1,000,463**	**38,043**	**763,502**	**1,802,008**
Total comprehensive income for the period				
Profit and total comprehensive income for the period (unaudited)	-	-	33,104	33,104
Transactions with owners, recorded directly in equity				
Dividends to owners (unaudited)	-	-	(28,000)	(28,000)
Non-cash contributions by and distributions to owners (unaudited)	(9,918)	(12)	-	(9,930)
Balance at 31 March 2012 (unaudited)	**990,545**	**38,031**	**768,606**	**1,797,182**

The condensed consolidated interim statements of changes in equity are to be read in conjunction with the notes to, and forming part of, the condensed consolidated interim financial statements set out on pages 8 to 18.

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
	Unaudited	Unaudited Restated
Cash flows from operating activities		
Cash receipts from customers	101,042	111,644
Cash paid to suppliers and employees	(50,362)	(47,540)
Cash flows from operations before income taxes	**50,680**	**64,104**
Income tax paid	-	(15,000)
Net cash from operating activities	**50,680**	**49,104**
Cash flows from investing activities		
Acquisition of property, plant and equipment	(49,581)	(99,414)
(Increase)/decrease in term deposits	(10,747)	1,125
(Increase)/decrease in restricted cash	(101)	5,790
Interest received	4,733	814
Net cash used in investing activities	**(55,696)**	**(91,685)**
Cash flows from financing activities		
Proceeds from borrowings	190	-
Interest paid	(20,647)	(22,330)
Net cash used in financing activities	**(20,457)**	**(22,330)**
Net decrease in cash and cash equivalents	**(25,473)**	**(64,911)**
Cash and cash equivalents at 1 January	61,553	323,943
Effect of exchange rate fluctuations on cash and cash equivalents	2,966	(6,743)
Cash and cash equivalents at 31 March	**39,046**	**252,289**

The condensed consolidated interim statements of cash flows are to be read in conjunction with the notes to, and forming part of, the condensed consolidated interim financial statements set out on pages 8 to 18.

1 Background

(a) Business environment

Georgian business environment

The Group's operations are primarily located in Georgia. Consequently, the Group is exposed to the economic and financial markets of Georgia which display characteristics of an emerging market. The conflict between Georgia and the Russian Federation has created additional uncertainty in the environment. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The condensed consolidated interim financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

(b) Reporting entity

Georgian Railway JSC (the "Company"), formerly incorporated as an LLC, and its subsidiaries (the "Group") comprise Georgian joint stock and limited liability companies as defined in the Civil Code of Georgia (see note 17).

The Group's principal activity is the operation of a nationwide railway system providing freight and passenger transportation services, maintenance and development of railway infrastructure and construction of railway lines within Georgia.

The Company was wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economy and Sustainable Development of Georgia as at 31 March 2011. On 25 October 2011 24% of the Company's charter capital was transferred to Partnership Fund JSC which is wholly owned by the State of Georgia (see note 17).

2 Basis of preparation

(a) Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*. They do not include all of the information required for full annual financial statements and should be read in conjunction with the consolidated financial statements of the Group as at and for the years ended 31 December 2011 and 2010.

(b) Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL"), which is the Company's functional currency and the currency in which these condensed consolidated interim financial statements are presented. All financial information presented in GEL has been rounded to the nearest thousand.

(c) Use of estimates and judgments

The preparation of condensed consolidated interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty were the same as those that applied to the consolidated financial statements as at and for the years ended 31 December 2011 and 2010.

3 Significant accounting policies

The accounting policies applied by the Group in these condensed consolidated interim financial statements are the same as those applied by the Group in its consolidated financial statements as at and for the years ended 31 December 2011 and 2010.

As part of preparing the current period condensed consolidated interim financial statements, Management identified errors in the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011 that were approved for issuance on 15 May 2011. These statements were neither audited nor reviewed. Management restated the condensed consolidated interim statements of comprehensive income, changes in equity and cash flows for the three-month period ended 31 March 2011 in accordance with International Financial Reporting Standard IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in these condensed consolidated interim financial statements to adjust for those errors (see note 18).

4 Financial risk management

The Group's financial risk management objectives and policies are consistent with those disclosed in the consolidated financial statements as at and for the years ended 31 December 2011 and 2010.

5 Operating segments

Information about reportable segments (unaudited)

'000 GEL	Freight transportation		Passenger transportation		Total	
	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Restated		Restated		Restated
External revenues	101,101	97,716	4,105	3,450	105,206	101,166
Reportable segment profit/(loss) before infrastructure costs, central overheads, net finance income or costs and income tax	60,752	57,943	(2,226)	(3,217)	58,526	54,726
Reportable segment assets	**359,081**	**337,733**	**108,382**	**101,359**	**467,463**	**439,092**

Reconciliation of reportable segment profit or loss (unaudited)

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Restated
Total profit or loss for reportable segments	58,526	54,726
Other profit or loss	(321)	(1,300)
Payroll expenses – infrastructure and headquarters	(8,044)	(12,768)
Depreciation expenses – infrastructure and headquarters	(12,622)	(12,068)
Net finance income	3,866	9,354
Other net unallocated expenses	(1,684)	(3,682)
Consolidated profit before income tax	**39,721**	**34,262**

There has been no change to the basis of segmentation or the measurement basis for the segment profit or loss since 31 December 2011 and 31 December 2010.

6 Revenue

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Restated
Freight traffic	87,276	89,271
Freight car rental	13,789	8,357
Passenger traffic	3,694	3,157
Other	1,039	2,611
	105,798	**103,396**

Railroad transportation in Georgia is a natural monopoly; however, prices are not subject to government regulation. According to clause 64 of the Railway Code of Georgia, which came into force on 1 July 2005, the Government of Georgia allowed the Group to set prices for all services provided including freight transportation, freight transportation-related additional services, and passenger and luggage transportation.

Tariffs for freight transportation are based on the International Rail Transit Tariff. The Group is a co-signatory of the Tariff Agreement together with CIS countries, Latvia, Lithuania and Estonia. The parties to the Agreement hold annual conferences to determine the tariff policy for the following year: each party declares tariffs denominated in Swiss Francs for railway transportation and states the general rules that apply to and modify tariffs. The agreed tariffs indicate the maximum level of tariffs applicable.

Effective from 1 February 2012, the Group changed the freight tariff currency from CHF to USD due to the volatility of the exchange rates between the CHF and other currencies and also to better align costs and revenues from its customers, which mainly trade in USD or GEL.

7 Electricity and materials used

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Restated
Electricity	6,114	8,466
Materials	3,953	1,771
Fuel	2,279	2,432
	12,346	**12,669**

8 Other expenses

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
		Restated
Freight car rental	4,995	5,561
Taxes other than income tax	4,992	4,168
Security	1,842	1,894
Repairs and maintenance	1,641	3,709
Write off of non-current assets	-	4,094
Other	1,233	1,038
	14,703	**20,464**

During the three-month period ended 31 March 2011 the Group identified impairment indicators leading to the write-off of several items of the Group's construction in progress. No such indicators were identified during the three-month period ended 31 March 2012.

9 Finance income and costs

(a) Foreign currency exchange rate fluctuations

Included in finance income for the three-month period ended 31 March 2012 is a net foreign exchange gain of GEL 6,426 thousand mainly as a result of the GEL depreciation against the Swiss Franc ("CHF") and GEL appreciation against the U.S. Dollar ("USD") as the Group held a significant part of its bank balances in CHF and the Group's loans and borrowing were denominated in USD during the three-month period ended 31 March 2012. In the three-month period ended 31 March 2011, the Group recognised a foreign exchange gain of GEL 10,251 thousand due to GEL appreciation against USD partly offset by the impact of GEL appreciation against CHF.

(b) Impairment of receivables

Included in finance costs for the three-month period ended 31 March 2012 is an impairment loss of GEL 6,536 thousand mainly due to disputed receivables for which the Group does not expect a repayment (three-month period ended 31 March 2011: GEL 1,514 thousand).

10 Income tax expense

Income tax is recognised based on management's best estimate of the weighted average annual income tax rate expected for the full financial year applied to the pre-tax income of the interim periods. The Group's consolidated effective tax rate for the three-month period ended 31 March 2012 was 17 percent (three-month period ended 31 March 2011: 17 percent). The statutory tax rate is 15 percent.

11 Property, plant and equipment and other non-current assets

(c) Acquisitions and disposals of property, plant and equipment

During the three-month period ended 31 March 2012 the Group acquired assets with a cost, excluding capitalized borrowing costs, of GEL 83,333 thousand mainly relating to the Main Line Modernization and Tbilisi Bypass projects (31 March 2011: GEL 30,144 thousand).

Capitalized borrowing costs related to the Main Line Modernization project for the three-month period ended 31 March 2012 amounted to GEL 6,056 thousand (31 March 2011: GEL 6,380 thousand) and capitalized borrowing costs related to the Tbilisi Bypass project for the three-month period ended 31 March 2012 amounted to GEL 4,254 thousand (31 March 2011: GEL 4,496 thousand).

During the three-month period ended 31 March 2012 assets with a carrying amount of GEL 827 thousand were transferred to the owner (31 March 2011: GEL 12,156 thousand).

(d) Investment property

In March 2012 the decision was made to transfer the Tbilisi Central Station building to the Government of Georgia although the Group retains a right of use over that portion of the Tbilisi Central Station necessary for the Group's operations. In the three-month period ended 31 March 2012, investment property of 6,838 thousand, mainly relating to the Tbilisi Central Station, was reclassified to property, plant and equipment due to the change in use of the property.

(e) Other non-current assets

The increase in other non-current assets is mainly related to prepayments made and materials and equipment purchased for the Main Line Modernization and Tbilisi Bypass Projects.

(f) Non-current assets held for distribution

During the three-month period ended 31 March 2012, the Group resolved to transfer to the Government of Georgia the partially-constructed Batumi Tower in the western part of Georgia, as well as the land plots upon which the building is being constructed, all of the rights and obligations under the construction agreement and all other agreements executed in connection with this project. The total value of such assets reclassified from property, plant and equipment and prepayments for non-current assets were GEL 33,033 thousand consisting land plots of GEL 4,220 thousand, construction in progress of GEL 9,186 thousand and prepayments for construction contracts of GEL 19,627 thousand. The transfer was completed in April 2012.

(g) Capital commitments and major projects

As at 31 March 2012 the Group entered into contracts for the construction or purchase of property, plant and equipment of GEL 854,646 thousand (31 March 2011: GEL 611,582 thousand), mainly relating to the Main Line Modernization (GEL 534,288 thousand) and Tbilisi Bypass Projects (GEL 277,815 thousand) excluding prepayments made for the contracts amounting to GEL 132,479 thousand as at 31 March 2012 (31 March 2011: GEL 71,957 thousand).

12 Prepayments and other current assets

During the three-month period ended 31 March 2012 the Group revised its estimate of the VAT recoverable within 12 months from 31 March 2012, which resulted in an increase in prepayments and other current assets and a reduction in other non-current assets as at 31 March 2012 of GEL 26,966 thousand.

13 Equity

(a) Dividends

Dividends were declared by the Group during the three-month period ended 31 March 2012 of GEL 28,000 thousand (three-month period ended 31 March 2011: nil) (see note 17).

14 Loans and borrowings

No significant issues or repayments of loans and borrowings occurred during the three-month periods ended 31 March 2012 and 31 March 2011. Changes in the carrying amounts are attributable to interest accruals and payments and foreign currency translation differences.

In July 2010 the Group issued bonds with a face value of USD 250 million maturing in July 2015. The proceeds are being used for the implementation of two capital projects: the Main Line Modernization and the Tbilisi Bypass.

Cash and cash equivalents include restricted cash of GEL 3,064 thousand as at 31 March 2012 (31 December 2011: GEL 2,963 thousand; 31 March 2011: GEL 6,036 thousand; 31 December 2010: GEL 11,912 thousand).

15 Trade and other payables

As at 31 March 2012 construction works completed by a contractor for the Bypass Project amounted to GEL 40,342 thousand representing an increase of GEL 35,339 thousand compared to 31 December 2011.

16 Related party transactions

(a) Parent and ultimate controlling party

The Company was wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economy and Sustainable Development of Georgia as at 31 March 2011. On 25 October 2011 24% of the Company's charter capital was transferred to Partnership Fund JSC which is wholly owned by the State of Georgia.

(b) Transactions with key management personnel

Key management received the following remuneration during the three-month periods ended 31 March 2012 and 2011, which is included in employee benefits expenses:

'000 GEL	Three-month period ended 31 March 2012	Three-month period ended 31 March 2011
Salaries and bonuses	**247**	279

(c) Other related party transactions

(i) Revenue, purchases and expenses

Until September 2011 the Group purchased most of its electricity from a State-owned operator which amounted to GEL 675 thousand for the three-month period ended 31 March 2012 (three-month period ended 31 March 2011: GEL 6,838 thousand). In September 2011, the Company signed an agreement for the purchase and sale of electricity from another provider. The Group also purchases security services from a state agency which amounted to GEL 1,902 thousand for the three-month period ended 31 March 2012 (three-month period ended 31 March 2011: GEL 1,910 thousand). During the three-month period ended 31 March 2012 the Group purchased goods of GEL 1,258 thousand from a State-owned company (three-month period ended 31 March 2011: GEL 656 thousand). The Group usually does not have significant balances for these purchases.

