Georgian Railway LLC

Transitional Consolidated
Financial Statements
For the Year Ended 31 December 2007

GEORGIAN RAILWAY LLC

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GEORGIAN RAILWAY LLC

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE TRANSITIONAL CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2007

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the special purpose independent auditors' report set out on pages 2-4, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the transitional consolidated financial statements of Georgian Railways LLC and its subsidiaries (collectively, the "Group").

Management is responsible for the preparation of the transitional consolidated financial statements that present fairly the financial position of the Group at 31 December 2007, the results of its operations and changes in equity for the year then ended, in accordance with the basis of accounting set out in Note 2.

In preparing the transitional consolidated financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether the basis of accounting set out in Note 2 has been followed, subject to any material departures disclosed and explained in the transitional consolidated financial statements; and
- Preparing the transitional consolidated financial statements on a going concern basis, unless it is inappropriate;
  to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Group, and which enable them to ensure that the transitional consolidated financial statements of the Group comply with the basis of accounting set out in Note 2;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of Georgia;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Detecting and preventing fraud, errors and other irregularities.

The transitional consolidated financial statements for the year ended 31 December 2007 were authorised for issue on 7 December 2009 by the management board.

On behalf of the Management Board:

General Director
Irakli Ezugbaia

Acting Chief Accountant
Amiran Tevzadze

Deloitte.

Deloitte & Touche LLC
36 a Lado Asatiani Street
Tbilisi, 0105
Georgia

Tel: +995 32 24 45 66
Fax: +995 32 24 45 69
www.deloitte.ge

SPECIAL PURPOSE INDEPENDENT AUDITORS' REPORT

To the management of Georgian Railway LLC:

We have audited the accompanying transitional consolidated financial statements of Georgian Railway LLC (the "Company") and its subsidiaries (the "Group"), which comprise the transitional consolidated balance sheet as of 31 December 2007 and the related transitional consolidated income statement, transitional consolidated statements of changes in equity, transitional consolidated statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditor's responsibility

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

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

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

Deloitte.

Basis for qualified opinion

Effects from lack of physical observance of inventory and associated tax effects

We did not observe the counting of physical inventories as of 31 December 2006, since this date was prior to the time we were initially engaged as auditors for the Group. Owing to the nature of accounting records of the Group, we were not able to satisfy ourselves as to the inventory quantities by other audit procedures. As a result, we were also unable to satisfy ourselves to the accuracy and completeness of the related materials of GEL 24,662 thousand and fuel of GEL 9,530 thousand included in raw materials and consumables used and their associated tax effects including such taxes as refundable VAT included in prepayments and other current assets and income tax expense/benefit in the income statement or current income tax payable in the balance sheet as of and for the years ended 31 December 2007 and 2006.

Deferred taxes

Management recorded deferred tax effects cumulatively for all prior years through retained earnings at 1 January 2007. We were unable to determine the portion of such recording which should have been posted to deferred tax expense/benefit for the year ended 31 December 2006 and therefore were unable to satisfy ourselves as to the appropriateness of the amount recorded as deferred tax expense/benefit for the year ended 31 December 2006.

Depreciation expense

Management recorded its adjustment to "deemed cost" for property, plant and equipment as defined under IFRS 1 "First-time Adoption of International Financial Reporting Standards", as of 1 January, 2007. Consequently, no allocation/adjustment was made for any depreciation expense which would have resulted from measurement and recognition of "deemed cost" as the basis for the calculation of depreciation expense for the year ended 31 December 2006. We were therefore unable to satisfy ourselves as to the appropriateness of the amount recorded as depreciation expense for the year ended 31 December 2006.

Lack of consolidation of subsidiaries

As disclosed in Note 17 the Group did not consolidate its subsidiaries in the financial statements, instead recording investments in subsidiaries in the non-current line item "Investments" on the balance sheet at their carrying value as of 31 December 2006. In our opinion, this is not in accordance with IAS 27 "Consolidated and Separate Financial Statements". Due to the nature of the accounting records of the subsidiaries, we were unable to estimate the consolidated amounts and the effect of the non-eliminated balances and transactions on the Group's financial position and results of operations as of and for the year ended 31 December 2006

Lack of equity method accounting for an associate

As disclosed in Note 17 the Group accounted for its investment in an associate at cost in the financial statements as of 31 December 2006. In our opinion, this is not in accordance with IAS 28 "Investment in Associates". Due to the nature of the accounting records of the associate, we were unable to estimate the effect on the Group's financial position and results of operations, as well as the associated disclosures, if any, as of and for the year ended 31 December 2006.

Transactions with related parties

The 2006 financial statements do not disclose the transactions with related parties as of and for the year ended 31 December 2006. Disclosure of this information is required by IAS 1 "Presentation of Financial Statements".

Prepayments

Due to the inadequacy of the accounting system and the underlying accounting records, we were unable to satisfy ourselves as to the prepaid taxes other than income taxes included in prepayments and other current assets of GEL 4,811 as at 31 December 2006.

Deloitte.

