Georgian Railway
Est. 1872

Management Discussion and Analysis for FY and Q4 2017

Financial and non-financial highlights

Revenue

Q4 2017	FY 2017
131,237	**434,534**
+12% from Q4 2016 +20% from Q3 2017	-1.2% from FY 2016

Results from operating activities

Q4 2017	FY 2017
-324,033	**-280,468**
-10.3x from Q4 2016 -17.3x from Q3 2017	-1.6x from FY 2016

EBITDA

Q4 2017	FY 2017
86,013	**211,851**
+43% from Q4 2016 +75% from Q3 2017	-25% from FY 2016

EBITDA margin

Q4 2017	FY 2017
65.5%	**48.8%**
+14 points from Q4 2016 +21 points from Q3 2017	-15 points from FY 2016

Adjusted EBITDA

Q4 2017	FY 2017
63,377	**181,425**
+16% from Q4 2016 +36% from Q3 2017	-7% from FY 2016

Adjusted EBITDA margin

Q4 2017	FY 2017
48.3%	**41.8%**
+2 points from Q4 2016 +5 points from Q3 2017	-3 points from FY 2016

Net investment in fixed capital

Q4 2017	FY 2017
19,534	**168,463**
-61% from Q4 2016 -29% from Q3 2017	-14% from FY 2016

Net debt to EBITDA

31 Dec 2017	31 Dec 2016
4.87	**3.48**
3.59 as at 30 Sep 2017	

Main developments in 2017

- Purchase of two double-decker passenger trains;
- Additional borrowing of USD 20.3 million to finance new passenger trains procurement;
- Transfer of land plots to the Government under the Tbilisi Bypass Project memorandum;
- Freight volume decreased by 10 percent;
- Long-term corporate rating downgrade to 'B+' from 'BB-' by Fitch Ratings in January 2017, affirmed at 'B+' with Stable Outlook in November 2017 and revise of outlook from Stable to Negative by S&P Global Ratings.

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1. Profit or loss statement

GEL '000	Q4 2017	Q4 2016	y-o-y	Q3 2017	q-o-q	2017	2016	y-o-y % change	y-o-y Abs. change
Revenue	131,237	116,916	12.2%	108,967	20.4%	434,534	439,922	-1.2%	-5,388
Income from transferred property	23,417	2,839	724.8%	0	NA	23,417	80,294	-70.8%	-56,877
Other income	2,082	4,778	-56.4%	3,595	-42.1%	15,560	19,122	-18.6%	-3,562
Impairment loss on property, plant and equipment	-382,616	0	NA	0	NA	-382,616	0	NA	-382,616
Employee benefits expense	-38,908	-37,516	3.7%	-35,559	9.4%	-148,302	-146,626	1.1%	-1,676
Depreciation and amortization	-27,430	-28,704	-4.4%	-30,297	-9.5%	-109,703	-106,267	3.2%	-3,435
Electricity, consumables and maintenance costs	-9,808	-12,751	-23.1%	-10,383	-5.5%	-41,490	-47,289	-12.3%	5,799
Other expenses	-22,007	-14,203	54.9%	-17,575	25.2%	-71,868	-63,668	12.9%	-8,200
Result from operating activities	**-324,033**	**31,359**	**-1,133.3%**	**18,747**	**-1,828.5%**	**-280,468**	**175,488**	**-259.8%**	**-455,956**
Net finance income/loss	**-123,661**	**-152,430**	**-18.9%**	**-40,969**	**201.8%**	**-72,984**	**-149,221**	**-51.1%**	**76,237**
Profit before income tax	**-447,694**	**-121,071**	**269.8%**	**-22,222**	**1,914.6%**	**-353,452**	**26,267**	**-1,445.6%**	**-379,719**
Income tax expense(benefit)	-106	56,019	-100.2%	-94	12.3%	-648	38,859	-101.7%	-39,507
Profit and total comprehensive income	**-447,800**	**-65,052**	**588.4%**	**-22,316**	**1,906.6%**	**-354,100**	**65,126**	**-643.7%**	**-419,226**
EBITDA	86,013	60,063	43.2%	49,044	75.4%	211,851	281,755	-24.8%	-69,904
EBITDA margin	65.54%	51.37%	NA	45.01%	NA	48.75%	64.05%	NA	-15.29%
Adjusted EBITDA	63,377	54,554	16.2%	46,698	35.7%	181,425	195,149	-7.0%	-13,724
Adjusted EBITDA Margin	48.29%	46.66%	NA	42.85%	NA	41.75%	44.36%	NA	-2.61%

1.1 Revenue

Most of the Group's revenue (about 60 percent in 2017) is derived from freight transportation. Thus, the Group's results are particularly sensitive to cargo flows, which mainly comprise transit shipments, which accounted for about 63 percent of freight transportation revenue in 2017. The transit transportation volume mainly comes from trade between Europe and Central Asia.

The majority of GR's freight traffic was transported from or to Azerbaijan and Armenia (about 28 percent and 23 percent of transportation revenue in 2017, respectively). Other significant trade partners for the Company in 2017 were Russia, Kazakhstan and Turkmenistan (together generating 38 percent of transportation revenue in 2017). Only about 6 percent of total transportation revenue in 2017 was generated by domestic transportation.

GEL '000	Q4 2017	Q4 2016	y-o-y	Q3 2017	q-o-q	2017	2016	% Change	% Change at constant currency	Abs. Change
Freight transportation*	67,298	74,465	-9.6%	68,538	-1.8%	262,772	292,612	-10.2%	-15.3%	-29,840
Freight handling*	12,015	14,722	-18.4%	13,201	-9.0%	50,189	52,974	-5.3%	-10.1%	-2,785
Logistical service*	40,571	17,713	129.0%	10,462	287.8%	73,774	52,582	40.3%	35.4%	21,192
Freight car rental	6,870	3,115	120.6%	4,044	69.9%	16,780	13,948	20.3%	13.4%	2,832
Passenger traffic	4,056	3,625	11.9%	10,846	-62.6%	22,843	18,007	26.9%	26.7%	4,836
Other	427	3,276	-87.0%	1,876	-77.2%	8,176	9,799	-16.6%	-17.5%	-1,623
Revenue	**131,237**	**116,916**	**12.2%**	**108,967**	**20.4%**	**434,534**	**439,922**	**-1.2%**	-6.0%	**-5,388**
Income from transferred property	**23,417**	**2,839**	**724.8%**	**0**	**NA**	**23,417**	**80,294**	**-70.8%**	**NA**	**-56,877**
Other income	**2,082**	**4,778**	**-56.4%**	**3,595**	**-42.1%**	**15,560**	**19,122**	**-18.6%**	**NA**	**-3,562**
Freight transportation	**67,298**	**74,465**	**-9.6%**	**68,538**	**-1.8%**	**262,772**	**292,612**	**-10.2%**	**-15.3%**	**-29,840**
Liquid cargoes	**30,766**	**37,516**	**-18.0%**	**28,257**	**8.9%**	**115,626**	**135,530**	**-14.7%**	**-17.4%**	**-19,903**
Oil products	28,985	30,295	-4.3%	27,352	6.0%	107,521	107,140	0.4%	-5.3%	381
Crude oil	1,781	7,220	-75.3%	905	96.8%	8,105	28,389	-71.5%	-73.1%	-20,285
Dry cargoes	**36,533**	**36,950**	**-1.1%**	**40,281**	**-9.3%**	**147,146**	**157,082**	**-6.3%**	**-11.6%**	**-9,936**
Ores	5,909	6,147	-3.9%	6,963	-15.1%	25,294	24,820	1.9%	-0.5%	475
Grain	2,158	4,166	-48.2%	1,864	15.8%	7,998	14,320	-44.1%	-47.3%	-6,322
Ferrous metals and scrap	2,383	3,769	-36.8%	3,004	-20.7%	10,508	20,936	-49.8%	-52.6%	-10,428
Sugar	3,850	1,482	159.8%	6,180	-37.7%	18,364	18,333	0.2%	-5.5%	31
Chemicals and fertilizers	3,959	2,958	33.8%	3,509	12.8%	12,682	9,397	35.0%	27.3%	3,284
Construction freight	457	1,429	-68.1%	1,863	-75.5%	5,663	6,275	-9.8%	7.9%	-612
Industrial freight	1,586	800	98.3%	1,157	37.1%	5,246	3,440	52.5%	46.1%	1,806
Cement	153	221	-30.7%	360	-57.5%	1,182	933	26.7%	70.1%	249
Other	16,078	15,978	0.6%	15,379	4.5%	60,209	58,628	2.7%	-3.1%	1,581
Freight turnover (million ton-km)	737	831	-11.3%	709	3.9%	2,930	3,391	-13.6%	-13.6%	-461
Revenue / ton-km (in Tetri)	9.13	8.96	1.9%	9.67	-5.5%	8.97	8.63	3.9%	-14.3%	0.34

** For better presentation, we have separated "logistical services" from "freight transportation" and "freight handling". "Logistical services" represents revenue generated by freight forwarding subsidiaries.*

Freight transportation

The Group's freight transportation revenue consists of liquid and dry cargoes. The split between liquid and dry cargo revenue in 2017 was about 44 and 56 percent, respectively.

Transportation revenue depends on multiple factors, which generally influence its performance and some of them are stated here:

Transportation volume - measured in tons transported.

Transportation turnover - measured in ton-kilometers, which is the product of tons transported and the distance covered.

Revenue per ton-kilometer - the term refers to the average revenue that the Group receives per ton-kilometer. This parameter varies for different types of cargo and largely depends on the cargo type mix and transportation direction mix.