Management estimates that the aggregate amounts of other income and expenses and the related balances with other government-related entities are not significant.

(ii) Other balances

'000 GEL	31 March 2012	31 December 2011	31 March 2011	31 December 2010
Liabilities to owner	**22,291**	13,188	**26,543**	29,241

Liabilities to owners relate to non-core property, plant and equipment that has been withdrawn but not yet transferred formally to the Government of Georgia. These liabilities are recognised at the carrying amount of assets to be transferred to the Government of Georgia.

17 Subsequent events

In April 2012 the Company changed its legal form from a limited liability company, whose charter capital is not divided into shares, to a joint stock company with a share capital of 1,049,751,200 shares having a par value of GEL 1 per share.

In April 2012, a Memorandum of Understanding was signed between the Company and the Government of Georgia which creates a set-off mechanism for the Company whereby dividends that would otherwise be payable to the State in respect of its shares in the Company are offset against the Group's future expenses in relation to the Bypass Project and in exchange for the transfer, by the Group to the Government, of approximately 70.1 hectares of land plots in Central Tbilisi. The amount to be offset under this mechanism is subject to an aggregate cap of CHF 138.0 million. If the dividends payable to the State are insufficient to cover the reimbursable expenses in full, the Group has the right to retain a pro-rata ownership interest in the land plots.

Pursuant to Government Resolution No. 789 of 30 April 2012 on "Contributing the Shares of JSC "Georgian Railway" owned by the State into the capital of JSC Partnership Fund", on 3 May 2012 the State transferred additional shares in the Company representing 1.5 per cent. of the Company's authorised capital, by way of capital contribution, to the JSC Partnership Fund.

In April 2012, the Company made a dividend payment in the amount of GEL 10 million.

In April 2012, land plots and assets located in Kulevi, with an aggregate value of approximately GEL 48.0 million, were contributed by the Government of Georgia to the Company's capital.

In April 2012, as part of the Modernisation Project, 33 land plots (including six buildings and a reservoir), with an aggregate value of approximately GEL 11.2 million, were contributed by the Government of Georgia to the Company's capital.

On 16 April 2012 the Government of Georgia announced its intention to proceed with an initial public offering of 25% of the ordinary shares (in the form of Global Depositary receipts) of the Company on The London Stock Exchange.

18 Correction of prior period errors

As part of preparing the current period condensed consolidated interim financial statements, Management identified errors in the condensed consolidated interim financial statements as at and for the three-month period ended 31 March 2011 that were approved for issuance on 15 May 2011. Management restated the condensed consolidated interim statements of comprehensive income, changes in equity and cash flows for the three-month period ended 31 March 2011 in accordance with International Financial Reporting Standard IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* in these condensed consolidated interim financial statements to adjust for those errors. This has resulted in the following changes in the amounts reported previously. There was no impact on the statement of financial position as at 31 December 2010.

Condensed consolidated interim statement of financial position as at 31 March 2011

'000 GEL	Balances as previously reported as at 31 March 2011	Restatements	Restated balances as at 31 March 2011
Non-current assets	1,919,242	(8,257)	1,910,985
Current assets	385,917	5,783	391,700
Total assets	**2,305,159**	**(2,474)**	**2,302,685**
Equity	1,646,176	6,370	1,652,546
Non-current liabilities	488,610	72	488,682
Current liabilities	170,373	(8,916)	161,457
Total equity and liabilities	**2,305,159**	**(2,474)**	**2,302,685**

Condensed consolidated interim statement of comprehensive income for the three-month period ended 31 March 2011

'000 GEL	Balances as previously reported as at 31 March 2011	Restatements	Restated balances as at 31 March 2011
Results from operating activities	31,433	(6,525)	24,908
Net finance (costs)/income	(1,963)	11,317	9,354
Profit before income tax	**29,470**	**4,792**	**34,262**
Income tax expense	(7,623)	1,904	(5,719)
Profit and total comprehensive income for the period	**21,847**	**6,696**	**28,543**

The errors identified by Management principally related to borrowing costs of GEL 10,875 thousand which should have been capitalised and certain items of construction in progress of GEL 4,094 thousand for which indicators of impairment were identified during the three-month period ended 31 March 2011 and which should have been written off.

Condensed consolidated interim statement of changes in equity for the three-month period ended 31 March 2011

'000 GEL	Balances as previously reported as at 31 March 2011	Restatements	Restated balances as at 31 March 2011
Balance as at 1 January 2011	**1,633,041**	-	**1,633,041**
Profit and total comprehensive income for the period	21,847	6,696	28,543
Total contributions by and distributions to owners	(8,712)	(326)	(9,038)
Balance as at 31 March 2011	**1,646,176**	**6,370**	**1,652,546**

Condensed consolidated interim statement of cash flows for the three-month period ended 31 March 2011

'000 GEL	Balances as previously reported as at 31 March 2011	Restatements	Restated balances as at 31 March 2011
Net cash from operating activities	15,025	34,079	49,104
Net cash used in investing activities	(86,828)	(4,857)	(91,685)
Net cash used in financing activities	-	(22,330)	(22,330)
Net increase in cash and cash equivalents	(71,803)	6,892	(64,911)
Cash and cash equivalents at 1 January 2011	373,876	(49,933)	323,943
Effect of exchange rate fluctuations on cash and cash equivalents	(7,055)	312	(6,743)
Cash and cash equivalents at 31 March 2011	**295,018**	**(42,729)**	**252,289**

Management identified errors related to the classification of deposits of GEL 36,896 thousand and restricted cash of GEL 6,036 thousand as cash and cash equivalents as at 31 March 2011.

Management also changed the classification of interest paid for the three-month period ended 31 March 2011 of GEL 22,330 thousand as financing activities rather than operating activities consistent with the presentation in the consolidated financial statements as at and for the year ended 31 December 2011.

Georgian Railway LLC

Consolidated Financial Statements
for the year ended 31 December 2011

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Independent Auditors' Report

To the Management Board
Georgian Railway LLC

We have audited the accompanying consolidated financial statements of Georgian Railway LLC (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2011, and the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2011, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Tbilisi branch of KPMG CIS Limited

Tbilisi Branch of KPMG CIS Limited
16 March 2012

KPMG CIS TBILISI BRANCH 204428146

'000 GEL	Note	2011	2010
ASSETS			
Non-current assets			
Property, plant and equipment	12	1,913,195	1,725,633
Investment property		6,838	9,926
Other non-current assets	13	276,039	136,375
Total non-current assets		**2,196,072**	**1,871,934**
Current assets			
Inventories	14	23,737	17,992
Current tax assets		511	-
Trade and other receivables	15	27,355	26,913
Prepayments and other current assets	16	27,714	42,665
Cash and cash equivalents	17	64,516	335,855
Bank deposits		76,449	38,021
Total current assets		**220,282**	**461,446**
Total assets		**2,416,354**	**2,333,380**
EQUITY AND LIABILITIES			
Equity			
Charter capital	18	1,000,463	985,376
Non-cash owner contribution reserve		38,043	35,404
Retained earnings		763,502	612,261
Total equity		**1,802,008**	**1,633,041**
Non-current liabilities			
Loans and borrowings	19	414,063	438,383
Trade and other payables	20	45	45
Deferred tax liabilities	21	60,925	66,521
Total non-current liabilities		**475,033**	**504,949**
Current liabilities			
Loans and borrowings	19	18,607	19,259
Trade and other payables	20	45,954	61,886
Liabilities to owners	18	13,188	29,241
Provisions	22	20,273	21,597
Other taxes payable	23	26,867	27,236
Other current liabilities		14,424	15,018
Current tax liabilities		-	21,153
Total current liabilities		**139,313**	**195,390**
Total liabilities		**614,346**	**700,339**
Total equity and liabilities		**2,416,354**	**2,333,380**

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 38.

'000 GEL	Note	2011	2010
Revenue	7	477,377	404,687
Other income		12,025	17,818
Employee benefits expense		(108,493)	(111,257)
Depreciation and amortization expense		(92,137)	(98,749)
Electricity and materials used	8	(47,763)	(44,620)
Other expenses	9	(73,219)	(71,815)
Results from operating activities		**167,790**	**96,064**
Finance income	10	27,036	45,411
Finance costs	10	(10,492)	(17,669)
Net finance income		**16,544**	**27,742**
Profit before income tax		**184,334**	**123,806**
Income tax expense	11	(9,921)	(22,273)
Profit and total comprehensive income for the year		**174,413**	**101,533**

These consolidated financial statements were approved by the Management Board on 16 March 2012 and were signed on its behalf by:

Irakli Ezugbaia
General Director

Amiran Tevzadze
Acting Chief Accountant

The consolidated statement of comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 38.

'000 GEL	Charter capital	Non-cash owner contribution reserve	Retained earnings	Total equity
Balance at 1 January 2010	967,207	25,311	556,165	1,548,683
Total comprehensive income for the year				
Profit and total comprehensive income for the year	-	-	101,533	101,533
Transactions with owners, recorded directly in equity				
Dividends to owners	-	-	(36,000)	(36,000)
Net non-cash contributions by and distributions to owners, net (see note 18)	14,278	10,093	(5,546)	18,825
Transfer of retained earnings to charter capital (see note 18)	3,891	-	(3,891)	-
Total contributions by and distributions to owners	18,169	10,093	(45,437)	(17,175)
Balance at 31 December 2010	**985,376**	**35,404**	**612,261**	**1,633,041**
Balance at 1 January 2011	985,376	35,404	612,261	1,633,041
Total comprehensive income for the year				
Profit and total comprehensive income for the year	-	-	174,413	174,413
Transactions with owners, recorded directly in equity				
Net non-cash contributions by and distributions to owners, net (see note 18)	(3,385)	2,639	(23,172)	(23,918)
Cash contributions by and distributions to owners (see note 18)	18,472	-	-	18,472
Total contributions by and distributions to owners	15,087	2,639	(23,172)	(5,446)
Balance at 31 December 2011	**1,000,463**	**38,043**	**763,502**	**1,802,008**

The consolidated statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 38.

'000 GEL	**Note**	**2011**	**2010**
Cash flows from operating activities			
Cash receipts from customers		480,859	433,749
Cash paid to suppliers and employees		(224,670)	(195,162)
Cash flows from operations before income taxes and interest paid		**256,189**	**238,587**
Income tax paid		(30,259)	(4,923)
Net cash from operating activities		**225,930**	**233,664**
Cash flows from investing activities			
Acquisition of property, plant and equipment		(436,028)	(281,738)
Proceeds from sale of investments		-	6,300
Increase in term deposits		(38,428)	(38,021)
Decrease/(increase) in restricted cash		8,949	(11,912)
Interest received		9,883	3,350
Net cash used in investing activities		**(455,624)**	**(322,021)**
Cash flows from financing activities			
Proceeds from borrowings		1,144	455,109
Repayment of borrowings		(477)	(28,975)
Interest paid		(43,080)	(2,163)
Dividends paid		-	(36,000)
Contribution of cash by owners		20,000	-
Distribution of cash to owners		(1,528)	-
Net cash (used in)/from financing activities		**(23,941)**	**387,971**
Net (decrease)/increase in cash and cash equivalents		**(253,635)**	**299,614**
Cash and cash equivalents at 1 January		323,943	1,361
Effect of exchange rate fluctuations on cash and cash equivalents		(8,755)	22,968
Cash and cash equivalents at 31 December	17	**61,553**	**323,943**

The consolidated statement of cash flows is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 38.

1. Background

(a) Business environment

The Group's operations are primarily located in Georgia. Consequently, the Group is exposed to the economic and financial markets of Georgia which display characteristics of an emerging market. The conflict between Georgia and the Russian Federation has created additional uncertainty in the environment. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Georgia. The consolidated financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

(b) Organisation and operations

Georgian Railway LLC (the "Company") and its subsidiaries (the "Group") comprise Georgian limited liability companies and joint stock companies as defined in the Civil Code of Georgia. The Company was established as a state-owned enterprise in December 1998 by the Decree of President of Georgia # 929 as an entity engaged in the provision of railway transportation services in Georgia.

The Company's registered office is 15 Queen Tamar Avenue, Tbilisi 0112, Georgia.

The Group's principal activity is the operation of a nationwide railway system providing freight and passenger transportation services, maintenance and development of railway infrastructure and construction of railway lines within Georgia.

The Company was wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economy and Sustainable Development of Georgia as at 30 September 2011. On 25 October 2011 24% of the Company's charter capital was transferred to Partnership Fund JSC which is wholly owned by the State of Georgia. Related party transactions are disclosed in note 28.

2. Basis of preparation

(a) Statement of compliance

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

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that property, plant and equipment was revalued to determine deemed cost as part of the adoption of IFRSs.

(c) Functional and presentation currency

The national currency of Georgia is Georgian Lari ("GEL"), which is the Company's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in GEL has been rounded to the nearest thousand.