Qualified opinion

In our opinion, except for the effect of adjustments, if any, which might have been determined to be necessary had we been able to satisfy ourselves with respect to the accuracy and completeness of the related materials and fuel included in raw materials and consumables used and their associated tax effects including such taxes as refundable VAT included in prepayments and other current assets and income tax expense/benefit in the income statement or current income tax payable in the balance sheet and except for the effects on the corresponding amounts as referred to in the preceding paragraphs, the transitional consolidated financial statements present fairly, in all material respects, the transitional consolidated financial position of Georgian Railway LLC and its subsidiaries (the "Group") as of 31 December 2007, its transitional consolidated financial performance and its transitional consolidated cash flows for the year then ended in accordance with the basis of accounting set out in Note 2, which describes how IFRS have been applied in accordance with IFRS 1 "First-time Adoption of International Financial Reporting Standards", including the assumptions the management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when the management prepares its first complete set of IFRS financial statements as of 31 December 2008.

Emphasis of matter – transition to IFRS and corresponding data

Without further qualifying our opinion, we draw your attention to the fact that the Group has adopted 1 January 2007 as its transition date to IFRS.

Note 2 describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as of 31 December 2008.

Note 2 explains why there is a possibility that these consolidated financial statements may require adjustments before constituting the first complete set of IFRS financial statements. Moreover, we draw attention to the fact that, under IFRS, only a complete set of financial statements comprising a balance sheet, statements of operations, changes in equity and cash flows, together with comparative financial information and explanatory notes, can provide a fair presentation of the Group's financial position, results of operations and cash flows in accordance with IFRS.

Emphasis of matter – corresponding figures

The corresponding figures as of 31 December 2006 and for the year then ended presented in these transitional consolidated financial statements had been prepared under reserved IFRS, with respect to which we have issued a report disclaiming an opinion on such financial statements dated 19 October 2009.

Emphasis of matter – various

Without qualifying our opinion further, we draw your attention to Note 4 which explains the key source of uncertainty in the valuation for tax purposes of de-installed equipment in the amount of GEL 14,585 thousand.

Without qualifying our opinion further, we draw your attention to Note 17 which explains why Chitakhevi-Borjomi JSC is no longer considered an associate of the Group under IAS 28 "Investment in Associates" and as a result is recorded in the non-current line item "Investments" on the balance sheet at cost in the amount GEL 2,021 thousand.

Deloitte & Touche

7 December 2009
Tbilisi, Georgia

TRANSITIONAL CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007

(in Georgian Lari and in thousands)

	Notes	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
CONTINUING OPERATIONS			
Revenue	6	307,457	306,888
Investment revenue	7	19,698	14,480
Other gains and losses	8	2,182	1,731
Depreciation and amortisation expense	9	(106,658)	(27,600)
Employee benefit expense	9	(105,307)	(85,073)
Raw materials and consumable used	10	(52,384)	(51,068)
Other expenses	11	(40,242)	(47,087)
Movement in provision	9	(2,476)	2,669
Finance costs	12	(792)	(1,016)
PROFIT BEFORE TAX		21,478	113,924
Income tax benefit/(expense)	13	17,706	(23,747)
PROFIT FOR THE YEAR		39,184	90,177

On behalf of the Management Board:

General Director
Irakli Ezugbaia

Acting Chief Accountant
Amiran Tevzadze

The notes on pages 11-49 are an integral part of these transitional consolidated financial statements.

GEORGIAN RAILWAY LLC

TRANSIATIONAL CONSOLIDATED BALANCE SHEET
AT 31 DECEMBER 2007
(in Georgian Lari and in thousands)

	Notes	31 December 2007	31 December 2006 Reserved IFRS
ASSETS			
Non-current assets			
Property, plant and equipment	14	1,635,190	1,265,890
Investment property	15	13,247	9,466
Other non-current assets	16	7,288	1,760
Investments	17	2,021	35,040
Total non-current assets		1,657,746	1,312,156
Current assets			
Cash and cash equivalents	18	4,211	21,557
Restricted cash	19	9,868	4,073
Trade and other receivables, net	20	7,968	11,037
Prepayments and other current assets	21	33,178	24,882
Inventories	22	27,858	27,389
Investments	17	-	2,100
Total current assets		83,083	91,038
TOTAL ASSETS		1,740,829	1,403,194
LIABILITIES AND EQUITY			
Capital and reserves			
Charter capital	23	935,588	586,481
Land Fund	23	9,397	-
Revaluation reserves	25	-	916,057
Retained earnings		484,332	(196,597)
Total Equity		1,429,317	1,305,941
Non-current liabilities			
Deferred tax payable	13	106,526	-
Borrowings	27	7,068	11,413
Total non-current liabilities		113,594	11,413

The notes on pages 11-49 are an integral part of these transitional consolidated financial statements.