- Cargo type mix - the Group transports different cargo categories (such as grain, ore, sugar etc.). These categories themselves are comprised of many sub-categories, each of which has different tariffs. Therefore, while the actual tariffs for cargo sub-categories may remain the same, the average revenue per ton-kilometer of a main cargo category may still change due to changes in the sub-category mix.
- Transportation direction mix - tariffs differ according to freight origins and directions according to the Group's tariff policy. Thus, when the tariffs for different cargo sub-categories and the sub-category mix remain the same, the average revenue per ton-kilometer may still change because of the change in transportation direction mix.

GEL/USD exchange rate - one important issue in analyzing the performance of the Group is the fact that most of its tariffs are denominated in USD. As the Group reports its revenue in GEL, the changes in the GEL/USD exchange rate can have a significant impact on the Group's profitability, as most of its expenses are denominated in Georgian Lari.

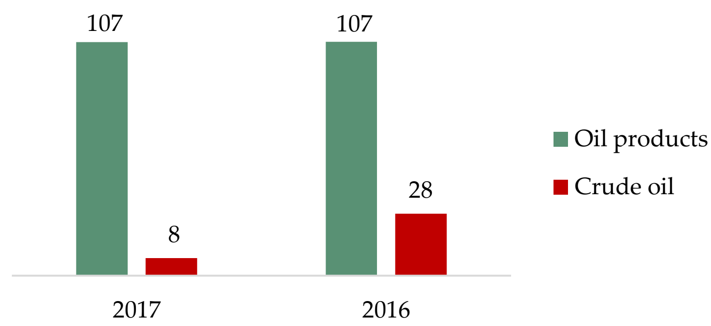
	Average exchange rates			*Reporting date spot rates*		
	2017	2016	% Change	2017	2016	Change
GEL/USD	2.51	2.37	6.0%	2.59	2.65	-2.1%
GEL/CHF	2.54	2.40	6.1%	2.60	2.42	2.3%

Liquid cargo

One of the key drivers of liquid freight traffic is the production of oil and oil products in the Caspian region, which has large oil reserves. In 2017, about 68 percent of crude oil and oil products were transported from three Caspian region countries (Kazakhstan, Turkmenistan and Azerbaijan) mostly to European countries and Georgia.

Most of the Group's liquid cargo revenue comes from oil products.

Breakdown of liquid cargo revenue in GEL mm



Oil products

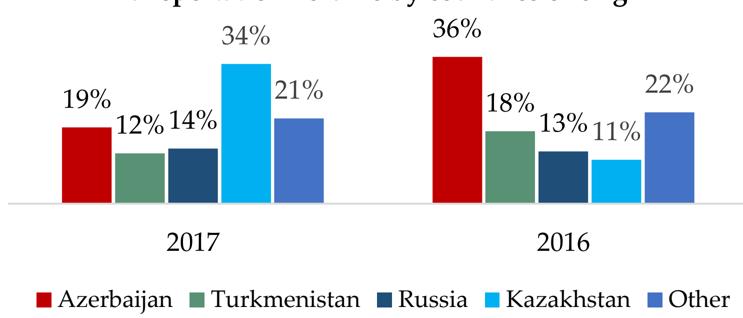
Revenue from the transportation of oil products for Q4 2017 decreased by 4 percent, compared to Q4 2016, but increased by 6 percent, compared to Q3 2017.

Main directions of cargo

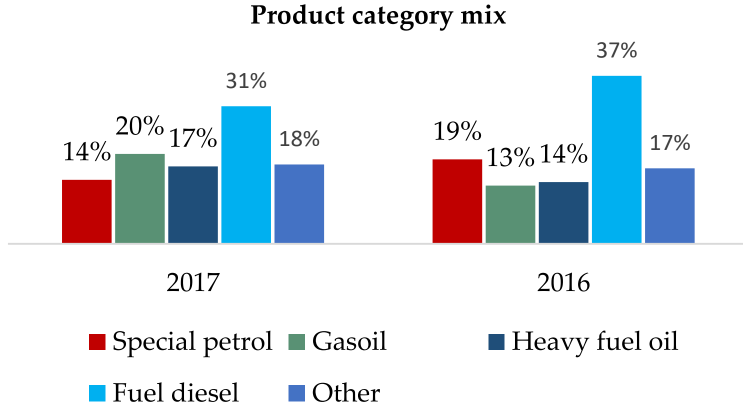
Oil products currently are the main component of liquid cargo (93 percent of the transportation volume of liquid cargo in 2017). They are mainly transported by rail, as there is practically no competition from pipelines.

Oil products transported by the Group during 2017 mainly originated from Azerbaijan, Turkmenistan, Russia and Kazakhstan, with significant changes in transportation direction mix compared to the same period of 2016. The share of Azerbaijan was down to 19 percent from 36 percent, while Kazakhstan's share was up to 34 percent from 11 percent in total oil products transported by the Group.

Transportation volume by countries of origin



Product category mix



Oil products

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	107.52	107.14	0.4%	-5.3%
Freight volume (million ton)	3.95	3.69	7.1%	7.1%
Freight turnover (million ton-km)	1,221.24	1,087.94	12.3%	12.3%
Revenue / ton-km (in Tetri)	8.80	9.85	-10.6%	-15.7%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*

*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers – 12 percent increase in transportation turnover was mainly driven by increased transported volume by 7 percent, caused by increased volumes from Kazakhstan and Russia, by 957,000 tons and 62,000 tons, respectively, which was partly offset by decreased volumes from Azerbaijan and Turkmenistan, by 591,000 tons and 168,000 tons, respectively. Another reason was increased average transportation distance, mainly driven by increased share from Kazakhstan (which covers longer distances) and decreased share from Azerbaijan (which covers shorter distances) in total transportation volume of oil products.

Revenue/ton-km (in Tetri) - decrease in average revenue per ton-kilometer during 2017, compared to 2016 was mainly due to changes in product category mix. The share of Fuel diesel (which is relatively more profitable product) has decreased and share of Gasoil (which is relatively less profitable product) has increased in total oil products transported by Georgian Railway.

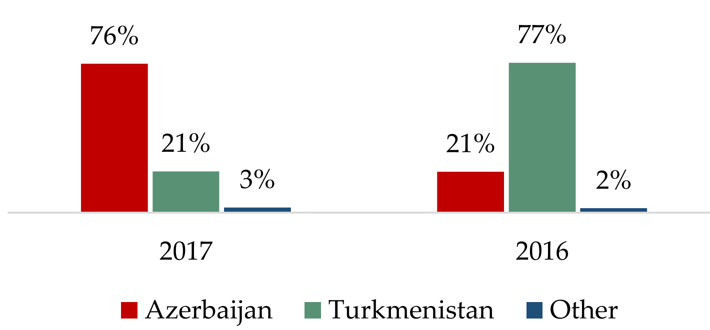
Crude oil

Revenue from the transportation of crude oil for Q4 2017 decreased by 75 percent, compared to Q4 2016, but increased by 97 percent, compared to Q3 2017.

Main directions of cargo

The crude oil transported by Georgian Railway during 2017 mostly originated from Azerbaijan (about 76 percent) and Turkmenistan (about 21 percent). The main points of destination in 2017 were USA (up to 76 percent from 16 percent in 2016) and Italy (down to 22 percent from 82 percent in 2016).

Transportation volume by countries of origin



Crude oil

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	8.10	28.39	-71.5%	-73.1%
Freight volume (million ton)	0.40	1.81	-77.8%	-77.8%
Freight turnover (million ton-km)	157.60	713.65	-77.9%	-77.9%
Revenue / ton-km (in Tetri)	5.14	3.98	29.3%	22.0%

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*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - decrease in freight turnover was mainly caused by the sharp fall in crude oil transportation volume from Turkmenistan to Italy during 2017, which was down by 1.3 million tons, compared to 2016.

Revenue/ton-km (in Tetri) - increase in revenue per ton-kilometer was mainly caused by changes in transportation direction mix. Transportation share from Azerbaijan, relatively more profitable direction, has seen a considerable increase during 2017, compared to the same period of the previous year, while transportation volume from Turkmenistan, relatively less profitable direction, has declined significantly.

Dry cargo

Dry cargo contributed about 56 percent to total transportation revenue in 2017. The major factors driving transportation of dry cargo are general national economic conditions and economic developments in Georgia and in partnering countries such as Azerbaijan, Armenia, Turkmenistan, Kazakhstan and other CIS countries.

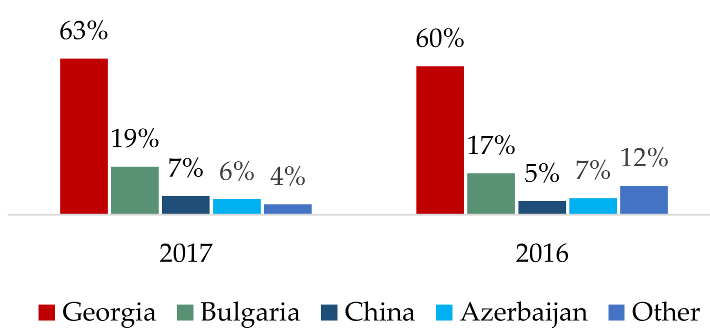
Ore products

Revenue from the transportation of ore products for Q4 2017 increased by 4 percent, compared to Q4 2016 and by 15 percent, compared to Q3 2017.

Main directions of cargo

The main origin countries for ore products during the period under review were Georgia, Armenia and Russia. No transportation was made from Brazil, Gabon and Switzerland during 2017, while the share of transportation volume from these countries for 2016 was 8 percent in total. The main destination points of ore products transported by the Group are Georgia, Bulgaria, China and Azerbaijan. About 35 percent of total transportation

Transportation volume by destination countries



volume in 2017 was transported within Georgia. Ore products transported by the Group in 2017 mostly comprise copper ores and concentrates (about 27 percent), manganese ores and concentrates (about 23 percent), and coal (about 16 percent).