(d) Use of estimates and judgments

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

- Note 3(d) – useful lives of property, plant and equipment
- Note 24(b) – impairment allowances for trade and other receivables

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year is included in note 22 – provisions.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

(ii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

(b) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period.

Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising in retranslation are recognised in profit or loss.

(c) Financial instruments

Non-derivative financial instruments comprise trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

(i) Non-derivative financial assets

The Group initially recognises loans and receivables on the date that they are originated. All other financial assets are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group classifies non-derivative financial assets into the loans and receivables category.

Loans and receivables

Loans and receivables are a category of financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses (see note3(f)(i)).

Loans and receivables category comprise trade and other receivables and cash and cash equivalents.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with maturities of three months or less from the acquisition date. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(ii) Non-derivative financial liabilities

The Group initially recognises financial liabilities on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortised cost using the effective interest method.

Other financial liabilities comprise loans and borrowings and trade and other payables.

(iii) Charter capital

Charter capital is classified as equity.

Reduction of charter capital

Charter capital reductions and non-cash distributions are recognised at the carrying amount of the assets distributed at the date of the distribution where the asset is ultimately controlled by the same parties both before and after the distribution.

Increase of charter capital

When charter capital is increased, any difference between the registered amount of charter capital and the fair value of the assets contributed is recognised as a separate component of equity as non-cash owner contribution reserve.

(d) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses. The cost of property, plant and equipment at 1 January 2007, the date of transition to IFRSs, was determined by reference to its fair value at that date.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Any gain or loss on disposal of an item of property, plant and equipment is determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and is recognised net within other income/other expenses in profit or loss.

(ii) Subsequent costs

The cost of replacing a component of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Group, and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.
Maintenance and repair expenses are recognised as follows:

- Rolling stock:
  - current maintenance expenses during the useful life of equipment (repair work and replacement of unusable and missing parts) are recognised as operating expenses in profit or loss as incurred;
  - expenses under multi-year major overhaul programmes are capitalised as a separate overhaul component and depreciated separately from the main asset;
  - overhauls performed near the end of the useful life of an asset, together with refurbishment, are capitalised when they extend the useful life of the underlying asset.

- Fixed installations:
  - current maintenance and repair expenses (technical inspections, maintenance contracts, etc.) are recognised as operating expenses in profit or loss as incurred;
  - labour, materials and other costs (associated with the installation of rails, sleepers and ballast) under multi-year major building or infrastructure maintenance programmes are capitalised through the partial or total replacement of each component concerned;
  - costs associated with infrastructure improvements are capitalized to the extent that they increase the functionality (traffic working speed) of the asset.

(iii) Depreciation

Items of property, plant and equipment are depreciated from the date that they are installed and are ready for use, or in respect of internally constructed assets, from the date that the asset is completed and ready for use. Depreciation is based on the cost of an asset less its residual value. Significant components of individual assets are assessed and if a component has a useful life that is different from the remainder of that asset, that component is depreciated separately.

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Land is not depreciated.

The estimated useful lives of significant items of property, plant and equipment for the current and comparative periods are as follows:

• buildings and constructions	44 years
• rail track infrastructure	23 years
• transport, machinery, equipment and other	12 years

Depreciation methods, useful lives and residual values are reviewed at each financial year end and adjusted if appropriate.

(e) Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first-in first-out principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(f) Impairment

(i) Non-derivative financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Group on terms that the Group would not consider otherwise, indications that a debtor will enter bankruptcy, adverse changes in the payment status of borrowers in the Group or economic conditions that correlate with defaults.

The Group considers evidence of impairment for loans and receivables at both a specific asset and collective level. All individually significant loans and receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables that are not individually significant are collectively assessed for impairment by grouping together loans and receivables with similar risk characteristics.

In assessing collective impairment the Group uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or CGU.

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated to reduce the carrying amounts of assets in the CGU (group of CGUs) on a pro rata basis.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(g) Employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee, and the obligation can be estimated reliably.

(h) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

(i) Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. A financial guarantee liability is recognised initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognised less cumulative amortisation or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees are recognised when losses are considered probable and can be measured reliably.

(i) Revenue

(i) Transportation activities

Revenue from freight and passenger transportation is measured at the fair value of the consideration received or receivable. Freight and passenger transportation revenue is recognized in profit or loss according to the percentage of completed service method based on transit time of freight and passengers moving from the original location to the final destination.

Revenue from services rendered in stations is recognised in profit or loss when the service is rendered.

(ii) Rental income

Rental income from investment property or other assets rented is recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

(j) Other expenses

(i) Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

(ii) Social expenditure

To the extent that the Group’s contributions to social programs benefit the community at large and are not restricted to the Group’s employees, they are recognised in profit or loss as incurred.

(k) Finance income and costs

Finance income comprises interest income on funds invested and foreign currency gains. Interest income is recognised as it accrues in profit or loss, using the effective interest method.

Finance costs comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses and impairment losses recognised on financial assets.

Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance cost depending on whether foreign currency movements are in a net gain or net loss position.

(l) Income tax

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

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

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; and
- temporary differences related to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(m) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are reviewed regularly by the Group's Management Board to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the Group's Management Board include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly railway infrastructure, corporate assets (primarily the Group's headquarters), head office expenses, financial income and expenses, tax expenses and tax assets and liabilities. Items related to infrastructure are not allocated as the Group has not implemented systems for such allocations.

Segment capital expenditure is the total cost incurred during the year to acquire property, plant and equipment, and intangible assets other than goodwill.

4. New standards and interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2011, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the Group's operations. The Group plans to adopt these pronouncements when they become effective.

- IFRS 9 *Financial Instruments* will be effective for annual periods beginning on or after 1 January 2015. The new standard is to be issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement*. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding classification and measurement of financial liabilities was published in October 2010. The remaining parts of the standard are expected to be issued during 2012. The Group recognises that the new standard introduces many changes to the accounting for financial instruments and is likely to have a significant impact on Group's consolidated financial statements. The impact of these changes will be analysed during the course of the project as further phases of the standard are issued. The Group does not intend to adopt this standard early.

- IFRS 12 *Disclosure of Interests in Other Entities* will be effective for annual periods beginning on or after 1 January 2013. The new standard contains disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. Interests are widely defined as contractual and non-contractual involvement that exposes an entity to variability of returns from the performance of the other entity. The expanded and new disclosure requirements aim to provide information to enable the users to evaluate the nature of risks associated with an entity's interests in other entities and the effects of those interests on the entity's financial position, financial performance and cash flows. Entities may early present some of the IFRS 12 disclosures early without a need to early-adopt the other new and amended standards. However, if IFRS 12 is early-adopted in full, then IFRS 10, IFRS 11, IAS 27 (2011) and IAS 28 (2011) must also be early-adopted.

- Various *Improvements to IFRSs* have been dealt with on a standard-by-standard basis. All amendments, which result in accounting changes for presentation, recognition or measurement purposes, will come into effect for annual periods beginning after 1 January 2011. The Group has not yet analysed the likely impact of the improvements on its financial position or performance.

5. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and for disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant and equipment

The fair value of property, plant and equipment contributed by the owners is based on market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. The fair value of items of plant, equipment, fixtures and fittings is based on market approach and cost approaches using quoted market prices for similar items when available.

When no quoted market prices are available, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

(b) Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

(c) Financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

6. Operating segments

The Group has two reportable segments, as described below, which are the Group's strategic business units. The strategic business units offer different products and services, and are managed separately because they require different technology and marketing strategies. For each of the strategic business units, the Group's Management Board reviews internal management reports on at least a quarterly basis. The following summary describes the operations in each of the Group's reportable segments:

- *Freight transportation*. Includes transportation of goods and commodities and related services.
- *Passenger transportation*. Includes transportation of passengers and luggage.

There are no inter-segment charges.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before infrastructure costs, central over heads, interest and income tax, as included in the internal management reports that are reviewed by the Group's Management Board. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries.

(i) Information about reportable segments

’000 GEL	Freight transportation 2011	Freight transportation 2010	Passenger transportation 2011	Passenger transportation 2010	Total 2011	Total 2010
External revenues	454,872	377,868	17,629	17,343	472,501	395,211
Depreciation and amortization	(38,044)	(39,522)	(6,696)	(7,840)	(44,740)	(47,362)
Reportable segment profit/(loss) before infrastructure costs, net interest cost and income tax	289,190	237,419	(10,906)	(10,798)	278,284	226,621
Reportable segment assets	353,766	340,474	106,823	90,126	460,589	430,600
Capital expenditure and other additions to non-current assets	34,495	20,722	28,157	20,976	62,652	41,698

(ii) Reconciliations of reportable segment revenues, profit or loss, assets and other material items

’000 GEL	2011	2010
Revenues		
Total revenue for reportable segments	472,501	395,211
Other revenue	4,876	9,476
Consolidated revenue	**477,377**	**404,687**
Profit or loss		
Total profit or loss for reportable segments	278,284	226,621
Other profit or loss	(835)	(537)
Payroll expenses – infrastructure and headquarters	(41,464)	(48,920)
Depreciation expenses – infrastructure and headquarters	(45,392)	(51,116)
Net finance income	16,544	27,742
Other net unallocated expenses	(22,803)	(29,984)
Consolidated profit before income tax	**184,334**	**123,806**
Assets		
Total assets for reportable segments	460,589	430,600
Property, plant and equipment - infrastructure and headquarters	1,522,671	1,365,672
Other unallocated assets, principally cash and non-current assets	433,094	537,108
Consolidated total assets	**2,416,354**	**2,333,380**

(iii) Other material items 2011

’000 GEL	Reportable segment totals	Infrastructure and headquarters	Consolidated totals
Capital expenditure and other additions to non-current assets	62,652	355,625	418,277
Depreciation and amortization	44,740	47,397	92,137

(iv) Other material items 2010

’000 GEL	**Reportable segment totals**	**Infrastructure and headquarters**	**Consolidated totals**
Capital expenditure and other additions to non-current assets	41,698	231,122	272,820
Depreciation and amortization	47,362	51,387	98,749

(v) Geographical information

Substantially all of the Group’s revenue is from Georgia and CIS countries and the non-current assets of the Group are located in Georgia.

(vi) Major customer

In 2011 one customer of the Group’s freight transportation segment represented approximately 30% of the Group’s total revenue (GEL 142,899 thousand). In 2010 one customer of the Group’s freight transportation segment represented approximately 30% of the Group’s total revenue (GEL 119,684 thousand).

7. Revenue

’000 GEL	**2011**	**2010**
Freight traffic	410,915	354,583
Freight car rental	43,957	23,285
Passenger traffic	15,257	14,685
Communication services	-	4,413
Other	7,248	7,721
	477,377	**404,687**

Railroad transportation in Georgia is a natural monopoly; however the prices are not subject to government regulation. According to clause 64 of the Railway Code of Georgia, which came into force on 1 July 2005, the Government of Georgia allowed the Group to set the prices for all services provided, including freight transportation, freight transportation-related additional services, and passenger and luggage transportation.

Tariffs for freight transportation are based on the International Rail Transit Tariff. The Group is a co-signatory of the Tariff Agreement together with CIS countries, Latvia, Lithuania and Estonia. The parties to the Agreement hold annual conferences to determine the tariff policy for the following year: each party declares tariffs denominated in Swiss Francs for railway transportation and states the general rules that apply to and modify tariffs. The agreed tariffs indicate the maximum level of tariffs applicable.

From January 2011 the Group changed the commercial terms of its agreement with a counterparty where both counterparties eliminated the full discount for a specified number of days of freight car rental leading to a significant increase in both freight car rental revenue and freight car rental expenses disclosed in note 9.

8. Electricity and materials used

’000 GEL	**2011**	**2010**
Electricity	24,180	21,386
Materials	13,849	13,565
Fuel	9,734	9,669
	47,763	**44,620**

9. Other expenses

’000 GEL	**2011**	**2010**
Freight car rental	23,400	9,046
Taxes other than income tax	17,658	16,277
Repairs and maintenance	11,100	5,009
Security	7,375	7,650
Write off of non-current assets	4,094	4,831
Guarantee provisions (see note 22)	-	15,509
Communication services	-	3,611
Other	9,592	9,882
	73,219	**71,815**

10. Finance income and finance costs

’000 GEL	**2011**	**2010**
Recognised in profit or loss		
Interest income on bank deposits	10,941	3,229
Net foreign exchange gain	16,095	42,182
Finance income	27,036	45,411
Impairment loss on trade receivables (note 24 (b)(ii))	(7,405)	(6,053)
Prepaid finance costs written off (note 19)	(3,047)	-
Interest expense on financial liabilities	(40)	(11,616)
Finance costs	(10,492)	(17,669)
Net finance costs recognised in profit or loss	**16,544**	**27,742**

11. Income tax expense

The Group's applicable income tax rate is the income tax rate of 15% (2009: 15%) for Georgian companies.