Ore Products

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	25.29	24.82	1.9%	-0.5%
Freight volume (million ton)	1.42	1.45	-2.1%	-2.1%
Freight turnover (million ton-km)	296.40	310.57	-4.6%	-4.6%
Revenue / ton-km (in Tetri)	8.53	7.99	6.8%	4.2%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*
*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - decrease in freight transportation turnover was mainly due to the reduction in transported volumes of manganese ores and concentrates and coal, by 70,000 tons and 56,000 tons, respectively, which was partly offset by increased transportation of Bituminous coal and copper ores and concentrates, by 55,000 tons and 41,000 tons, respectively. Another reason for decreased turnover was reduction in average transportation distance for ore products directed to Georgia.

Revenue/ton-km (in Tetri) – average revenue per ton-kilometer in 2017 increased by 7 percent, compared to 2016. GR signed a contract with entity according to which an agreement was made on fixed exchange. Without this issue taken into account, average revenue per ton-kilometer would have increased by 10 percent.

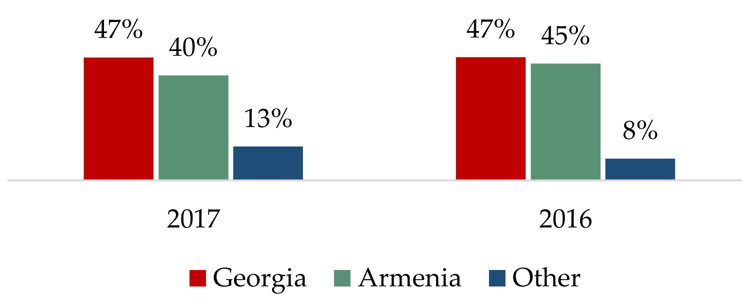
Grain and grain products

Revenue from the transportation of grain and grain products for Q4 2017 decreased by 48 percent, compared to Q4 2016, but increased by 16 percent, compared to Q3 2017.

Main directions of cargo

Transportation volume of wheat represents about 81 percent of total grain and grain products transported in 2017. The main country of origin for grain and grain products was Russia (72 percent in 2017). The main destination countries were Georgia and Armenia.

Transportation volume by destination countries



Grain and grain products

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	8.00	14.32	-44.1%	-47.3%
Freight volume (million ton)	0.30	0.45	-32.5%	-32.5%
Freight turnover (million ton-km)	75.33	140.64	-46.4%	-46.4%
Revenue / ton-km (in Tetri)	10.62	10.18	4.3%	-1.6%

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*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - decrease in freight transportation turnover by 46 percent was mainly caused by the decreased transportation of wheat originated from Russia in the direction of Georgia and Armenia, by 59,000 and 93,000 tons, respectively. Another reason was significant reduction (53 percent) of average transportation distance for one of the main destination countries, Georgia.

Revenue/ton-km (in Tetri) – decrease in average revenue per ton-kilometer at constant currency was mainly driven by reduced share of freight transported to Armenia (relatively more profitable direction) in total volume transported by the Group.

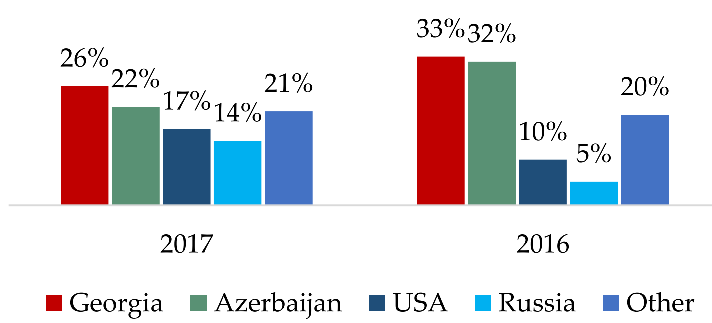
Ferrous metals and scrap

Revenue from the transportation of ferrous metals and scrap for Q4 2017 decreased by 37 percent, compared to Q4 2016 and by 21 percent, compared to Q3 2017.

Main directions of cargo

The main destination countries for ferrous metals and scrap during the period under review were Georgia, Azerbaijan, USA and Russia, together creating 79 percent of total volume transported in 2017.

Transportation volume by destination countries



Ferrous metals and scrap

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	10.51	20.94	-49.8%	-52.6%
Freight volume (million ton)	0.53	0.66	-20.2%	-20.2%
Freight turnover (million ton-km)	123.44	163.10	-24.3%	-24.3%
Revenue / ton-km (in Tetri)	8.51	12.84	-33.7%	-37.4%

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*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers – the main driver of 24 percent decrease in transportation turnover during 2017, compared to 2016, was 20 percent decrease in total ferrous metals and scrap transported by the Group caused by ceased transportation of pipes for oil and gas pipelines to Azerbaijan. Decreased transportation turnover was also driven by reduction in average transportation distance, which was on its own caused by reduced share of freight transported to Azerbaijan (which covers longer distances) from 32 percent to 22 percent in total volume transported, while the share of freight transported to Russia (which covers shorter distances) has increased from 5 to 14 percent.

Revenue/ton-km (in Tetri) - decrease in average revenue per ton-kilometer was due to ceased transportation of pipes for oil and gas pipelines to Azerbaijan (14 percent of ferrous metals and scrap transported in 2016), which are relatively more profitable products, because of changes in product category mix transported to Georgian direction and also due to the increase of shares of volumes directed to Russia and USA (which are less profitable directions) in total volume transported by the group.

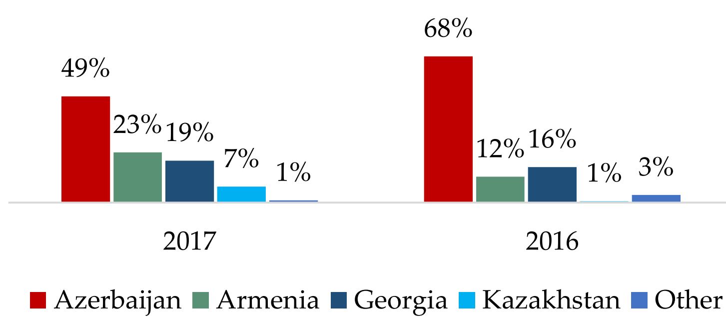
Sugar

Revenue from the transportation of sugar for Q4 2017 increased by 160 percent, compared to Q4 2016 but decreased by 38 percent, compared to Q3 2017.

Main directions of cargo

Brazil was the main country of origin for transported volumes of sugar in 2017 and 2016, with the share of 93 percent and 91 percent, respectively. Main destination countries of the sugar were Azerbaijan, Armenia, Georgia and Kazakhstan (99 percent of total volume transported by the Group).

Transportation volume by destination countries



Sugar

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	18.36	18.33	0.2%	-5.5%
Freight volume (million ton)	0.38	0.50	-24.2%	-24.2%
Freight turnover (million ton-km)	134.82	183.89	-26.7%	-26.7%
Revenue / ton-km (in Tetri)	13.62	9.97	36.6%	28.9%

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*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - decrease in transportation turnover in 2017, compared to 2016, was driven by reduced transportation of reed sugar for refining from Brazil to Azerbaijan, by 160,000 tons.

Revenue/ton-km (in Tetri) – 37 percent increase in average revenue per ton-kilometer was caused by the contract according to which the entity was obliged to transport specified volume of sugar and in the case of failure it should have paid the amount of underperformed volumes. The entity failed to perform volumes amount of which was GEL 3.9 million. As a result, only transportation revenue increased. Without this issue taken into account, the average revenue per ton-kilometer has increased by 8 percent.

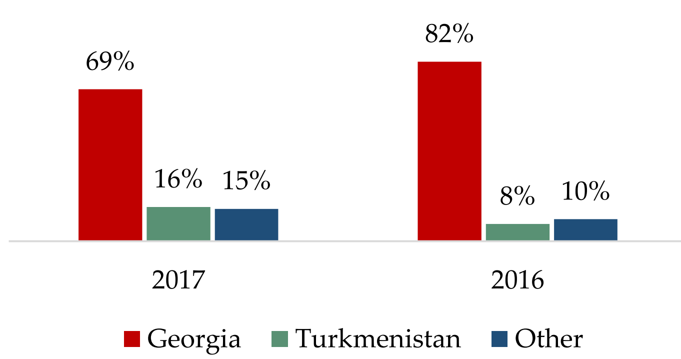
Chemicals and fertilizers

Revenue from the transportation of chemicals and fertilizers for Q4 2017 increased by 34 percent, compared to Q4 2016 and by 13 percent, compared to Q3 2017.

Main directions of cargo

The main countries of origin for transported volumes for chemicals and fertilizers during the period under review were Georgia and Turkmenistan, together creating 85 percent of total volume transported in 2017. Chemicals and fertilizers were mainly transported to Black Sea ports. Relatively small portion of the products was transported to Georgia and Armenia. In 2017, the Group has mainly transported ammonium nitrate under the chemicals and fertilizers freight category, with 77 percent of share.

Transportation volume by countries of origin



Chemicals and fertilizers

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	12.68	9.40	35.0%	27.3%
Freight volume (million ton)	0.57	0.43	31.8%	31.8%
Freight turnover (million ton-km)	184.28	132.77	38.8%	38.8%
Revenue / ton-km (in Tetri)	6.88	7.08	-2.8%	-8.3%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*
*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - increase in transportation turnover during 2017, compared to 2016, was mainly due to the increased transportation of ammonium nitrate and urea by 74,000 tons and 55,000 tons, respectively. Another reason was increased average transportation distance, as a result of changes in product category mix and transportation direction mix.