'000 GEL	**2011**	**2010**
Current tax expense		
Current year	30,221	30,569
Over-provided in prior years	(14,704)	-
	15,517	30,569
Deferred tax expense		
Origination and reversal of temporary differences	(5,596)	(8,296)
	9,921	**22,273**

Reconciliation of effective tax rate:

	2011		**2010**	
	'000 GEL	**%**	**'000 GEL**	**%**
Profit before income tax	184,334	100	123,806	100
Income tax at applicable tax rate	27,650	15	18,571	15
(Net non-taxable income)/non-deductible expenses	(3,025)	(2)	3,702	3
Over-provided in prior years	(14,704)	(8)	-	-
	9,921	**5**	**22,273**	**18**

During 2011 the Group won a case in the Supreme Court of Georgia related to additional tax liabilities assessed by the Georgian Tax Authorities for the years 1998 to 2003, and accrued by the Group before 2007, of approximately GEL 13 million. The case was finalised in September 2011. The Georgian Tax Authorities recognised the decision of the Supreme Court of Georgia and the amount of the assessment, which had been paid by the Group, was recorded as a prepayment on the Group's tax card. The Group reversed the provision for the assessment and recognised a related current tax asset as at 31 December 2011.

12. Property, plant and equipment

'000 GEL	Land	Buildings and constructions	Rail track infrastructure	Transport, machinery, equipment and other	Construction in progress	Total
Cost or deemed cost						
Balance at 1 January 2010	481,217	138,563	681,676	591,249	108,647	2,001,352
Additions	36,818	281	461	21,413	87,291	146,264
Disposals	(4,779)	(1,863)	(6,142)	(5,637)	(2,924)	(21,345)
Transfers	5,175	1,678	28,776	22,738	(58,367)	-
Write offs	-	-	-	-	(4,831)	(4,831)
Balance at 31 December 2010	518,431	138,659	704,771	629,763	129,816	2,121,440
Balance at 1 January 2011	518,431	138,659	704,771	629,763	129,816	2,121,440
Additions	10,926	-	627	27,895	290,644	330,092
Disposals	(3,253)	(8,220)	(32,133)	(15,388)	(6,813)	(65,807)
Transfers	10,052	3,294	22,998	38,667	(75,011)	-
Write offs	-	-			(4,095)	(4,095)
Balance at 31 December 2011	536,156	133,733	696,263	680,937	334,541	2,381,630
Depreciation						
Balance at 1 January 2010	-	11,545	109,030	180,837	-	301,412
Depreciation for the year	-	4,539	40,840	53,342	-	98,721
Disposals		(384)	(1,347)	(2,595)		(4,326)
Balance at 31 December 2010	-	15,700	148,523	231,584	-	395,807
Balance at 1 January 2011	-	15,700	148,523	231,584	-	395,807
Depreciation for the year	-	4,263	36,158	51,582	-	92,003
Disposals	-	(1,190)	(11,270)	(6,915)	-	(19,375)
Balance at 31 December 2011	-	18,773	173,411	276,251	-	468,435
Carrying amounts						
At 1 January 2010	481,217	127,018	572,646	410,412	108,647	1,699,940
At 31 December 2010	**518,431**	**122,959**	**556,248**	**398,179**	**129,816**	**1,725,633**
At 31 December 2011	**536,156**	**114,960**	**522,853**	**404,685**	**334,541**	**1,913,195**

(a) Property, plant and equipment under construction

During the year ended 31 December 2010 the Group started two large capital projects: the Main Line Modernization and the Tbilisi Bypass and started to incur expenditures for the projects in September 2010 and November 2010 respectively. To partly finance the projects the Group issued unsecured bonds in 2010 (see note 19). All the borrowing costs of the unsecured bond allocated to each project on a 59%/41% basis were capitalized upon starting to incur expenditures for the projects. Capitalised borrowing costs related to the projects amounted to GEL 42,141 thousand (2010: GEL 10,388 thousand).

13. Other non-current assets

’000 GEL	**2011**	**2010**
Prepayments for non-current assets	157,694	102,810
Construction materials	71,991	33,333
VAT recoverable	45,000	-
Other	1,354	232
	276,039	**136,375**

14. Inventories

’000 GEL	**2011**	**2010**
Materials	20,838	14,569
Rails	3,559	4,884
Fuel	2,143	1,922
Other	2,184	1,810
	28,724	23,185
Allowance for inventory obsolescence	(4,987)	(5,193)
	23,737	**17,992**
Reversal of previous write-down of inventories	206	293

15. Trade and other receivables

’000 GEL	**2011**	**2010**
Trade receivables	105,363	95,131
Other receivables	1,787	4,172
	107,150	99,303
Impairment allowance on trade receivables	(79,795)	(72,390)
	27,355	**26,913**

The Group’s exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 24.

16. Prepayments and other current assets

’000 GEL	2011	2010
VAT recoverable	25,720	37,869
Prepaid taxes other than income tax	1,969	2,508
Advances paid to suppliers	25	2,266
Other current assets	-	22
	27,714	**42,665**

17. Cash and cash equivalents

’000 GEL	2011	2010
Current accounts	64,351	335,716
Petty cash	165	139
Cash and cash equivalents in the statement of financial position	**64,516**	**335,855**
Restricted cash	(2,963)	(11,912)
Cash and cash equivalents in the statement of cash flows	**61,553**	**323,943**

The Group’s exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities are disclosed in note 24.

18. Equity and liabilities to the owners

(a) Charter capital

Charter capital, which is not divided into shares, represents the nominal amount of capital in the founding documentation of the Company and is subject to state registration.

The owners of charter capital are entitled to receive dividends as declared from time to time and are entitled to the number of votes corresponding to the percentage of shareholding in the Company at meetings of the Company.

’000 GEL	2011	2010
Balance at 1 January	985,376	967,207
Contribution of cash and cash equivalents	20,000	-
Contribution of property, plant and equipment	8,133	22,423
Distribution of cash and cash equivalents	(1,528)	-
Transfer of retained earnings to charter capital	-	3,891
Withdrawal of property, plant and equipment	(11,518)	(8,145)
	1,000,463	**985,376**

(b) Non-cash owner contribution reserve

The difference between the nominal amount of registered charter capital for non-cash assets contributed by the owner and the fair value of the contributed assets is recognised in the non-cash owner contribution reserve.

Non-cash assets registered in the charter capital as future contributions by the owners but not yet registered under the ownership of the Group are recorded in the non-cash owner contribution reserve until the ownership registration is complete.

’000 GEL	**2011**	**2010**
Balance at 1 January	35,404	25,311
Fair value adjustment of non-cash owner contributions	2,639	10,093
	38,043	**35,404**

(c) Liabilities to owners

Liabilities to the owners represent liabilities in the form of property, plant and equipment which are withdrawn as a reduction in charter capital but not yet transferred formally to the owners. These liabilities are recorded at the carrying amount of assets to be transferred to the owner.

’000 GEL	**2011**	**2010**
Liabilities to owners	**13,188**	**29,241**

19. Loans and borrowings

This note provides information about the contractual terms of the Group’s interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group’s exposure to interest rate, foreign currency and liquidity risk, see note 24.

’000 GEL	**2011**	**2010**
Non-current liabilities		
Unsecured bank facility	36	-
Unsecured bond issue	414,027	438,383
Loans and borrowings	**414,063**	**438,383**
Current liabilities		
Unsecured bank facility	635	-
Current portion of unsecured bond issue	17,972	19,259
Loans and borrowings	**18,607**	**19,259**

Terms and debt repayment schedule

Terms and conditions of outstanding loans and borrowings were as follows:

				31 December 2011		31 December 2010	
’000 GEL	Currency	Nominal interest rate	Year of maturity	Face value	Carrying amount	Face value	Carrying amount
Unsecured bond issue	USD	9.9%	2015	414,028	431,999	443,200	457,642
Unsecured bank facility	GEL	11%	2012	635	635	-	-
Unsecured bank facility	USD	11.5%	2013	36	36	-	-
Total interest-bearing liabilities				**414,699**	**432,670**	**443,200**	**457,642**

In July 2010 the Group issued bonds with a face value of USD 250 million maturing in July 2015. The proceeds are to be used for the implementation of two capital projects: Main Line Modernization and the Tbilisi Bypass.

On 17 March 2010 a loan agreement was signed between the Group and the European Bank for Reconstruction and Development (“EBRD”), by which the EBRD agreed to lend the Group up to CHF 146.2 million partly to finance the Tbilisi Bypass project. No funds were drawn down under this facility. On 4 November 2011, following intensive negotiations with the EBRD the loan agreement executed between the Company and the EBRD was cancelled. Prepaid finance costs included in trade and other receivables related to this loan agreement of GEL 3,047 thousand were written off in 2011. The Group also paid a cancellation fee related to this loan of GEL 2,289 thousand in 2011, included in other expenses.

20. Trade and other payables

’000 GEL	2011	2010
Non-current liabilities		
Trade payables	45	45
	45	**45**
Current liabilities		
Trade payables	28,390	44,720
Advances received from customers	17,564	17,166
	45,954	**61,886**

The Group’s exposure to currency and liquidity risk related to trade and other payables is disclosed in note 24.

21. Deferred tax assets and liabilities

(a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
’000 GEL	**2011**	**2010**	**2011**	**2010**	**2011**	**2010**
Property, plant and equipment and investment property	-	-	(87,639)	(89,532)	(87,639)	(89,532)
Inventories	8,374	5,327	-	-	8,374	5,327
Trade and other receivables	11,826	10,740	-	-	11,826	10,740
Prepayments and other current assets	1,335	1,488	-	-	1,335	1,488
Other non-current assets	30	30	-	-	30	30
Other current liabilities	2,123	1,231	-	-	2,123	1,231
Provisions	3,041	3,239	-	-	3,041	3,239
Trade and other payables	-	956	(15)	-	(15)	956
Net tax assets/(liabilities)	**26,729**	**23,011**	**(87,654)**	**(89,532)**	**(60,925)**	**(66,521)**

(b) Movement in temporary differences during the year

’000 GEL	**1 January 2011**	**Recognised in profit or loss**	**31 December 2011**
Property, plant and equipment and investment property	(89,532)	1,893	(87,639)
Inventories	5,327	3,047	8,374
Trade and other receivables	10,740	1,086	11,826
Prepayments and other current assets	1,488	(153)	1,335
Other non-current assets	30	-	30
Other current liabilities	1,231	892	2,123
Provisions	3,239	(198)	3,041
Trade and other payables	956	(971)	(15)
	(66,521)	**5,596**	**(60,925)**

'000 GEL	**1 January 2010**	**Recognised in profit or loss**	**31 December 2010**
Property, plant and equipment and investment property	(93,586)	4,054	(89,532)
Inventories	5,613	(286)	5,327
Trade and other receivables	9,836	904	10,740
Prepayments and other current assets	2,261	(773)	1,488
Other non-current assets	146	(116)	30
Other current liabilities	-	1,231	1,231
Provisions	913	2,326	3,239
Trade and other payables	-	956	956
	(74,817)	**8,296**	**(66,521)**

22. Provisions

'000 GEL	**Guarantees**	**Other**	**Total**
Balance at 1 January	15,305	6,292	21,597
Provisions made during the year	(960)	(364)	(1,324)
Balance at 31 December	**14,345**	**5,928**	**20,273**

The provision for guarantees relates to the Group's guarantee of a third party's loan from a Georgian bank. In 2010 the Group recognised a provision for the guarantee as there were indications that the beneficiary of the guarantee will not be able to discharge its liabilities. The provision is based on the full amount of the loan. The Group expects to incur most of the liability over the next year.

23. Other taxes payable

'000 GEL	**2011**	**2010**
Property tax liabilities	25,255	17,076
Personal income tax payable	1,190	1,226
Other taxes payable	422	8,934
	26,867	**27,236**

24. Financial instruments and risk management

(a) Overview

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

Risk management framework

The Management Board has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

(b) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers.

(i) Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was as follows:

	Carrying amount	
’000 GEL	**2011**	**2010**
Cash and cash equivalents - 5 largest Georgian banks (not impaired or past due)	64,351	335,716
Bank deposits - 5 largest Georgian banks (not impaired or past due)	76,449	38,021
Trade receivables	25,568	22,741
Other receivables	1,787	4,172
	168,155	**400,650**

(ii) Trade and other receivables

The Group’s exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the demographics of the Group’s customer base, including the default risk of the industry and country, in which customers operate, as these factors may have an influence on credit risk, particularly in the currently deteriorating economic circumstances. Approximately 30% (2010: 30%) of the Group’s revenue is attributable to sales transactions with a single customer.

Credit risk is managed by requesting prepayments from freight and passenger transportation customers. Accordingly the Group’s trade receivables mainly consist of receivables from foreign railway companies. Credit risk related to receivables from foreign railway companies is managed through the monthly monitoring of receivable balances and requiring immediate repayment of a debt when the balance approaches specific limits set for each individual counterparty.

More than 90% of the Group’s foreign railway customers have been transacting with the Group for over four years, and losses have occurred infrequently. In monitoring customer credit risk, customers are grouped according to their credit characteristics, including aging profile, maturity and existence of previous financial difficulties.

No collateral in respect of trade and other receivables is generally required.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The main component of this allowance is a specific loss component that relates to individually significant exposures.

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	Carrying amount	
’000 GEL	**2011**	**2010**
CIS countries	18,695	14,223
Domestic	6,873	8,518
	25,568	**22,741**

The Group's five most significant customers account for GEL 22,134 thousand of the trade receivables carrying amount at 31 December 2011 (2010: GEL 12,857 thousand).

Impairment losses

The aging of trade receivables at the reporting date was:

'000 GEL	Gross 2011	Impairment 2011	Gross 2010	Impairment 2010
Not past due	-	-	-	-
Past due 0- 90 days	14,178	2,000	5,622	572
Past due 91-180 days	8,725	1,393	4,097	1,104
Past due 181-365 days	6,283	2,137	6,712	1,301
Past due more than one year	76,177	74,265	78,700	69,413
	105,363	**79,795**	**95,131**	**72,390**

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

'000 GEL	2011	2010
Balance at beginning of the year	72,390	66,337
Increase during the year	7,405	6,053
Balance at end of the year	**79,795**	**72,390**

Most of the impairment loss at 31 December 2011 relates to several customers that have indicated that they are not expecting to be able to pay their outstanding balances either because of economic circumstances or as a result of bankruptcy. The Group believes that the unimpaired amounts that are past due are still collectible, based on historic payment behaviour and analyses on the underlying customers' credit ratings, when available.

The allowance account in respect of trade receivables is used to record impairment losses until all possible opportunities for recovery have been exhausted; at that point the amounts are written off against the financial asset directly.

Based on historic default rates, the Group believes that, apart from the above, no impairment allowance is necessary in respect of trade receivables.

(iii) Cash and cash equivalents

To mitigate the credit risk of cash and bank balances, the Group holds its funds with the largest five Georgian banks. The Group does not expect any counterparty to fail to meet its obligations.

(c) Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of three months, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

The Group has significant contractual commitments to purchase property, plant and equipment (see note 26) for the Main Line Modernisation and Tbilisi Bypass projects expected to be completed by the end of 2016 and 2013 respectively. The proceeds from the bonds issued by the Group in July 2010 for the implementation of the two capital projects (see note 19) were substantially used as at 31 December 2011. Management believes that the Group will have sufficient cash flows from operating activities to finance these two projects. It is expected that the bonds will be redeemed from the proceeds of the sale of land made available as a result of the Tbilisi Bypass project.

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements.

2011

’000 GEL	Carrying amount	Contractual cash flows	0-6 months	6-12 months	1-2 years	2-5 years
Unsecured bond issues	431,999	582,517	20,617	20,618	41,236	500,046
Trade payables	28,435	28,435	21,659	6,731	45	-
Other current liabilities	14,424	14,424	14,424	-	-	-
Guarantees issued	14,345	14,345	14,345	-	-	-
	489,203	**639,721**	**71,045**	**27,349**	**41,281**	**500,046**

2010

’000 GEL	Carrying amount	Contractual cash flows	0-6 months	6-12 months	1-2 years	2-5 years
Unsecured bond issues	457,642	662,030	21,883	21,883	43,766	574,498
Trade payables	44,765	44,765	39,215	5,505	45	-
Other current liabilities	15,018	15,018	15,018	-	-	-
Guarantees issued	15,305	15,305	15,305	-	-	-
	532,730	**737,118**	**91,421**	**27,388**	**43,811**	**574,498**

(d) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group’s income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

(i) Currency risk

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than GEL. The currencies in which these transactions primarily are denominated are U.S. Dollars (USD) and Swiss Francs (CHF).

A majority of the Group’s revenue is denominated in CHF. The Group’s policy is to conclude significant purchase contracts in CHF to match the cash flows generated from operations.

Effective from 1 February 2012, the Group changed the basic currency of freight tariffs from CHF to USD. The Group is in the process of changing the significant purchase contracts to USD to match the cash flows generated from operations.

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows based on notional amounts:

'000 GEL	USD - denominated 2011	CHF - denominated 2011	USD- denominated 2010	CHF - denominated 2010
Cash and cash equivalents	26,143	24,180	14,979	312,535
Bank deposits	13,362	63,087	10,637	27,384
Trade receivables	633	19,049	84	14,139
Unsecured bank facility	(36)	-	-	-
Unsecured bond issue	(431,999)	-	(457,642)	-
Trade and other payables	(78)	(39)	(12,270)	-
Net exposure	**(391,975)**	**106,277**	**(444,212)**	**354,058**

The following significant exchange rates applied during the year:

in GEL	Average rate		Reporting date spot rate	
	2011	**2010**	**2011**	**2010**
USD 1	1.69	1.78	1.67	1.77
CHF 1	1.91	1.71	1.78	1.89

Sensitivity analysis

A strengthening of the GEL, as indicated below, against the following currencies at 31 December would have increased (decreased) profit or loss net of taxes by the amounts shown below. There would have been no impact directly on equity. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2010.

'000 GEL	Profit or loss
2011	
USD (10% strengthening)	33,318
CHF (10% strengthening)	(9,034)
2010	
USD (10% strengthening)	37,758
CHF (10% strengthening)	(30,095)

A weakening of the GEL against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

(ii) Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

Profile

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	Carrying amount	
'000 GEL	**2011**	**2010**
Fixed rate instruments		
Financial assets	76,449	38,021
Financial liabilities	(432,670)	(457,642)
	(356,221)	**(419,621)**

Bank deposits (included in financial assets above) have a maturity of up to fourteen months from the reporting date and bear annual interest of 12%.

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial assets and liabilities as fair value through profit or loss or as available for sale. Therefore a change in interest rates at the reporting date would not affect profit or loss or equity.

(e) Fair values versus carrying amount

Management believes that the fair value of the Group's financial assets and liabilities approximates their carrying amounts.

The basis for determining fair values is disclosed in note 5.

(f) Capital management

The Group has no formal policy for capital management but management seeks to maintain a sufficient capital base for meeting the Group's operational and strategic needs, and to maintain confidence of market participants. This is achieved with efficient cash management, constant monitoring of the Group's revenues and profit, and long-term investment plans mainly financed by the Group's operating cash flows. With these measures the Group aims for steady profits growth.

The Group's debt to capital ratio at the end of the reporting period was as follows:

'000 GEL	**2011**	**2010**
Total liabilities	614,346	700,339
Less: cash and cash equivalents	(61,553)	(323,943)
Net debt	**552,793**	**376,396**
Total equity	**1,802,008**	**1,633,041**
Debt to capital ratio at 31 December	0.31	0.23

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

25. Operating leases

Non-cancellable operating lease rentals are receivable as follows:

'000 GEL	**2011**	**2010**
Less than one year	2,284	1,939
Between one and five years	8,601	7,468
More than five years	64,795	60,872
	75,680	**70,279**

Operating leases mainly relate to investment property owned by the Group with lease terms of between 10 to 50 years, as well as the rental of other buildings, containers, locomotives and fittings. Lessees do not have an option to purchase the property at the end of the lease term.

26. Capital commitments

As at 31 December 2011 the Group had entered into contracts for construction works and the purchase of plant and equipment for GEL 961,014 thousand mainly relating to the Main Line Modernisation and Tbilisi Bypass projects (2010: GEL 653,370 thousand). Included in capital commitments are contracts for the construction of a building in the west of Georgia for future sale or lease for USD 22,345 thousand.

27. Contingencies

(a) Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group's operations and financial position.

(b) Taxation contingencies

The taxation system in Georgia is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes unclear, contradictory and subject to varying interpretation. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by the tax authorities after six years have passed since the end of the year in which the breach occurred.

These circumstances may create tax risks in Georgia that are more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Georgian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

(c) Litigation

In the ordinary course of business, the Group is subject to legal actions, litigations and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations.

28. Related party transactions

(a) Control relationships

The Company was wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economy and Sustainable Development of Georgia as at 30 September 2011. On 25 October 2011 24% of the Company's charter capital was transferred to Partnership Fund JSC which is wholly owned by the State of Georgia.

(b) Tansactions with key management personnel

(i) Key management remuneration

Key management received the following remuneration during the year, which is included in payroll expenses:

'000 GEL	**2011**	**2010**
Salaries and bonuses	**1,181**	**950**

(c) Other related party transactions

(i) Transactions with the government

The Group transacts in its daily operations with a number of entities that are either controlled, jointly controlled or under significant influence by the Government of Georgia. The Group has opted to apply the exemption in IAS 24 *Related Party Disclosures* that allows the presentation of reduced related party disclosures regarding transactions with government-related entities.

The Group's other related party transactions are disclosed below.

(ii) Revenue, purchases and expenses

The Group purchases most of its electricity from a State-owned operator which amounted to GEL 13,885 thousand for the year ended 31 December 2011 (year ended 31 December 2010: GEL 16,476 thousand). The Group also purchases security services from a state agency which amounted to GEL 7,631 thousand for the year ended 31 December 2011 (year ended 31 December 2010: GEL 7,550 thousand). The Group usually does not have significant balances for these purchases.

Management estimates that the aggregate amounts of other income and expenses and the related balances with other Government-related entities are not significant.

29. Significant subsidiaries

Subsidiary	Country of incorporation	Principal activities	2011 Ownership/ voting	2010 Ownership/ voting
Georgian Railway Property Management LLC	Georgia	Property management and development	100%	100%
Georgian Railway Transcontainer LLC	Georgia	Container transportation	100%	100%
Georgian Railway Construction JSC	Georgia	Construction and other projects	100%	100%
Borjomi Bakuriani Railway LLC	Georgia	Passenger transportation	100%	100%

Georgian Railway LLC

Consolidated Financial Statements for the year ended 31 December 2010

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Independent Auditors' Report

To the Management Board
Georgian Railway LLC

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

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

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

Tbilisi Branch of KPMG CIS Limited

KPMG CIS TBILISI BRANCH 204428140

Tbilisi Branch of KPMG CIS Limited
13 May 2011

’000 GEL	Note	2010	2009
ASSETS			
Non-current assets			
Property, plant and equipment	11	1,725,633	1,699,940
Investment property		9,926	9,926
Other non-current assets	12	136,375	12,817
Total non-current assets		**1,871,934**	**1,722,683**
Current assets			
Inventories	13	17,992	23,725
Current tax assets		-	4,615
Trade and other receivables	14	26,913	22,194
Prepayments and other current assets	15	42,665	35,061
Cash and cash equivalents	16	335,855	1,361
Bank deposits		38,021	-
Total current assets		**461,446**	**86,956**
Total assets		**2,333,380**	**1,809,639**
EQUITY AND LIABILITIES			
Equity	17		
Charter capital		985,376	967,207
Non-cash owner contribution reserve		35,404	25,311
Retained earnings		612,261	556,165
Total equity		**1,633,041**	**1,548,683**
Non-current liabilities			
Loans and borrowings	18	438,383	24,900
Trade and other payables	19	45	28,853
Deferred tax liabilities	21	66,521	74,817
Total non-current liabilities		**504,949**	**128,570**
Current liabilities			
Loans and borrowings	18	19,259	3,855
Trade and other payables	19	61,886	66,035
Liabilities to owners	17	29,241	26,636
Provisions	20	21,597	6,088
Other taxes payable	22	27,236	21,794
Other current liabilities		15,018	7,978
Current tax liabilities		21,153	-
Total current liabilities		**195,390**	**132,386**
Total liabilities		**700,339**	**260,956**
Total equity and liabilities		**2,333,380**	**1,809,639**

The consolidated statement of financial position is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 39.

'000 GEL	Note	2010	2009
Revenue	6	404,687	318,838
Other income		17,818	10,678
Employee benefits expense		(111,257)	(106,113)
Depreciation and amortization expense		(98,749)	(96,111)
Electricity and materials used	7	(44,620)	(40,315)
Other expenses	8	(71,815)	(64,139)
Results from operating activities		**96,064**	**22,838**
Finance income	9	45,411	610
Finance costs	9	(17,669)	(4,771)
Net finance income/(costs)		**27,742**	**(4,161)**
Profit before income tax		**123,806**	**18,677**
Income tax expense	10	(22,273)	(2,869)
Profit and total comprehensive income for the year		**101,533**	**15,808**

These consolidated financial statements were approved by the Management Board on 13 May 2011 and were signed on its behalf by:

Irakli Ezugbaia
General Director

Amiran Tevzadze
Acting Chief Accountant

The consolidated statement of comprehensive income is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 39.

’000 GEL	Charter capital	Non-cash owner contribution reserve	Retained earnings	Total equity
Balance at 1 January 2009	933,635	33,752	576,357	1,543,744
Profit and total comprehensive income for the year	-	-	15,808	15,808
Transactions with owners, recorded directly in equity				
Non-cash contributions by and distributions to owners, net (see note 17)	33,572	(8,441)	-	25,131
Dividends to owners	-	-	(36,000)	(36,000)
Total contributions by and distributions to owners	33,572	(8,441)	(36,000)	(10,869)
Balance at 31 December 2009	**967,207**	**25,311**	**556,165**	**1,548,683**
Balance at 1 January 2010	967,207	25,311	556,165	1,548,683
Total comprehensive income for the year				
Profit and total comprehensive income for the year	-	-	101,533	101,533
Transactions with owners, recorded directly in equity				
Dividends to owners	-	-	(36,000)	(36,000)
Net non-cash contributions by and distributions to owners, net (see note 17)	14,278	10,093	(5,546)	18,825
Transfer of retain earnings to charter capital (see note 17)	3,891	-	(3,891)	-
Total contributions by and distributions to owners	18,169	10,093	(45,437)	(17,175)
Balance at 31 December 2010	**985,376**	**35,404**	**612,261**	**1,633,041**

The consolidated statement of changes in equity is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 39.