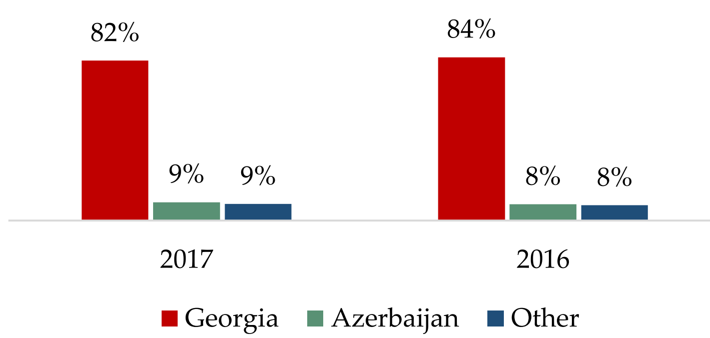
Revenue/ton-km (in Tetri) - decrease in average revenue per ton-kilometer was mainly due to reduced average revenue per ton-kilometer for ammonium nitrate in line with changes in product category mix as the share in total transported volume of relatively less profitable products, urea and ammonium hydrogen phosphate, has increased.

Construction freight

Revenue from the transportation of construction freight for Q4 2017 decreased by 68 percent, compared to Q4 2016 and by 75 percent, compared to Q3 2017.

Main directions of cargo

Transportation volume by countries of origin



Transportation of construction freight correlates with activities of the construction sector in Georgia. The share of construction freight transported within Georgia was about 81 percent. The second largest country of origin after Georgia in 2017 and 2016 was Azerbaijan, with 9 percent and 8 percent of total transported volume of construction freight, respectively. The main product under construction freight category was limestone with 60 percent of share of total volume in 2017, compared to 61 percent in 2016.

Construction freight

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	5.66	6.28	-9.8%	7.9%
Freight volume (million ton)	1.16	1.07	8.6%	8.6%
Freight turnover (million ton-km)	159.67	142.03	12.4%	12.4%
Revenue / ton-km (in Tetri)	3.55	4.42	-19.7%	-4.0%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*
*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

<u>Ton-kilometers</u> – 9 percent increase in transportation turnover was driven by increased volumes due to increased transportation of limestone (by 43,000 tons) and pebbles, gravel and crushed stone (together by 25,000 tons) within Georgia combined with increased average transportation distance for two main origin countries, Georgia (by 3 percent) and Azerbaijan (by 19 percent), which itself was caused by changes in transportation direction mix.

<u>Revenue/ton-km (in Tetri)</u> - decrease in average revenue per ton-kilometer was mainly due to decreased average revenue per ton-kilometer for Georgia, main origin country, by 5 percent, caused by changes in product category mix. Another reason was that GR signed a contract with entity according to which an agreement was made on fixed exchange rate. Without this issue taken into account, average revenue per ton-kilometer in GEL terms would have increased by 2 percent.

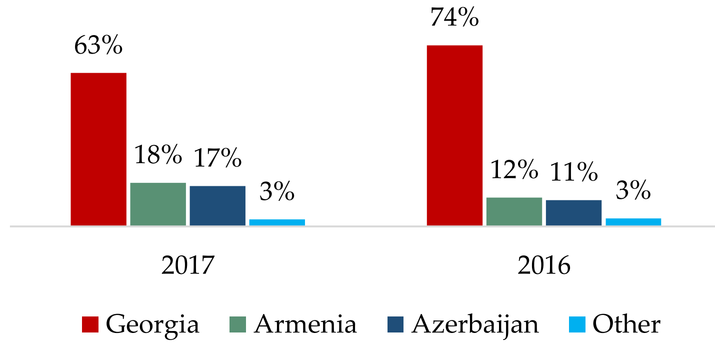
Industrial freight

Revenue from the transportation of industrial freight for Q4 2017 increased by 98 percent, compared to Q4 2016 and by 37 percent, compared to Q3 2017.

Main directions of cargo

The main country of origin for total transported volume of industrial freight during 2017 was Azerbaijan, with 47 percent of share. The significant part of cargo (97 percent) was directed to Georgia, Armenia and Azerbaijan. In 2017, the Group has mainly transported cement clinker under the industrial freight category, with 46 percent of share.

Transportation volume by destination countries



Industrial freight

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	5.25	3.44	52.5%	46.1%
Freight volume (million ton)	0.30	0.27	11.7%	11.7%
Freight turnover (million ton-km)	52.51	38.67	35.8%	35.8%
Revenue / ton-km (in Tetri)	9.99	8.90	12.3%	7.6%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*

*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers – 36 percent increase in transportation turnover was driven by two reasons. First of them was increased volume by 12 percent, caused by increased transportation of barite to Azerbaijan, by 23,000 tons and increased transported volume of siliceous sand and quartz to Armenia, by 23,000 tons. Another reason was increased average transportation distance by 22 percent, due to increased shares of volumes directed to Azerbaijan and Armenia (which cover longer distances) and decreased share of Georgia (which covers shorter distances) in total industrial freight transported during 2017 as well as increase in average transportation distance in direction of Armenia, by 35 percent.

Revenue/ton-km (in Tetri) – increased share of barite, siliceous sand and quartz (which are relatively more profitable products) in total industrial freight transported by the Group, combined with increased average revenue per ton-kilometer of cement clinker, by 18 percent contributed to increase in average revenue per ton-kilometer for industrial freight.

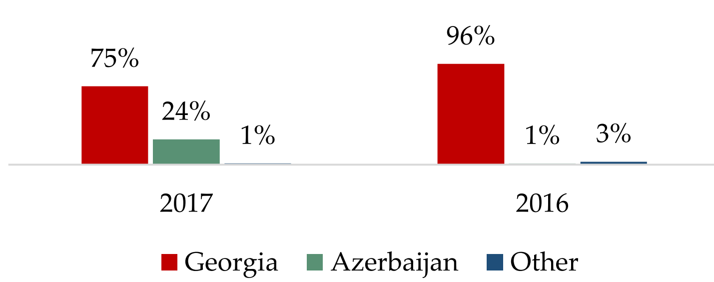
Cement

Revenue from the transportation of cement for Q4 2017 decreased by 31 percent, compared to Q4 2016 and by 57 percent, compared to Q3 2017.

Main directions of cargo

Cement is mainly transported within Georgia, the share of which was down from 96 percent in 2016 to 75 percent in 2017. This decrease was caused by increased transportation of cement originated from Azerbaijan.

Transportation volume by countries of origin



Cement

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	1.18	0.93	26.7%	70.1%
Freight volume (million ton)	0.09	0.06	53.2%	53.2%
Freight turnover (million ton-km)	22.35	17.08	30.9%	30.9%
Revenue / ton-km (in Tetri)	5.29	5.46	-3.2%	30.0%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*
*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers – transportation turnover has increased by 31 percent, although volume has increased by 53 percent (caused by increased transportation from Azerbaijan and Georgia by 22,000 tons and 11,000 tons, respectively). These disproportional changes were mainly due to decreased average transportation distance caused by increased share of Azerbaijan (which covers relatively shorter distances) in total transported volume of cement in 2017.

Revenue/ton-km (in Tetri) - increase in average revenue per ton-kilometer at constant currency was caused by increased share of cement originated from Azerbaijan (which is more profitable direction) in total transportation volume during 2017, compared to 2016. The reason for 3 percent decrease in GEL terms was that GR signed a contract with entity according to which an agreement was made on fixed exchange. Without this issue taken into account, average revenue per ton-kilometer in GEL terms would have increased by 38 percent.

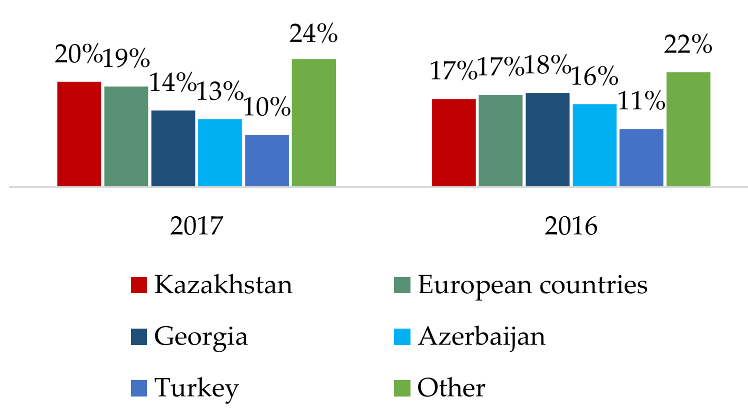
Other product categories

Revenue from the transportation of other product categories for Q4 2017 increased by 1 percent, compared to Q4 2016 and by 5 percent, compared to Q3 2017.

Main directions of cargo

The main origin countries for other product categories in 2017 were Azerbaijan, Ukraine and Georgia. The cargo was mainly directed to Kazakhstan, European countries, Georgia, Azerbaijan and Turkey. Main products transported in 2017 were methanol (about 15 percent of total volume), mineral waters (about 7 percent of total volume) and meat (about 6 percent of total volume).