'000 GEL	Note	2010	2009
Cash flows from operating activities			
Cash receipts from customers		433,749	336,695
Cash paid to suppliers and employees		(195,162)	(200,350)
Cash flows from operations before income taxes and interest paid		**238,587**	**136,345**
Income tax paid		(4,923)	(18,043)
Interest paid		(2,163)	(1,604)
Net cash from operating activities		**231,501**	**116,698**
Cash flows from investing activities			
Acquisition of property, plant and equipment		(281,738)	(89,976)
Proceeds from sale of investments		6,300	-
Increase in term deposits		(38,021)	-
Increase in restricted cash		(11,912)	-
Interest received		3,350	622
Net cash used in investing activities		**(322,021)**	**(89,354)**
Cash flows from financing activities			
Proceeds from borrowings		455,109	27,900
Repayment of borrowings		(28,975)	(21,146)
Dividends paid		(36,000)	(36,000)
Net cash from/(used) in financing activities		**390,134**	**(29,246)**
Net increase/(decrease) in cash and cash equivalents		**299,614**	**(1,902)**
Cash and cash equivalents at 1 January		1,361	3,196
Effect of exchange rate fluctuations on cash and cash equivalents		22,968	67
Cash and cash equivalents at 31 December	**16**	**323,943**	**1,361**

The consolidated statement of cash flows is to be read in conjunction with the notes to, and forming part of, the consolidated financial statements set out on pages 8 to 39.

1 Background

(a) Business environment

Georgian business environment

The Group's operations are primarily located in Georgia. Consequently, the Group is exposed to the economic and financial markets of Georgia which display characteristics of an emerging market. The conflict between Georgia and the Russian Federation has created additional uncertainty in the environment. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in Georgia. The consolidated financial statements reflect management's assessment of the impact of the Georgian business environment on the operations and the financial position of the Group. The future business environment may differ from management's assessment.

(b) Organisation and operations

Georgian Railway LLC (the "Company") and its subsidiaries (the "Group") comprise Georgian limited liability companies as defined in the Civil Code of Georgia. The Company was established as a state-owned enterprise in December 1998 by the Decree of President of Georgia # 929 as an entity engaged in the provision of railway transportation services in Georgia.

The Company's registered office is 15 Queen Tamar Avenue, Tbilisi 0112, Georgia.

The Group's principal activity is the operation of a nationwide railway system providing freight and passenger transportation services, maintenance and development of railway infrastructure and construction of railway lines within Georgia.

The Group is wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economic Development of Georgia. Related party transactions are disclosed in note 27.

2 Basis of preparation

(a) Statement of compliance

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

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that property, plant and equipment was revalued to determine deemed cost as part of the adoption of IFRSs.

(c) Functional and presentation currency

The national currency of Georgia is the Georgian Lari ("GEL"), which is the Company's functional currency and the currency in which these consolidated financial statements are presented. All financial information presented in GEL has been rounded to the nearest thousand.

(d) Use of estimates and judgments

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about critical judgements in applying accounting policies that have a significant effect on the amounts recognised in the consolidated financial statements is included in the following notes:

- Note 3(d) – useful lives of property, plant and equipment
- Note 23(b) – impairment allowances for trade and other receivables

In the opinion of management, there are no assumptions or estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities.

(a) Basis of consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

(ii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(b) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period.

Non-monetary items in a foreign currency that are measured in terms of historical cost are translated using the exchange rate at the date of the transaction. Foreign currency differences arising in retranslation are recognised in profit or loss.

(c) Non-derivative financial instruments

Non-derivative financial instruments comprise trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

(i) Non-derivative financial assets

The Group initially recognises loans and receivables on the date that they are originated. All other financial assets are recognised initially on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Group classifies non-derivative financial assets into the following category: loans and receivables.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables category comprise the following classes of assets: trade and other receivables as presented in note 14 and cash and bank balances as presented in note 16.

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with original maturities of three months or less. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(ii) Non-derivative financial liabilities

The Group initially recognises financial liabilities on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Group classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortised cost using the effective interest method. Other financial liabilities comprise loans and borrowings and trade and other payables.

(iii) Charter capital

Charter capital is classified as equity.

Reduction of charter capital

Charter capital reductions and non-cash distributions are recognised at the carrying amount of the assets distributed at the date of the distribution where the asset is ultimately controlled by the same parties both before and after the distribution.

Increase of charter capital

When charter capital is increased, any difference between the registered amount of charter capital and the fair value of the assets contributed is recognised as a separate component of equity as non-cash owner contribution reserve.

(d) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment, are measured at cost less accumulated depreciation and impairment losses. Items of property, plant and equipment contributed by the shareholder are initially measured at fair value. The cost of property, plant and equipment at 1 January 2007, the date of transition to IFRSs, was determined by reference to its fair value at that date.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

The gain or loss on disposal of an item of property, plant and equipment is determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and is recognised net within other income/other expenses in profit or loss.

(ii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

Maintenance and repair expenses are recognised as follows:

- Rolling stock:

− current maintenance expenses during the useful life of equipment (repair work and replacement of unusable and missing parts) are recognised as operating expenses in profit or loss as incurred;
− expenses under multi-year major overhaul programmes are capitalised as a separate overhaul component and depreciated separately from the main asset;
− overhauls performed near the end of the useful life of an asset, together with refurbishment, are capitalised when they extend the useful life of the underlying asset.

- Fixed installations:

− current maintenance and repair expenses (technical inspections, maintenance contracts, etc.) are recognised as operating expenses in profit or loss as incurred;
− labour, materials and other costs (associated with the installation of rails, sleepers and ballast) under multi-year major building or infrastructure maintenance programmes are capitalised through the partial or total replacement of each component concerned;
− costs associated with infrastructure improvements are capitalized to the extent that they increase the functionality (traffic working speed) of the asset.

(iii) Depreciation

Depreciation is based on the cost of an asset less its residual value. Significant components of individual assets are assessed and if a component has a useful life that is different from the remainder of that asset, that component is depreciated separately.

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment, since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Land is not depreciated.

The estimated useful lives for the current and comparative periods are as follows:

• buildings and constructions	44 years
• rail track infrastructure	23 years
• transport, machinery, equipment and other	12 years

Depreciation methods and useful lives are reviewed at each financial year end and adjusted if appropriate.

(e) Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first-in first-out principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(f) Impairment

(i) Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include default or delinquency by a debtor, restructuring of an amount due to the Group on terms that the Group would not consider otherwise, indications that a debtor will enter bankruptcy, adverse changes in the payment status of borrowers in the Group or economic conditions that correlate with defaults.

The Group considers evidence of impairment for loans and receivables at both a specific asset and collective level. All individually significant loans and receivables are assessed for specific impairment. All individually significant receivables found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables that are not individually significant are collectively assessed for impairment by grouping together loans and receivables with similar risk characteristics.

In assessing collective impairment the Group uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset or its related cash-generating unit (CGU) exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets or CGU.

The Group's corporate assets do not generate separate cash inflows and are utilised by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of CGUs are allocated to reduce the carrying amount of assets in the CGU (group of CGUs) on a pro rata basis.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(g) Employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee, and the obligation can be estimated reliably.

(h) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. A financial guarantee liability is recognised initially at fair value net of associated transaction costs, and is measured subsequently at the higher of the amount initially recognised less cumulative amortisation or the amount of provision for losses under the guarantee. Provisions for losses under financial guarantees are recognised when losses are considered probable and can be measured reliably.

(i) Revenue

(i) Transportation activities

Revenue from feight and passenger transportation is measured at the fair value of the consideration received or receivable. Freight and passenger transportation revenue is recognized in profit or loss according to the percentage of completed service method based on transit time of freight and passengers moving from the original location to the final destination.

Revenue from services rendered in stations is recognised in profit or loss when the service is rendered.

(ii) Rental income

Rental income from investment property or other assets rented is recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

(j) Other expenses

(i) Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

(ii) Social expenditure

To the extent that the Group's contributions to social programs benefit the community at large and are not restricted to the Group's employees, they are recognised in profit or loss as incurred.

(k) Finance income and costs

Finance income comprises interest income on funds invested and foreign currency gains. Interest income is recognised as it accrues in profit or loss, using the effective interest method.

Finance costs comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses and impairment losses recognised on financial assets.

Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in profit or loss using the effective interest method.

Foreign currency gains and losses are reported on a net basis as either finance income or finance cost depending on whether foreign currency movements are in a net gain or net loss position.

(l) Income tax

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

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

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; and
- temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(m) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are reviewed regularly by the Group's Management Board to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available.

Segment results that are reported to the Management Board include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly railway infrastructure, corporate assets (primarily the Group's headquarters), head office expenses, financial income and expenses, tax expenses and tax assets and liabilities. Items related to infrastructure are not allocated as the Group has not implemented systems for such allocations.

Segment capital expenditure is the total cost incurred during the year to acquire property, plant and equipment and intangible assets other than goodwill.

(n) New Standards and Interpretations not yet adopted

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2010, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the Group's operations. The Group plans to adopt these pronouncements when they become effective.

- Revised IAS 24 *Related Party Disclosures (2010)* introduces an exemption from the basic disclosure requirements in relation to related party disclosures and outstanding balances, including commitments, for government-related entities. Additionally, the standard has been revised to simplify some of the presentation guidance that was previously non-reciprocal. The revised standard is to be applied retrospectively for annual periods beginning on or after 1 January 2011. The Group has not yet determined the potential effect of the amendment.

- IFRS 9 *Financial Instruments* will be effective for annual periods beginning on or after 1 January 2013. The new standard is to be issued in phases and is intended ultimately to replace International Financial Reporting Standard IAS 39 *Financial Instruments: Recognition and Measurement*. The first phase of IFRS 9 was issued in November 2009 and relates to the classification and measurement of financial assets. The second phase regarding classification and measurement of financial liabilities was published in October 2010. The remaining parts of the standard are expected to be issued during the first half of 2011. The Group recognises that the new standard introduces many changes to the accounting for financial instruments and is likely to have a significant impact on Group’s consolidated financial statements. The impact of these changes will be analysed during the course of the project as further phases of the standard are issued. The Group does not intend to adopt this standard early.

- Various *Improvements to IFRSs* have been dealt with on a standard-by-standard basis. All amendments, which result in accounting changes for presentation, recognition or measurement purposes, will come into effect not earlier than 1 January 2011. The Group has not yet analysed the likely impact of the improvements on its financial position or performance.

4 Determination of fair values

A number of the Group’s accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and for disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant and equipment

The fair value of property, plant and equipment contributed by the shareholder is based on the market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm’s length transaction after proper marketing wherein the parties had each acted knowledgeably and willingly. The fair value of items of plant, equipment, fixtures and fittings is based on market approach and cost approach using quoted market prices for similar items when available.

When no quoted market prices are available, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

(b) Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes.

(c) Financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

5 Operating segments

The Group has two reportable segments, as described below, which are the Group's strategic business units. The strategic business units offer different products and services, and are managed separately because they require different technology and marketing strategies. For each of the strategic business units, the Group's Management Board reviews internal management reports on at least a quarterly basis. The following summary describes the operations in each of the Group's reportable segments:

- *Freight transportation*. Includes transportation of goods and commodities and related services.
- *Passenger transportation*. Includes transportation of passengers and luggage.

Other operations include provision of internet services, leasing of fibre-optic and other cable and telephone services. None of these segments meets any of the quantitative thresholds for determining reportable segments in 2010 or 2009.

There are no inter-segment charges.

Information regarding the results of each reportable segment is included below. Performance is measured based on segment profit before infrastructure costs, central over heads, interest and income tax, as included in the internal management reports that are reviewed by the Group's Management Board. Segment profit is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate within these industries.

(i) Information about reportable segments

	Freight transportation		**Passenger transportation**		**Total**	
'000 GEL	**2010**	**2009**	**2010**	**2009**	**2010**	**2009**
External revenues	377,868	291,334	17,343	15,560	395,211	306,894
Depreciation and amortization	(39,522)	(40,033)	(7,840)	(8,387)	(47,362)	(48,420)
Reportable segment profit/(loss) before infrastructure costs, net interest cost and income tax	237,419	155,408	(10,798)	(13,001)	226,621	142,407
Reportable segment assets	340,474	379,167	90,126	98,895	430,600	478,062
Capital expenditure and other additions to non-current assets	20,722	89,860	20,976	12,011	41,698	101,871

(ii) Reconciliations of reportable segment revenues, profit or loss, assets and other material items

’000 GEL	2010	2009
Revenues		
Total revenue for reportable segments	395,211	306,894
Other revenue	9,476	11,944
Consolidated revenue	**404,687**	**318,838**
Profit or loss		
Total profit or loss for reportable segments	226,621	142,407
Other profit or loss	(537)	614
Payroll expenses – infrastructure and headquarters	(48,920)	(45,411)
Depreciation expenses – infrastructure and headquarters	(51,116)	(47,040)
Net finance income/(costs)	27,742	(4,161)
Other net unallocated expenses	(29,984)	(27,732)
Consolidated profit before income tax	**123,806**	**18,677**
Assets		
Total assets for reportable segments	430,600	478,062
Other assets	-	8,494
Property, plant and equipment - infrastructure and headquarters	1,365,672	1,221,911
Other unallocated assets, principally cash	537,108	101,172
Consolidated total assets	**2,333,380**	**1,809,639**

(iii) Other material items 2010

’000 GEL	Reportable segment totals	Infrastructure and headquarters	Other	Consolidated totals
Capital expenditure and other additions to non-current assets	41,698	231,122	-	272,820
Depreciation and amortization	47,362	51,116	271	98,749

(iv) Other material items 2009

’000 GEL	Reportable segment totals	Infrastructure and headquarters	Other	Consolidated totals
Capital expenditure and other additions to non-current assets	101,871	61,550	2,285	165,706
Depreciation and amortization	48,420	47,040	651	96,111

(v) Geographical information

Substantially all of the Group’s revenue is from and the non-current assets of the Group are located in Georgia.

(vi) Major customer

In 2010 one customer of the Group's freight transportation segment represented approximately 30% of the Group's total revenue (GEL 119,684 thousand). In 2009 two customers of the Group's freight transportation segment represented approximately 35% of the Group's total revenue (GEL 69,399 thousand and GEL 42,079 thousand).

6 Revenue

'000 GEL	**2010**	**2009**
Freight traffic	354,583	274,150
Freight car rental	23,285	16,543
Passenger traffic	14,685	13,952
Communication services	4,413	10,462
Other	7,721	3,731
	404,687	**318,838**

Railroad transportation in Georgia is a natural monopoly; however the prices are not subject to government regulation. According to clause 64 of the Railway Code of Georgia, which came into force on 1 July 2005, the Government of Georgia allowed the Group to set the prices for all services provided, including freight transportation, freight transportation-related additional services, and passenger and luggage transportation.

Tariffs for freight transportation are based on the International Rail Transit Tariff. The Group is a co-signatory of the Tariff Agreement together with CIS countries, Latvia, Lithuania and Estonia. The parties to the Agreement hold annual conferences to determine the tariff policy for the following year: each party declares tariffs denominated in Swiss Francs for railway transportation and states the general rules that apply to and modify tariffs. The agreed tariffs indicate the maximum level of tariffs applicable.

7 Electricity and materials used

'000 GEL	**2010**	**2009**
Electricity	21,386	19,311
Materials	13,565	13,345
Fuel	9,669	7,659
	44,620	**40,315**

8 Other expenses

’000 GEL	**2010**	**2009**
Taxes other than income tax	16,277	16,591
Guarantee provisions (see note 20)	15,509	-
Freight car rental	9,046	6,378
Security	7,650	6,541
Repairs and maintenance	5,009	9,176
Write off of non-current assets	4,831	6,622
Communication services	3,611	7,116
Inventory write-downs due to obsolescence	-	2,668
Other	9,882	9,047
	71,815	**64,139**

9 Finance income and finance costs

’000 GEL	**2010**	**2009**
Recognised in profit or loss		
Interest income	3,229	610
Net foreign exchange gain	42,182	-
Finance income	**45,411**	**610**
Impairment loss on trade receivables	(6,053)	(3,235)
Interest expense on financial liabilities	(11,616)	(1,525)
Net foreign exchange loss	-	(11)
Finance costs	(17,669)	(4,771)
Net finance costs recognised in profit or loss	**27,742**	**(4,161)**

10 Income tax expense

The Group's applicable income tax rate is the income tax rate of 15% (2009: 15%) for Georgian companies.

'000 GEL	**2010**	**2009**
Current tax expense		
Current year	30,569	9,835
Deferred tax expense		
Origination and reversal of temporary differences	(8,296)	(6,966)
	22,273	**2,869**

Reconciliation of effective tax rate:

	2010		**2009**	
	'000 GEL	**%**	**'000 GEL**	**%**
Profit before income tax	123,806	100	18,677	100
Income tax at applicable tax rate	18,571	15	2,802	15
Net non-deductible expenses	3,702	3	67	-
	22,273	**18**	**2,869**	**15**

11 Property, plant and equipment

'000 GEL	Land	Buildings and constructions	Rail track infrastructure	Transport, machinery, equipment and other	Construction in progress	Total
Cost or deemed cost						
Balance at 1 January 2009	454,813	136,144	661,010	486,395	102,461	1,840,823
Additions	27,144	656	107	105,249	32,550	165,706
Disposals	(740)	(4)	-	(1,172)	-	(1,916)
Transfers	-	1,767	20,559	777	(23,103)	-
Write offs	-	-	-	-	(3,261)	(3,261)
Balance at 31 December 2009	481,217	138,563	681,676	591,249	108,647	2,001,352
Balance at 1 January 2010	481,217	138,563	681,676	591,249	108,647	2,001,352
Additions	36,818	281	461	21,413	87,291	146,264
Disposals	(4,779)	(1,863)	(6,142)	(5,637)	(2,924)	(21,345)
Transfers	5,175	1,678	28,776	22,738	(58,367)	-
Write offs	-	-	-	-	(4,831)	(4,831)
Balance at 31 December 2010	518,431	138,659	704,771	629,763	129,816	2,121,440
Depreciation						
Balance at 1 January 2009	-	7,549	72,875	124,917	-	205,341
Depreciation for the year	-	3,996	36,155	55,920	-	96,071
Balance at 31 December 2009	-	11,545	109,030	180,837	-	301,412
Balance at 1 January 2010	-	11,545	109,030	180,837	-	301,412
Depreciation for the year	-	4,539	40,840	53,342	-	98,721
Disposals	-	(384)	(1,347)	(2,595)	-	(4,326)
Balance at 31 December 2010	-	15,700	148,523	231,584	-	395,807
Carrying amounts						
At 1 January 2009	454,813	128,595	588,135	361,478	102,461	1,635,482
At 31 December 2009	481,217	127,018	572,646	410,412	108,647	1,699,940
At 31 December 2010	**518,431**	**122,959**	**556,248**	**398,179**	**129,816**	**1,725,633**

(a) Impairment assessment

At 31 December 2009, following the decline in the volume of freight transported, the Group determined that there was an indication of impairment of its property, plant and equipment. The Group estimated the recoverable amount of the property, plant and equipment based on its value in use. The estimated recoverable amount did not result in an impairment loss being recognized. Management has assessed that there are no impairment indications as at 31 December 2010.

(b) Property, plant and equipment under construction

During the year ended 31 December 2010 the Group started two large capital projects: the Main Line Modernization and Tbilisi Bypass and started to incur expenditures for the projects in September 2010 and November 2010 respectively. To partly finance the projects the Group issued unsecured bonds in 2010 (see note 18). All the borrowing costs of the unsecured bond allocated to each project on a 59%/41% basis were capitalized upon starting to incur expenditures for the projects. Capitalised borrowing costs related to the projects amounted to GEL 10,388 thousand (2009: nil).

12 Other non-current assets

’000 GEL	**2010**	**2009**
Prepayments for non-current assets	102,810	9,585
Construction materials	33,333	-
Other	232	3,232
	136,375	**12,817**

13 Inventories

’000 GEL	**2010**	**2009**
Materials	14,569	17,365
Rails	4,884	6,528
Fuel	1,922	3,215
Other	1,810	2,103
	23,185	29,211
Allowance for inventory obsolescence	(5,193)	(5,486)
	17,992	**23,725**

14 Trade and other receivables

’000 GEL	**2010**	**2009**
Trade receivables	95,131	87,307
Other receivables	4,172	1,224
	99,303	88,531
Impairment allowance on trade receivables	(72,390)	(66,337)
	26,913	**22,194**

The Group’s exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 23.

15 Prepayments and other current assets

'000 GEL	**2010**	**2009**
VAT recoverable	37,869	31,448
Prepaid taxes other than income tax	2,508	2,600
Advances paid to suppliers	2,266	1,001
Other current assets	22	12
	42,665	**35,061**

16 Cash and cash equivalents

'000 GEL	**2010**	**2009**
Current accounts	335,716	1,264
Petty cash	139	97
Cash and cash equivalents in the statement of financial position	**335,855**	**1,361**
Restricted cash	(11,912)	-
Cash and cash equivalents in the statement of cash flows	**323,943**	**1,361**

The Group holds GEL 141,330 thousand (2009: nil) in an escrow account included in current accounts based on a loan agreement according to which the cash can be used by the Group only after consent by the lender and for the Tbilisi Bypass project (see note 11). No funds were drawn down under the loan agreement as at the reporting date.

17 Equity and liabilities to the owners

(a) Charter capital

Charter capital represents the nominal amount of capital in the founding documentation of the Company and is subject to state registration.

The owners of charter capital are entitled to receive dividends as declared from time to time and are entitled to the number of votes corresponding to the percentage of shareholding in the Company at meetings of the Company.

'000 GEL	**2010**	**2009**
Balance at 1 January	967,207	933,635
Contribution of property, plant and equipment	22,423	35,843
Transfer of retained earnings to charter capital	3,891	-
Withdrawal of property, plant and equipment	(8,145)	(2,271)
	985,376	**967,207**

(b) Non-cash owner contribution reserve

The difference between the nominal amount of registered charter capital for non-cash assets contributed by the shareholder and the fair value of the contributed assets is recognised in the non-cash owner contribution reserve.

Non-cash assets registered in the charter capital as future contributions by the shareholder but not yet registered under the ownership of the Group are recorded in the non-cash owner contribution reserve until the ownership registration is complete.

’000 GEL	**2010**	**2009**
Balance at 1 January	25,311	33,752
Fair value adjustment of non-cash owner contributions	10,093	18,686
Contribution of property, plant and equipment not registered under the ownership of the Group	-	(27,127)
	35,404	**25,311**

(c) Liabilities to the owners

Liabilities to the owners represent liabilities in the form of property, plant and equipment which are withdrawn as a reduction in charter capital but not yet transferred formally to the shareholder. These liabilities are recorded at the carrying amount of assets to be transferred to the shareholder.

(d) Dividends

In accordance with Georgian legislation the Company’s distributable reserves are limited to the balance of retained earnings as recorded in the Company’s statutory financial statements prepared in accordance with IFRSs. As at 31 December 2010 the Company had retained earnings, including the profit for the current year, of GEL 591,670 thousand (2009: GEL 552,872 thousand).

18 Loans and borrowings

This note provides information about the contractual terms of the Group’s interest-bearing loans and borrowings, which are measured at amortised cost. For more information about the Group’s exposure to interest rate, foreign currency and liquidity risk, see note 23.

’000 GEL	**2010**	**2009**
Non-current liabilities		
Unsecured bond issue	438,383	24,900
	438,383	**24,900**
Current liabilities		
Unsecured bank loans	-	3,773
Unsecured bond issue	19,259	82
	19,259	**3,855**

Terms and debt repayment schedule

Terms and conditions of outstanding loans and borrowings were as follows:

				31 December 2010		31 December 2009	
'000 GEL	**Currency**	**Nominal interest rate**	**Year of maturity**	**Face value**	**Carrying amount**	**Face value**	**Carrying amount**
Unsecured bond issue	USD	9.9%	2015	443,200	457,642	-	-
Unsecured bond issue	GEL	13.5%	2011	-	-	24,982	24,982
Unsecured bank facility	USD	Libor+1%	2010	-	-	3,773	3,773
Total interest-bearing liabilities				**443,200**	**457,642**	**28,755**	**28,755**

In July 2010 the Group issued bonds with a face value of USD 250 million maturing in July 2015. The proceeds are to be used for the implementation of two capital projects: Main Line Modernization and the Tbilisi Bypass.

On 17 March 2010 a loan agreement was signed between the Group and the European Bank for Reconstruction and Development ("EBRD"), by which EBRD agreed to lend the Group up to CHF 146.2 million to partly finance the Tbilisi Bypass project. No funds have been drawn down under this facility as at the reporting date or as at the date of issue of these consolidated financial statements.

19 Trade and other payables

'000 GEL	**2010**	**2009**
Non-current liabilities		
Trade payables	45	28,853
	45	**28,853**
Current liabilities		
Trade payables	44,720	56,540
Advances received from customers	17,166	9,495
	61,886	**66,035**

The Group's exposure to currency and liquidity risk related to trade and other payables is disclosed in note 23.

20 Provisions

’000 GEL	**Guarantees**	**Other**	**Total**
Balance at 1 January	-	6,088	6,088
Provisions made during the year	15,305	204	15,509
Balance at 31 December	15,305	6,292	21,597

The provision for guarantees relates to a guarantee by the Group to a party for the repayment of a loan to a Georgian bank. In 2010 the Group recognised a provision for the guarantee as there were indications that the beneficiary of the guarantee will not be able to discharge its liabilities. The provision is based on the full amount of the loan. The Group expects to incur most of the liability over the next 2 years.