Transportation volume by destination countries



Other products

For the year ended 31 December

	2017	2016	% Change	% Change at constant currency
Revenue (GEL million)	60.21	58.63	2.7%	-3.1%
Freight volume (million ton)	1.57	1.50	5.1%	5.1%
Freight turnover (million ton-km)	502.15	460.66	9.0%	9.0%
Revenue / ton-km (in Tetri)	11.99	12.73	-5.8%	-11.1%

**For better presentation, we have separated "logistical services" from "freight transportation" and ''freight handling''. ''Logistical services'' represents revenue generated by freight forwarding subsidiaries.*
*** Revenue per ton-kilometer represents revenue from freight transportation (excluding revenue from logistic service) divided by ton-kilometers.*

Factors influencing performance

Ton-kilometers - decreased transportation turnover in 2017, compared to 2016, was mainly due to increased transported volume directed to Kazakhstan, by 63,000 tons and increased average transportation distance caused by changes in transportation direction mix.

Revenue/ton-km (in Tetri) - decrease in average revenue per ton-kilometer was mainly due to changes in transportation direction mix and product category mix. The share of transported volume directed to relatively more profitable directions, Georgia and Azerbaijan, in total transported volume has decreased, while the share of relatively less profitable direction, European countries, has increased. The share of relatively more profitable product, meat, in total transported volume was down from 8 percent in 2016 to 6 percent in 2017, while the share of relatively less profitable product, methanol was up from 8 percent in 2016 to 15 percent in 2017.

Freight handling

General description

Revenue from freight handling comprises several components:

- Revenue from station services, derived from railcar marshaling, freight pick-up, delivery at customer facilities and other related services;
- Revenue from 24-hour railcar delays, which is represented by a fee paid by customers for failing to load or unload a railcar within 24 hours from delivery of railcar at an agreed destination;
- Revenue from certain other services, derived from cargo loading/unloading, storage, accelerated service fees and other sources.

Currency and tariff setting

Most of the freight handling revenue, about 86 percent in 2017, was denominated in USD, while the rest was denominated in GEL (10 percent) and CHF (4 percent). The Group sets its tariffs independently.

Driver

The revenue from this source largely fluctuates in line with transportation volumes in tons. The correlation, however, is not perfect as there are many influential factors.

Freight handling

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Station services	43,048	47,205	-8.8%	-4,157
24-hour service	3,223	4,298	-25.0%	-1,075
Other	3,918	1,471	166.3%	2,447
Total	**50,189**	**52,974**	**-5.3%**	**-2,785**

Revenue from freight handling for Q4 2017 decreased by 18 percent, compared to Q4 2016 and by 9 percent, compared to Q3 2017.

Factors influencing performance

5 percent decrease in revenue from freight handling during the period under review, compared to the same period of the previous year, was mainly driven by 10 percent decrease in transportation volumes.

Logistical services

General description

Revenue from logistical services is generated by GR's subsidiaries.

Currency and tariff setting

Revenue from logistical services is denominated in USD and GEL, with 62 percent and 38 percent, respectively.

Driver

Revenue from this source mainly changes in line with transportation turnover and volumes in tons.

Logistical services

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Revenue from logistical services	73,774	52,582	40.3%	21,192

Revenue from logistical services for Q4 2017 increased by 129 percent, compared to Q4 2016 and by 288 percent, compared to Q3 2017.

Factors influencing performance

40 percent increase in revenue from logistical services during 2017, compared to 2016, was driven by GEL 26.4 million (equivalent of USD 10.2 million) revenue from ship-or-pay agreement, according to which Turkmenistan side should have reimbursed the contract amount, if it did not transport crude oil by Georgian Railway.

Freight car rental

General description

Freight car rental revenue is derived when the Group's railcars are used by other railways.

Currency and tariff setting

Revenue from freight car rental is denominated in CHF and tariffs are set by The Council for Rail Transport of CIS States (CRT CIS).

Drivers

Freight car rental revenue changes according to tariffs and the number of days the Group's railcars are used by other railways.

Freight car rental

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Freight car rental	16,780	13,948	20.3%	2,832

Freight car rental revenue for Q4 2017 increased by 121 percent, compared to Q4 2016 and by 70 percent, compared to Q3 2017.

Factors influencing performance

The increase in revenue from freight car rental by 20 percent (GEL 2.8 million) in 2017 compared to 2016 was largely attributable to increased usage of open top-box wagons by Kazakhstan (CHF 410,962 in fourth quarter of 2017, compared to CHF 503 in full year 2016).

Passenger traffic

General description

Passenger transportation comprises domestic and international services. Domestic transportation includes regional and long-distance transportation. Long-distance traffic accounts for the majority of the Group's passenger traffic, while the regional services, in particular suburban services, typically serve the low-income sections of society and fares for such services are low. Georgian rail lines are linked to Azerbaijan and Armenia, and international transportation services are provided to both countries.

In July 2016, the Group acquired two new double-decker trains meeting European standards from Swiss rolling stock manufacturer Stadler Bussnang, which started to serve the passengers going from Tbilisi to the Black Sea resorts in the summer. Two more double-decker trains were procured in 2017.

Currency and tariff setting

Tariffs for domestic transportation are set independently by the Group, in GEL. Tariffs are not determined by market forces and are kept relatively low, because the Group's affordable passenger transportation services have social importance. Accordingly, GR may be restricted from removing or reducing services on certain passenger routes, even in cases when such routes are not economically feasible.

Tariffs for international transportation are set through negotiations between countries and are denominated in CHF.

Drivers

Passenger revenue fluctuations are in line with the tariffs and number of passengers transported.

Passenger transportation

For the year ended 31 December

	2017	2016	% Change	Abs. change
Revenue in GEL '000	22,843	18,007	26.9%	4,836
Number of passengers '000	2,684	2,463	9.0%	221

Revenue from passenger transportation for Q4 2017 increased by 12 percent, compared to Q4 2016 but decreased by 63 percent, compared to Q3 2017.

Factors influencing performance

Revenue from passenger transportation increased by 27 percent (GEL 4.8 million) in 2017, compared to 2016, while the number of passengers has increased by 9 percent. The higher increase in revenue was driven by increased share of number of passengers on the main line (as a result of increased number of passengers by 191,000 caused by introduction of two more double-decker trains in 2017 in addition to first two, operating since summer 2016) in total number of passengers transported, which is relatively more profitable direction. The average loading rate of the trains on the main line in 2017 was 67 percent, compared to 65 percent in 2016.

Other revenue

General description

Other revenue is mostly denominated in GEL and comprises items such as revenue from renting out spaces in buildings owned by the Group, sale of scrap and repair services for third parties.

Other revenue

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Revenue from rent	4,434	4,871	-9.0%	-438
Revenue from repair	425	450	-5.6%	-25
Revenue from sale of materials (scrap)	1,456	2,663	-45.3%	-1,206
Other	1,860	1,815	2.5%	46
Total	**8,176**	**9,799**	**-16.6%**	**-1,623**

Other revenue for Q4 2017 decreased by 87 percent, compared to Q4 2016 and by 77 percent, compared to Q3 2017.

Factors influencing performance

Decrease in other revenue by GEL 1.6 million during 2017, compared to 2016, was driven by decrease in revenue from sale of scrap, by 45 percent.

1.2 Income from transferred property

General description

In April 2012, GR and the Government signed the Tbilisi Bypass Project Memorandum according to which the Government aims to purchase from the Group approximately 70 hectares of land plots which will be released as a result of the removal of railway infrastructure from Tbilisi city center. The Company will be reimbursed for the amount of VAT paid for the sale. The Government agreed to pay the equivalent of CHF 138 million in the national currency to the Group by reducing the amount of dividends payable to the Government. In 2012, the Company declared dividends of which GEL 232 million (CHF 138 million) were classified as an advance received from the Government for the sale of the land for the Tbilisi Bypass Project Memorandum.

Income from transferred property

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Income from transferred property	23,417	80,294	-70.8%	-56,877

Factors influencing performance

In 2017 and 2016, GR transferred 44,672 and 89,166 square meter land plots with attached constructions, respectively, to the Government within the framework of the Tbilisi Bypass Project Memorandum.

The difference between the fair value and the carrying value of the transferred property (GEL 23,417,000 and GEL 80,294,000, respectively in 2017 and 2016) was recognized as income in the consolidated profit or loss statement.

1.3 Other income

General description

Other income mostly comprises items such as penalties accrued on debtors or creditors, sale of fixed assets and provision reversals.

In order to better illustrate the operational profitability of the Group, other income is split into two categories: continuing operations (such as penalties on creditors and debtors); and non-continuing operations (such as provision reversals and sale of fixed assets, which are not expected to sustainably reoccur in the future).

Other income

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Continuing operations	7,748	12,165	-36.3%	-4,417
Non-continuing operations	7,812	6,957	12.3%	855
Total	**15,560**	**19,122**	**-18.6%**	**-3,562**

Other income for Q4 2017 decreased by 56 percent, compared to Q4 2016 and by 42 percent, compared to Q3 2017.

Factors influencing performance

The decrease in continuing operations in 2017, compared to 2016 was mainly due to the decrease of accrued penalties on debtors by GEL 5.3 million.

1.4 Operating expenses

General description

Most of the Group's operating expenses are fixed. Variable expenses that depend on the volume of transportation include: freight car rental; electricity of traction; fuel expenses; materials, repair and maintenance expenses.

Operating expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Employee benefits expense	148,302	146,626	1.1%	1,676
Depreciation and amortization	109,703	106,267	3.2%	3,435
Impairment loss on property, plant and equipment	382,616	0	NA	382,616
Electricity	20,868	21,687	-3.8%	-819
Materials	11,565	14,121	-18.1%	-2,556
Repair and maintenance	3,820	7,175	-46.8%	-3,355
Fuel	5,237	4,306	21.6%	931
Freight car rental	4,095	4,407	-7.1%	-312
Logistical services	12,996	14,270	-8.9%	-1,274
Security, other op. expenses	27,734	18,517	49.8%	9,218
Taxes other than income tax	27,043	26,474	2.2%	569
Total	**753,980**	**363,850**	**107.2%**	**390,128**

Total operating expenses for Q4 2017 increased by 416.0 percent, compared to Q4 2016 and by 412.5 percent, compared to Q3 2017.