21 Deferred tax assets and liabilities

(a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		**Liabilities**		**Net**	
’000 GEL	**2010**	**2009**	**2010**	**2009**	**2010**	**2009**
Property, plant and equipment and investment property	-	-	(89,532)	(93,586)	(89,532)	(93,586)
Inventories	5,327	5,613	-	-	5,327	5,613
Trade and other receivables	10,740	9,836	-	-	10,740	9,836
Prepayments and other current assets	1,488	2,261	-	-	1,488	2,261
Other non-current assets	30	146	-	-	30	146
Other current liabilities	1,231	-	-	-	1,231	-
Provisions	3,239	913	-	-	3,239	913
Trade and other payables	956	-	-	-	956	-
Net tax assets/(liabilities)	**23,011**	**18,769**	**(89,532)**	**(93,586)**	**(66,521)**	**(74,817)**

(b) Movement in temporary differences during the year

'000 GEL	1 January 2010	Recognised in profit or loss	31 December 2010
Property, plant and equipment and investment property	(93,586)	4,054	(89,532)
Inventories	5,613	(286)	5,327
Trade and other receivables	9,836	904	10,740
Prepayments and other current assets	2,261	(773)	1,488
Other non-current assets	146	(116)	30
Other current liabilities	-	1,231	1,231
Provisions	913	2,326	3,239
Trade and other payables	-	956	956
	(74,817)	**8,296**	**(66,521)**

'000 GEL	1 January 2009	Recognised in profit or loss	31 December 2009
Property, plant and equipment and investment property	(99,046)	5,460	(93,586)
Inventories	4,350	1,263	5,613
Trade and other receivables	9,347	489	9,836
Prepayments and other current assets	2,343	(82)	2,261
Other non-current assets	35	111	146
Loans and borrowings	(8)	8	-
Provisions	1,186	(273)	913
Trade and other payables	10	(10)	-
	(81,783)	**6,966**	**(74,817)**

22 Other taxes payable

'000 GEL	2010	2009
Property tax liabilities	17,076	11,463
Personal income tax payable	1,226	1,407
Other taxes payable	8,934	8,924
	27,236	**21,794**

23 Financial instruments and risk management

(a) Overview

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

Risk management framework

The Management Board has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

(b) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers.

(i) Cash and bank balances

To mitigate the credit risk of cash and bank balances, the Group holds its funds with the largest five Georgian banks. The Group does not expect any counterparty to fail to meet its obligations.

(ii) Trade and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. Approximately 30% (2009: 22%) of the Group's revenue is attributable to sales transactions with a single customer.

Credit risk is managed by requesting prepayments from freight and passenger transportation customers. Accordingly the Group's trade receivables mainly consist of receivables from foreign railway companies. Credit risk related to receivables from foreign railway companies is managed through the monthly monitoring of the respective receivable balances and requiring immediate repayment of the debt when the balance approaches specific limits set for each individual counterparty.

More than 90% of the Group's foreign railway customers have been transacting with the Group for over four years, and losses have occurred infrequently. In monitoring customer credit risk, customers are grouped according to their credit characteristics, including aging profile, maturity and existence of previous financial difficulties.

No collateral in respect of trade and other receivables is generally required.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables. The main component of this allowance is a specific loss component that relates to individually significant exposures.

(iii) Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

	Carrying amount	
'000 GEL	**2010**	**2009**
Cash and cash equivalents - 5 largest Georgian banks (not impaired or past due)	335,716	1,264
Bank deposits - 5 largest Georgian banks (not impaired or past due)	38,021	-
Trade receivables	22,741	20,970
Other receivables	4,172	1,224
	400,650	**23,458**

The maximum exposure to credit risk for trade receivables at the reporting date by geographic region was:

	Carrying amount	
'000 GEL	**2010**	**2009**
CIS countries	14,223	12,706
Domestic	8,518	8,202
United States	-	62
	22,741	**20,970**

The Group's five most significant customers account for GEL 12,857 thousand of the trade receivables carrying amount at 31 December 2010 (2009: GEL 13,367 thousand).

Impairment losses

The aging of trade receivables at the reporting date was:

’000 GEL	Gross 2010	Impairment 2010	Gross 2009	Impairment 2009
Not past due	-	-	199	-
Past due 0- 90 days	5,622	572	4,788	-
Past due 91-180 days	4,097	1,104	3,178	-
Past due 181-365 days	6,712	1,301	7,769	2,709
Past due more than one year	78,700	69,413	71,373	63,628
	95,131	**72,390**	**87,307**	**66,337**

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

’000 GEL	2010	2009
Balance at beginning of the year	66,337	63,102
Increase during the year	6,053	3,235
Balance at end of the year	**72,390**	**66,337**

Most of the impairment loss at 31 December 2010 relates to several customers that have indicated that they are not expecting to be able to pay their outstanding balances either because of economic circumstances or as a result of bankruptcy. The Group believes that the unimpaired amounts that are past due are still collectible, based on historic payment behaviour and analyses on the underlying customers’ credit ratings.

The allowance account in respect of trade receivables is used to record impairment losses until all possible opportunities for recovery have been exhausted; at that point the amounts are written off against the financial asset directly. At 31 December 2010 the Group does not have any collective impairment on its trade receivables (2009: nil).

(c) Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group’s reputation.

The Group ensures that it has sufficient cash on demand to meet expected operational expenses for a period of three months, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

In addition the Group has an undrawn loan facility from EBRD to partly finance the Tbilisi Bypass project (see note 18).

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements. It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amounts.

2010

’000 GEL	**Carrying amount**	**Contractual cash flows**	**0-6 months**	**6-12 months**	**1-2 years**	**2-5 years**
Unsecured bond issues	457,642	662,030	21,883	21,883	43,766	574,498
Trade and other payables	44,765	44,765	39,215	5,505	45	-
Other current liabilities	15,018	15,018	15,018	-	-	-
Guarantees issued	15,305	15,305	15,305	-	-	-
	532,730	**737,118**	**91,421**	**27,388**	**43,811**	**574,498**

2009

’000 GEL	**Carrying amount**	**Contractual cash flows**	**0-6 months**	**6-12 months**	**1-2 years**	**2-5 years**
Unsecured bond issues	24,982	31,750	1,688	1,688	28,374	-
Unsecured bank facility	3,773	3,876	52	3,824	-	-
Trade and other payables	85,393	85,393	38,300	18,240	28,853	-
Other current liabilities	7,978	7,978	7,978	-	-	-
Guarantees issued	-	15,305	15,305	-	-	-
	122,126	**144,302**	**63,323**	**23,752**	**57,227**	**-**

(d) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group’s income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

(i) Currency risk

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than GEL. The currencies in which these transactions primarily are denominated are U.S. Dollars (USD) and Swiss Francs (CHF).

A majority of the Group’s revenue is denominated in CHF. The Group’s policy is to conclude significant purchase contracts in CHF to match the cash flows generated from operations.

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows based on notional amounts:

'000 GEL	USD - denominated	CHF - denominated	USD- denominated	CHF - denominated
	2010	**2010**	**2009**	**2009**
Cash and cash equivalents	14,979	312,535	387	45
Bank deposits	10,637	27,384	-	-
Trade receivables	84	14,139	233	13,477
Unsecured bank facility	-	-	(3,773)	-
Unsecured bond issues	(457,642)	-	-	-
Trade and other payables	(12,270)	-	(16,770)	(1,813)
Net exposure	**(444,212)**	**354,058**	**(19,923)**	**11,709**

The following significant exchange rates applied during the year:

in GEL	Average rate		Reporting date spot rate	
	2010	**2009**	**2010**	**2009**
USD 1	1.78	1.67	1.77	1.69
CHF 1	1.71	1.54	1.89	1.63

Sensitivity analysis

A strengthening of the GEL, as indicated below, against the following currencies at 31 December would have increased (decreased) profit or loss net of taxes by the amounts shown below. There would have been no impact directly on equity. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2009.

'000 GEL	Profit or loss
2010	
USD (10% strengthening)	37,758
CHF (10% strengthening)	(30,095)
2009	
USD (10% strengthening)	1,693
CHF (10% strengthening)	(995)

A weakening of the GEL against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

(ii) Interest rate risk

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

Profile

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	Carrying amount	
'000 GEL	**2010**	**2009**
Fixed rate instruments		
Financial assets	38,021	-
Financial liabilities	(457,642)	(24,982)
	(419,621)	**(24,982)**
Variable rate instruments		
Financial liabilities	-	(3,773)
	-	**(3,773)**

Bank deposits (included in financial assets above) have a maturity of up to six months from the reporting date and bear annual interest from 3.5% to 8.25%.

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial assets and liabilities at fair value. Therefore a change in interest rates at the reporting date would not affect profit or loss or equity.

(e) Fair values versus carrying amount

Management believes that the fair value of the Group's financial assets and liabilities approximates their carrying amounts.

The basis for determining fair values is disclosed in note 4.

(f) Capital management

The Group has no formal policy for capital management but management seeks to maintain a sufficient capital base for meeting the Group's operational and strategic needs, and to maintain confidence of market participants. This is achieved with efficient cash management, constant monitoring of the Group's revenues and profit, and long-term investment plans mainly financed by the Group's operating cash flows. With these measures the Group aims for steady profits growth. The Group's debt to capital ratio at the end of the reporting period was as follows:

'000 GEL	**2010**	**2009**
Total liabilities	700,339	260,956
Less: cash and cash equivalents	(323,943)	(1,361)
Net debt	**376,396**	**259,595**
Total equity	**1,633,041**	**1,548,683**
Debt to capital ratio at 31 December	0.23	0.17

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

24 Operating leases

Non-cancellable operating lease rentals are receivable as follows:

'000 GEL	**2010**	**2009**
Less than one year	1,408	3,378
Between one and five years	5,341	7,266
More than five years	37,627	37,403
	44,376	**48,047**

Operating leases mainly relate to investment property owned by the Group with lease terms of between 10 to 50 years, as well as the rental of other buildings, containers, locomotives and fittings. Lessees do not have an option to purchase the property at the end of the lease term.

25 Capital commitments

As at 31 December 2010 the Group had entered into contracts for construction works and the purchase of plant and equipment for GEL 653,370 thousand (2009: GEL 36,234 thousand).

26 Contingencies

(a) Insurance

The insurance industry in Georgia is in a developing state and many forms of insurance protection common in other parts of the world are not yet generally available. The Group does not have full coverage for its plant facilities, business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations. Until the Group obtains adequate insurance coverage, there is a risk that the loss or destruction of certain assets could have a material adverse effect on the Group’s operations and financial position.

(b) Taxation contingencies

The taxation system in Georgia is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes unclear, contradictory and subject to varying interpretation. In the event of a breach of tax legislation, no liabilities for additional taxes, fines or penalties may be imposed by the tax authorities after six years have passed since the end of the year in which the breach occurred.

These circumstances may create tax risks in Georgia that are more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Georgian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

(c) Litigation

In the ordinary course of business, the Group is subject to legal actions, litigations and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations.

27 Related party transactions

(a) Control relationships

The Company is wholly owned by the State of Georgia represented by the State Enterprise Management Agency of the Ministry of Economic Development of Georgia.

(b) Transactions with management and close family members

(i) Management remuneration

Key management received the following remuneration during the year, which is included in payroll expenses:

’000 GEL	2010	2009
Salaries and bonuses	**911**	**880**

(c) Transactions with other related parties

The Group's other related party transactions are disclosed below.

(i) Revenue

’000 GEL	Transaction value 2010	Transaction value 2009	Outstanding balance 2010	Outstanding balance 2009
Services provided:				
State-owned companies and government bodies	2	6	-	2

All outstanding balances with related parties are to be settled in cash within six months of the reporting date. None of the balances are secured.

(ii) Expenses and purchases

’000 GEL	Transaction value 2010	Transaction value 2009	Outstanding balance 2010	Outstanding balance 2009
Purchase of goods:				
State-owned companies and government bodies	11,564	2,479	1,548	436
Services received:				
State-owned companies and government bodies	8,072	9,614	1,209	1,083
	19,636	**12,093**	**2,757**	**1,519**

Goods purchased from related parties mainly relate to contruction materials purchased from state-owned companies. Services received mainly relate to security services provided by government bodies.

All outstanding balances with related parties are to be settled in cash within six months of the reporting date. None of the balances are secured.

(iii) Other balances

’000 GEL	2010	2009
Liabilities to the owners	29,352	26,636

Liabilities to the owners relate to property, plant and equipment that has been withdrawn but not yet transferred formally to the Government of Georgia. These liabilities are recognised at the carrying amount of assets to be transferred to the Government of Georgia.

28 Significant subsidiaries

Subsidiary	Country of incorporation	Principal activities	2010 Ownership/ voting	2009 Ownership/ voting
Georgian Railway Property Management LLC	Georgia	Property management and development	100%	100%
Georgian Railway Transcontainer LLC	Georgia	Container transportation	100%	100%
Georgian Railway Construction LLC	Georgia	Construction and other projects	100%	100%
Borjomi Bakuriani Railway LLC	Georgia	Passenger transportation	100%	100%

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