Total operating expenses in 2017 increased by 107.2 percent (GEL 390.1 million), compared to 2016, mainly driven by impairment loss on property, plant and equipment incurred by impairment of Tbilisi Bypass Project. The increase also incurred in fixed expenses such as employee benefits expense (by GEL 1.7 million), depreciation and amortization (by GEL 3.4 million), security and other operating expenses (by GEL 9.2 million) and taxes other than income tax (by GEL 0.6 million), which was partly offset by decrease in variable expenses as a result of decreased transportation volumes.

Employee benefits expense

General description

The Group's salary expenses are not related to changes in the transportation volume as employees' salaries are fixed. The salaries are denominated in GEL, thus FX changes do not affect the cost.

Employee benefits expenses

For the year ended 31 December *In GEL '000*

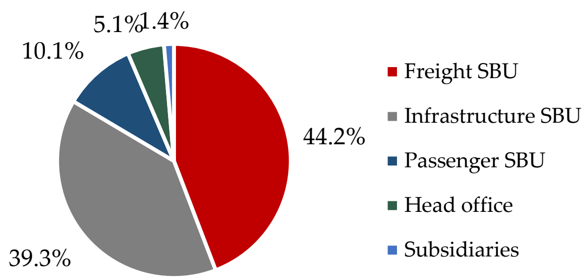
	2017	2016	% Change	Abs. change
Salary	125,632	125,938	-0.2%	-306
Bonus-reward	6,882	6,188	11.2%	694
Other benefits	15,788	14,500	8.9%	1,285
Total	**148,302**	**146,626**	**1.1%**	**1,676**

Employee benefits expenses for Q4 2017 increased by 4 percent, compared to Q4 2017 and by 9 percent, compared to Q3 2017.

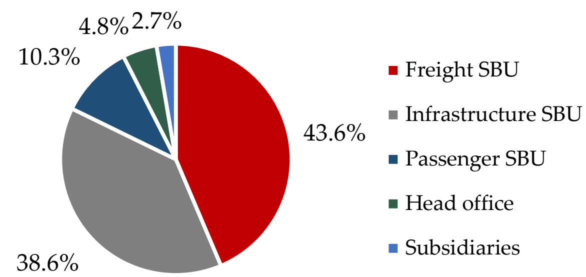
Factors influencing changes

The Group is one of the largest corporate employers and taxpayers in Georgia. This fact underlines its importance for the Government of Georgia along with other important economic and social benefits for the country. Total employee benefit expense increased by GEL 1.7 million in 2017, compared to 2016, mainly driven by increased insurance expenses by GEL 1.0 million.

Distribution of staff by business unit as at the end of 2017



Distribution of staff by business unit as at the end of 2017



Depreciation and amortization expenses

General description

The Group's depreciation and amortization expenses are mainly affected by capital additions and property retirements from disposal, sale or abandonment. The expenses are denominated in GEL and thus are not affected by fluctuations in foreign exchange rates.

Depreciation and amortization expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Depreciation and amortization	109,703	106,267	3.2%	3,435

Depreciation and amortization expenses for Q4 2017 decreased by 4 percent, compared to Q4 2016 and by 9 percent, compared to Q3 2017.

Factors influencing changes

An increase in depreciation and amortization expenses in 2017, compared to 2016, was mainly driven by revision of useful lives for certain infrastructure assets, as well as increase of PP&E as a result of the Group's investments in infrastructure.

Electricity expenses

General description

Approximately 97 percent of GR's railway network is electrified. Until September 2011, the Company purchased most of its electricity on the open market in Georgia. In 2011, the Company signed a ten-year contract with the electricity provider, JSC Energo-pro Georgia, securing a fixed price for more than 90% of its electricity needs (subject to certain circumstances in which these tariffs can be increased). The tariffs are denominated in GEL.

Electricity expenses are split into two categories: electricity expenses of traction, which are driven by transportation turnover (the Group uses electric locomotives for freight transportation and diesel locomotives for shunting operations); and utility expenses which is not related to transportation volume and is normally considered to be fixed.

Electricity expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Electricity expenses of traction	17,537	18,373	-4.6%	-836
Utility expenses	3,333	3,314	0.6%	19
Total	**20,868**	**21,687**	**-3.8%**	**-819**

Electricity expenses for Q4 2017 decreased by 6 percent, compared to Q4 2016 but increased by 9 percent, compared to Q3 2017.

Factors influencing changes

The decrease in electricity expenses of traction in 2017 compared to 2015, was caused by decreased turnover, which was partly offset by increased average electricity tariffs.

Purchased electricity and weighted average tariff

For the year ended 31 December

	2017			2016		
	GWH	Gross ton-km (MM)	Weighted av. tariff (GEL)	GWH	Gross ton-km (MM)	Weighted av. tariff (GEL)
January	14.5	620.3	0.121	12.5	491.3	0.119
February	12.6	497.4	0.121	13.5	586.8	0.119
March	12.5	490.7	0.119	12.7	536.2	0.115
April	11.4	416.7	0.118	12.0	498.1	0.116
May	10.9	408.3	0.117	12.0	502.9	0.116
June	11.5	451.7	0.116	12.4	537.8	0.116
July	12.4	459.5	0.116	13.1	562.4	0.116
August	12.3	465.8	0.117	15.5	684.6	0.117
September	12.6	489.3	0.118	13.8	596.4	0.116
October	12.0	463.1	0.119	13.8	593.6	0.117
November	12.5	480.9	0.119	12.4	508.7	0.117
December	12.8	484.9	0.119	13.5	533.4	0.117
Total	**148.1**	**5,728.6**	**0.118**	**157.3**	**6,632.1**	**0.117**

Note: The table above includes only electricity consumed of traction.

Materials, repair and maintenance expenses

General description

The Group consumes materials for repair works performed internally by its own employees. This consumption is presented under "materials expenses". However, some repair works are outsourced and are presented under "repair and maintenance expenses".

The Group's materials, repair and maintenance expenses are all tied to its rolling stock equipment balance, their utilization level and transportation volume. When the transportation volume and transportation by the Group's own rolling stock increases, so too do the expenses for materials, repair and maintenance. However, this expense can also be affected by increased capital expenditures on the fleet and infrastructure, which reduces operating expenditures on repairs.

Materials, repair and maintenance expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Materials expenses	11,565	14,121	-18.1%	-2,557
Repair and maintenance	3,820	7,175	-46.8%	-3,356
Total	**15,385**	**21,296**	**-27.8%**	**-5,912**

Materials, repair and maintenance expenses for Q4 2017 decreased by 51 percent, compared to Q4 2016 but increased by 32 percent, compared to Q3 2017.

Factors influencing changes

28 percent decrease in materials, repair and maintenance expenses during 2017, compared to 2016, was driven by fewer repair works as a result of downturn in cargo volumes.

Fuel expenses

General description

The Group's fuel consumption principally relates to diesel locomotives fulfilling shunting operations. It should be noted that the main driver for these operations is dry cargo. In everyday business processes, diesel-locomotives are used for railcar marshaling, freight pick-up and delivery at customer facilities.

Another factor affecting the fuel expenses is the nature of the cargo (whether it is import, export, local or transit). While transit cargo is mainly served at one of the Group's stations, most local, export and import cargoes are served in two stations (the origin and destination stations).

Fuel expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Fuel expenses	5,237	4,306	21.6%	931

Fuel expenses for Q4 2017 increased by 28 percent, compared to Q4 2016 and by 29 percent, compared to Q3 2017.

Factors influencing changes

Total fuel expenses increased by 22 percent (GEL 0.9 million) in 2017, compared to 2016. This change was mainly caused by increase in fuel prices.

Freight car rental expenses

General description

Freight car rental expenses represent short-term rent expenses derived from the usage of other railways' railcars by the Group, for which it is charged a daily fee. This expense counters the freight car rental revenue. The expense is based on CHF tariffs and thus is tied to the GEL/CHF exchange rate and the amount of cargo GR transports using other railways' railcars.

Freight car rental expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Freight car rental expenses	4,095	4,407	-7.1%	-312

Freight car rental expenses for Q4 2017 increased by 90 percent, compared to Q4 2016 and by 92 percent, compared to Q3 2017.

Factors influencing changes

Despite the appreciation of CHF against GEL by about 6 percent in 2017 compared to 2016, freight car rental expenses decreased by 7 percent (GEL 0.3 million). This decrease was largely driven by a fall in freight volumes and by reduced usage of Azerbaijani tank cars By GR.

Logistical services

General description

Expenses for logistical services refer to operating expenses relating to transportation and other logistics-related services of GR's subsidiaries, which are operating in freight forwarding and logistics fields.

Logistical services

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Logistical services	12,996	14,270	-8.9%	-1,274

Expenses for logistical services for Q4 2017 decreased by 8 percent, compared to Q4 2016 but increased by 37 percent, compared to Q3 2017.

Factors influencing changes

Expenses for logistical services in 2017 decreased by 9 percent (GEL 1.3 million) compared to 2016. The decrease was mainly caused by reduced expenses of GR's subsidiary that mainly serves crude oil and oil products transported by the Company.

Security and other operating expenses

General description

Security expenses mainly comprise the Group's buildings, depots and station protection expenses.

Other operating expenses mainly consist of items such as communication, legal costs, consulting services, membership fees, rent expenses and advertising expenses.

Security and other operating expenses are mostly denominated in GEL and are mainly fixed.

Security and other operating expenses

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Security	8,918	8,928	-0.1%	-10
Other op. expenses	18,818	9,589	96.3%	9,229
Total	**27,734**	**18,517**	**49.8%**	**9,218**

Security and other operating expenses for Q4 2017 increased by 236.6 percent, compared to Q4 2016 and decreased by 51.4 percent, compared to Q3 2017.

Factors influencing changes

49.8 percent increase in security and other operating expenses in 2017, compared to 2016, was caused by increase in other operating expenses, specifically increase in other tax expenses, which occurred by difference of accounting and tax cards by GEL 7.8 million. Security expenses have remained at about the same level.

Taxes other than income tax

General description

Land taxes are determined by the municipalities in which the land is located, while property taxes are calculated at 1 percent of the average book value of the asset. Railway infrastructure assets, such as rail lines, are exempt from property tax.

Taxes other than income tax

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Property tax	14,122	14,086	0.3%	36
Land tax	11,821	11,248	5.1%	572
Other taxes*	1,100	1,141	-3.6%	-41
Total	**27,043**	**26,474**	**2.2%**	**569**

** Other taxes also include all subsidiaries' taxes (other than income tax).*

Taxes other than income tax for Q4 2017 increased by 3.1 percent, compared to Q4 2016 and decreased by 11.7 percent, compared to Q3 2017.

Factors influencing changes

The increase in property tax by 0.3 percent during 2017, compared to 2016 was largely driven by the implementation of the Modernization Project, but it was offset by tax reduction on property and land because of impairment loss incurred in 2017. Property tax will be reduced after the Modernization Project is put into operation, as railway-related assets are free from property tax, and assets under the project are taxed by property tax while under construction.

Impairment loss on property, plant and equipment

Impairment loss on property, plant and equipment

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Impairment loss on property plant and equipment	-382,616	0	NA	-382,616

Factors influencing changes

In June 2013, the Group announced a decision to redesign the Tbilisi Bypass Project. The Group held negotiations with the Government of Georgia and with the main third party construction companies to agree a plan for the conservation of the Project for the period of redesigning. All construction works in progress were substantially completed by the end of October 2013 and further construction was suspended. No borrowing costs are capitalised since October 2013.

In March 2014, the Government of Georgia decided that the suspension of the construction of Tbilisi Bypass Project will last for 18 months until the final modified project is presented.

During 2016 and 2015, the Group was in discussion with the Tbilisi City Hall and the Government of Georgia about various scenarios of completing the Project. One of the scenarios under discussion included an option envisaging a change of the original bypass location, because of which the existing bypass infrastructure may become redundant. The alternative scenarios also included the determination of the future use of the existing infrastructure, should it become redundant. The options of future use of the infrastructure were bypass automobile road, light rail/extension of the Tbilisi Metro System, freight depot, etc., however, as at 31

December 2017, no decision was made by the Government of Georgia about the redesign of the Tbilisi Bypass Project.

Due to significant uncertainties associated with either the continuation of the existing project or implementation of any other scenarios, envisaging the change in the existing use of the Project, and also considering the fact that the Management does not expect that the Project will generate any future economic benefit to the Group either individually, or in combination with other non-current assets, the carrying value of the Project was written-down to its recoverable amount.

As a result, the carrying amount of the Project of GEL 397,305,000 was determined to be higher than its recoverable amount of GEL 14,689,000 and the respective impairment loss of GEL 382,616,000 was recognized in the impairment loss during 2017.

Impairment loss on property, plant and equipment is a non-cash expense and thus, is not included in the calculation of EBITDA. On the contrary, it reduces the net book value of PP&E, thus, property tax (calculated as 1% of average net book value) is reduced. In 2017, saving of GEL 1.8 million was made in property tax, accordingly increasing EBITDA by the same amount. Property tax saving effect will double in 2018.

1.5 Finance income and cost

General description

Finance income of the Group mainly consists of interest income, which represents the interest accrued on the Group's cash balances and foreign exchange gains.

Finance cost mainly consists of interest expenses and foreign exchange losses. Some of the Group's interest expenses are capitalized, as the Group's main debt obligations were issued in order to finance capital projects (Modernization and Tbilisi Bypass). Thus, until the projects are in the construction phase, part of the interest accrued is capitalized in accordance with International Financial Reporting Standards (IFRS).

The main source of FX gain or loss is the Group's Eurobonds, which are denominated in USD. This is, however, partly countered by the Group's USD cash balances and receivables in foreign hard currencies. It must be noted that such FX gain or loss on Eurobonds is not monetary in nature and will not be realized until maturity. The Group's revenues are mostly denominated in hard currencies, (81 percent in USD and 4 percent in CHF, based on 2017 revenue). As most of the tariffs are set in USD, the Group's revenue creates a natural economic hedge against foreign exchange fluctuations.

Finance income and cost

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Interest income	17,793	23,882	-25.5%	-6,089
Impairment loss on trade receivables	-39,330	-7,972	393.4%	-31,358
Impairment loss on issued loans	-23,502	0	N/A	-23,502
Interest expenses	-53,433	-52,822	1.2%	-611
FX gain/loss	25,488	-112,309	-122.7%	137,797
Total	**-72,984**	**-149,221**	**-51.1%**	**76,237**

Factors influencing changes

Net financial loss in 2017 decreased by 44 percent (GEL 65.4 million) compared to the previous year. This was mainly caused by FX gain of GEL 25.5 million in 2017, compared to FX loss of GEL 112.3 million in 2016.

Lower interest income by GEL 6.1 million in 2017, compared to 2016, was mainly due to lower average cash balances and lower interest rates. In addition, in 2016, GR received interest income from the loan provided to the state controlled entity by the end of 2015, which was fully repaid during 2016.

GEL 31.3 million increase in impairment loss on trade receivables was mainly caused by provision of GEL 27.1 million made against the VAT receivable from the Government, created as a result of the land plots transfer transaction.

Impairment loss on issued loans of GEL 23.5 million in 2017 represents provision made against loan provided to the entity managed by the group.

Higher interest expense during 2017, compared to 2016, was due to additional borrowing of USD 20.3 million to finance new passenger trains procurement and depreciation of GEL against USD by 6 percent.

GEL/USD exchange rate fluctuation has significant effect on net finance income/(cost). Due to GEL appreciation against USD by 2 percent as at 31 December 2017 compared to 31 December 2016 (GEL/USD exchange rate 2.59 versus 2.65), the Group experienced net foreign exchange gain of GEL 25.5 million, however due to depreciation of GEL against USD by 10 percent as at 31 December 2016 compared to 31 December 2015 (GEL/USD exchange rate 2.65 versus 2.39), the Group showed net foreign exchange loss of GEL 112.3 million.

1.6 Income tax expense/benefit

General description

In May 2016, the Parliament of Georgia adopted amendments to the Tax Code of Georgia. The new tax code is effective from 1 January 2017. According to the new tax code, previously active profit tax regulation was changed to so-called "tax on distributed profits" model.

Income tax expense/benefit

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Current tax expense				
Current year	-648	-5,532	-88.3%	4,884
Deferred tax benefit				
Change in recognized temporary differences (due to change in legislation)	0	44,391	-100.0%	-44,391
Total	**-648**	**38,859**	**-101.7%**	**-39,507**

Factors influencing changes

The changes in tax legislation lead to the termination of deferred tax accruals. As a response, GR reversed deferred tax assets and liabilities in profit or loss statement, causing GEL 44.4 million deferred tax benefit in 2016.

2. Balance Sheet

2.1 Non-current assets

Non-current assets

As at 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Property, plant and equipment	2,368,380	2,623,594	-9.7%	-255,214
Other non-current assets	123,562	147,565	-16.3%	-24,003
Loan receivable	18,113	35,717	-49.3%	-17,604
Total	**2,510,055**	**2,806,876**	**-10.6%**	**-296,821**

Factors influencing changes

Property, plant and equipment – A GEL 255.2 million decrease in property, plant and equipment in 2017, compared to 2017, was mainly due to the impairment of Tbilisi Bypass Project.

Loan receivable - In 2016, the Group issued long-term loans amounting in total to USD 14.5 million. The loans were issued in USD, at market rates. USD 6 million was provided to the shareholder. USD 8.5 million was issued in 2016 to the owner of liquid cargo terminals on the Black Sea, which is under the management of the Group. The provision was made against this amount in 2017.

2.2 Current assets

Current assets

As at 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Inventories	32,807	29,752	10.3%	3,055
Loan receivable	0	3,974	-100.0%	-3,974
Tax assets	2,360	7,129	-66.9%	-4,769
Trade and other receivables	73,614	99,649	-26.1%	-26,035
Prepayments and other current assets	383	350	9.5%	33
Cash and cash equivalents	243,018	277,953	-12.6%	-34,935
Total	**352,182**	**418,807**	**-15.9%**	**-66,625**

Factors influencing changes

Loan receivable - Loan receivables as at the end of 2016 represent the current portion of the loans issued in 2016 and provided to the entity managed by the group, against which the provision was made in 2017.

Trade and other receivables – Out of the total decrease of GEL 26.0 million, a decrease of GEL 27.1 million in 2017 was driven by provision made against the VAT receivable from the Government, created as a result of the land plots transfer transaction.

2.3 Equity

Equity

As at 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Share capital	1,053,271	1,053,004	0.0%	267
Non-cash owner contribution reserve	98,192	98,312	-0.1%	-120
Retained earnings	93,385	447,960	-79.2%	-354,575
Total	**1,244,848**	**1,599,276**	**-22.2%**	**-354,428**

There was a GEL 354.4 million decrease in total equity in 2017 compared to the previous year. This decrease was mainly due to the impairment cost incurred by impairment of Tbilisi Bypass Project.

2.4 Non-current liabilities

Non-current liabilities

As at 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Loans and borrowings	1,374,363	1,361,602	0.9%	12,761
Advances received from the Government	46,594	73,809	-36.9%	-27,215
Total	**1,420,957**	**1,435,411**	**-1.0%**	**-14,454**

Factors influencing changes

Loans and borrowings - In 2016, the Group raised funds through export credit to finance the acquisition of four new passenger trains, two of which were delivered in 2016, other two in 2017 and are currently in operation. The total credit facility was USD 43.7 million. GEL 42.8 million at the end of 2016 and GEL 80.3 million at the end of 2017 was classified as non-current loans and borrowings. The remainder, GEL 1,294,069 million of non-current loans and borrowings at 31 December 2017, represents Eurobonds maturing in 2022.

Eurobonds and Export credit facility

For the year ended 31 December

Type	Date of maturity	Amount (in mln)	Currency	Coupon/percent	Payments
Eurobonds	11-Jul-22	500.0	USD	7.75%	Semi-annually
Export credit facility	10-Nov-26	39.2	USD	LIBOR+1.25%	Semi-annually

Advances received from the Government – These decreased, mainly due to land plots transfer transaction, mentioned in subheading 1.2 ''Income from transferred property''.

2.5 Current liabilities

Current liabilities

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Loans and borrowings	58,809	57,172	2.9%	1,637
Trade and other payables	112,221	109,638	2.4%	2,583
Liabilities to the Government	7,592	8,399	-9.6%	-807
Provisions	7,953	8,547	-6.9%	-594
Other current liabilities	9,857	7,240	36.1%	2,617
Total	**196,432**	**190,996**	**2.8%**	**5,436**

Factors influencing changes

Loans and borrowings – Currently, the Group has two debts, Eurobonds and a secured loan, obtained for the sole purpose of the acquisition of passenger trains. As at 31 December 2017, current loans and borrowings include interest payable of about GEL 47.1 million and current portion of long-term borrowing, GEL 11.7 million, which was raised for financing new passenger trains. GEL 1.6 million increase in current loans and borrowings was caused by withdrawal of additional amount of loan in 2017, which was partly offset by appreciation of GEL against USD as at balance sheet dates by 2.1 percent, which caused revaluation of debt, as the Group's debts are denominated in USD.

Trade and other payables - In 2017, trade and other payables increased by 2 percent (GEL 2.6 million). The main contributor to this increase was increase in payables for the Modernization Project, which was partly offset by reduction in payables for new passenger trains acquired.

3. Cash flow statement

By the end of 2017, the Group held GEL 243.0 million of cash and cash equivalents. These cash resources are held to support existing and future capital expenditures. Capital expenditures mainly entail the Modernization Project and the Tbilisi Bypass Project. Works on the Modernization Project continued in 2017, while the Tbilisi Bypass Project remained suspended.

The Group can also rely on its available credit lines of about GEL 158.8 million as at the end of 2017.

The Group mainly relies on its operating activities in order to fund its future cash requirements.

3.1 Operating activities

Operating activities

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Cash receipts from customers	447,510	456,742	-2.0%	-9,232
Cash paid to suppliers and employees	-268,592	-264,102	1.7%	-4,490
Income tax paid	-2,685	-5,229	-48.7%	2,544
Net cash from operating activities	**176,233**	**187,411**	**-6.0%**	**-11,178**

Factors influencing changes

Net cash from operating activities decreased by GEL 2.8 million in 2017, compared to 2016. This change was driven by a decrease in cash receipts from customers by GEL 9.2 million, mainly due to the decreased transportation volume.

3.2 Investing activities

Investing activities

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Acquisition of property, plant and equipment	-165,265	-200,274	-17.5%	35,009
Proceeds from sale of property, plant and equipment	5,133	3,350	53.2%	1,783
Interest received	14,806	22,435	-100.0%	-7,629
Issuance of loans	0	-32,563	-100.0%	32,563
Repayment of issued loans	0	37,838	-100.0%	-37,838
Dividends received	0	1,075	-100.0%	-1,075
Net cash used in investing activities	**-145,327**	**-168,139**	**-13.6%**	**22,812**

Factors influencing changes

Cash paid for the acquisition of property, plant and equipment in 2017 decreased by GEL 35.0 million compared to 2016, which was mainly due to decreased capital expenditures on Modernization Project (GEL 91.5 million in 2017, compared to GEL 108.9 million in 2016). Modernization project is planned to be finished at the end of 2019. Another large component was cash paid for procurement of four new passenger trains (two of them in 2016 and another two in 2017) from Suisse manufacturer (GEL 50.2 million and GEL 42.3 million in 2017 and 2016, respectively).

The decrease in interest received was mainly due to lower average cash balance held by the Group and lower interest rates during the period under review, compared to the same period of the previous year.

Issuance of loans (GEL 32.6 million) in 2016 represent USD 6 million provided to the parent company and USD 8.5 million provided to the owner of a liquid cargo terminal on the Black Sea.

Repayment of the issued loans (GEL 37.8 million) mainly comprises the collection of a short-term loan (USD 16 million) that the Group provided to a state-controlled entity by the end of 2015 and the partial collection of the principal due from the loan provided to the owner of a liquid cargo terminal on the Black Sea.

3.3 Financing activities

Financing activities

For the year ended 31 December *In GEL '000*

	2017	2016	% Change	Abs. change
Interest paid	-103,127	-91,948	12.2%	-11,179
Dividends paid	0	-1,607	-100.0%	1,607
Repayment of borrowings	-10,996	0	NA	-10,996
Proceeds from borrowings	50,248	42,349	18.7%	7,899
Net cash used in financing activities	**-63,875**	**-51,206**	**24.7%**	**-12,669**

Factors influencing changes

Higher interest paid in 2017, compared to 2016, was mainly due to the interest paid on loan for passenger trains, which was borrowed to finance new passenger trains and depreciation of GEL against USD, as the Group's debts are denominated in USD.

Repayment of borrowings of GEL 11.0 million represents the amount paid for current portion of the loan acquired for new passenger trains.

Proceeds from borrowings of GEL 50.2 million represents the loan for financing the purchase of the new passenger trains.

Appendix

Appendix 1

Breakdown of freight transportation in tons

For the year ended 31 December *In million tons*

	2017	2016	% Change	Abs. change
Liquid cargoes	**4.3**	**5.5**	**-20.9%**	**-1.1**
Oil products	3.9	3.7	7.1%	0.3
Crude oil	0.4	1.8	-77.8%	-1.4
Dry cargoes	**6.3**	**6.4**	**-1.0%**	-0.1
Ores	1.4	1.5	-2.1%	-0.0
Grain	0.3	0.4	-32.5%	-0.1
Ferrous metals and scrap	0.5	0.7	-20.2%	-0.1
Sugar	0.4	0.5	-24.2%	-0.1
Chemicals and fertilizers	0.6	0.4	31.8%	0.1
Construction freight	1.2	1.1	8.6%	0.1
Industrial freight	0.3	0.3	11.7%	0.0
Cement	0.1	0.1	53.2%	0.0
Other	1.6	1.5	5.1%	0.1
Total	**10.7**	**11.9**	**-10.2%**	**-1.2**

Appendix 2

Breakdown of freight transportation in ton-kilometers

For the year ended 31 December

In million ton-kilometers

	2017	2016	% Change	Abs. change
Liquid cargoes	**1,379**	**1,802**	**-23.5%**	**-423**
Oil products	1,221	1,088	12.3%	133
Crude oil	158	714	-77.9%	556
Dry cargoes	**1,551**	**1,589**	**-2.4%**	**-38**
Ores	296	311	-4.6%	-14
Grain	75	141	-46.4%	-65
Ferrous metals and scrap	123	163	-24.3%	-40
Sugar	135	184	-26.7%	-49
Chemicals and fertilizers	184	133	38.8%	52
Construction freight	160	142	12.4%	18
Industrial freight	53	39	35.8%	14
Cement	22	17	30.9%	5
Other	502	461	9.0%	42
Total	**2,930**	**3,391**	**-13.6%**	**-461**

Appendix 3

Calculations of ratio of Net Financial Indebtedness to EBITDA:

'000 GEL	Twelve-month period ended 31-Dec-17	Twelve-month period ended 31-Dec-16
Revenue	434,534	439,922
Income from the transferred property	23,417	80,294
Other income	15,560	19,122
Impairment loss on property, plant and equipment	-382,616	
Employee benefits expenses	-148,300	-146,626
Depreciation and amortization expense	-109,703	-106,267
Electricity, consumables and maintenance costs	-41,490	-47,289
Other expenses	-71,869	-63,668
Results from operating activities	**-280,467**	**175,488**
Finance income	43,281	23,882
Finance costs	-116,265	-173,103
Net finance costs	**-72,984**	**-149,221**
Profit/(loss) before income tax	**-353,451**	**26,267**
Income tax benefit	-648	38,859
Profit/(loss)and total comprehensive income/(loss) for the year	**-354,099**	**65,126**
Results from operating activities	**-280,467**	**175,488**
Depreciation add-back	109,703	106,267
Impairment loss on property, plant and equipment add-back	382.616	0
EBITDA	**211,852**	**281,755**
Net Financial Indebtedness:		
Financial Indebtedness	1,433,172	1,418,774
less:		
Available Credit Facilities	158,833	161,400
Cash	243,018	277,953
Net Financial Indebtedness:	**1,031,321**	**979,422**
Net Financial Indebtedness/EBITDA	**4.87**	**3.48**