TRANSITIONAL CONSOLIDATED BALANCE SHEET (CONTINUED)
AT 31 DECEMBER 2007
(in Georgian Lari and in thousands)

	Notes	31 December 2007	31 December 2006 Reserved IFRS
Current Liabilities			
Liability to the owners	28	32,389	28,965
Current portion of borrowings	27	3,832	4,215
Provisions	29	7,414	6,597
Trade payables and advances received	30	32,711	27,170
Current income tax payable	32	2,201	9,832
Other taxes payable	31	13,466	2,897
Other liabilities	33	105,905	6,164
Total current liabilities		197,918	85,840
TOTAL LIABILITIES		311,512	97,253
TOTAL EQUITY AND LIABILITIES		1,740,829	1,403,194

On behalf of the Management Board:

General Director
Irakli Ezugbaia

Acting Chief Accountant
Amiran Tevzadze

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TRANSITIONAL CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31 DECEMBER 2007

(in Georgian Lari and in thousands)

	Notes	Charter capital	Land fund	PPE revaluation reserve	Investment property revaluation reserve	Retained earnings	Total
Balance at 31 December 2005		**362,764**	**-**	**-**	**-**	**53,169**	**415,933**
Profit for the period		-	-	-	-	90,177	90,177
Revaluation Gain		-	-	910,143	5,914	-	916,057
Retained earnings	26	199,838	-	-	-	(199,838)	-
Net contribution to capital		23,879	-	-	-	-	23,879
Restatement of impairment		-	-	-	-	(134,255)	(134,255)
Dividends		-	-	-	-	(5,850)	(5,850)
Balance at 31 December 2006		**586,481**	**-**	**910,143**	**5,914**	**(196,597)**	**1,305,941**
Correction of deferred tax	5	-	-	(159,629)	(1,894)	14,967	(146,556)
Recognition of deemed cost	5	-	-	(750,514)	(4,020)	754,534	-
Balance at 1 January 2007		**586,481**	**-**	**-**	**-**	**572,904**	**1,159,385**

The notes on pages 11-49 are an integral part of these transitional consolidated financial statements.

TRANSITIONAL CONSOLIDATED STATEMENT OF CHANGES IN EQUITY(CONTINUED)
FOR THE YEAR ENDED 31 DECEMBER 2007

(in Georgian Lari and in thousands)

	Notes	Charter capital	Land fund	PPE Revaluation Reserve	Investment property Revaluation Reserve	Retained earnings	Total
Profit for the period		-	-	-	-	39,184	39,184
Net contribution to capital	23	333,451	9,397	-	-	-	342,848
Retained earnings capitalisation	26	15,656	-	-	-	(15,656)	-
Dividends declared	24	-	-	-	-	(112,100)	(112,100)
Balance at 31 December 2007		**935,588**	**9,397**	**-**	**-**	**484,332**	**1,429,317**

In 2007 the Company declared dividends of GEL 112,100 thousand (2006: GEL 5,850 thousand). The dividends were paid to Georgian Government throughout the year, refer Note 24.

On behalf of the Management Board:

General Director
Irakli Ezugbaia

Acting Chief Accountant
Amiran Tevzadze

The notes on pages 11-49 are an integral part of these transitional consolidated financial statements.

GEORGIAN RAILWAY LLC

TRANSITIONAL CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2007

(in Georgian Lari and in thousands)

	Year ended 2007	Year ended 2006 Reserved IFRS
OPERATING ACTIVITIES:		
Cash receipts from customers	338,572	343,589
Cash paid to suppliers and employees	(209,881)	(216,988)
Cash generated by operations	128,691	126,601
Income tax paid	(32,161)	(26,381)
Interest paid	(934)	(1,029)
Net cash generated by operating activities	95,596	99,191
INVESTING ACTIVITIES:		
Proceeds from investments	2,634	-
Purchase of investments	-	(2,100)
Interest received	1,658	3,107
Dividends received	181	36
Purchase of property, plant and equipment	(95,846)	(75,036)
Net cash used in investing activities	(91,373)	(73,993)
FINANCING ACTIVITIES:		
Increase in restricted cash	(5,795)	(4,073)
Dividends paid	(12,450)	(5,500)
Repayment of borrowings	(3,749)	(3,971)
Net cash used in financing activities	(21,994)	(13,544)
NET INCREASE IN CASH AND CASH EQUIVALENTS	(17,771)	11,654
CASH AND CASH EQUIVALENTS, beginning of year	21,557	10,908
Effects of exchange rate changes on the balance of cash held in foreign currencies	425	(1,005)
CASH AND CASH EQUIVALENTS, end of year	4,211	21,557

On behalf of the Management Board:

General Director
Irakli Ezugbaia

Acting Chief Accountant
Amiran Tevzadze

The notes on pages 11-49 are an integral part of these transitional consolidated financial statements.

(in Georgian Lari and in thousands)

1. GENERAL INFORMATION AND DESCRIPTION OF BUSINESS

These transitional consolidated financial statements include the financial statements of Georgian Railways LLC (the "Company") and its subsidiaries (collectively, the "Group").

Limited Liability Company "Georgian Railway" was incorporated in Georgia on 8 December 1998 by the Decree of President of Georgia # 929 as entity engaged in provision of railway transportation services in Georgia.

The legal address of the Company is: 15 Queen Tamar Avenue, Tbilisi 0112, Georgia.

The Company is fully owned by the State of Georgia represented by the State Enterprise Management Agency.

The Company operates the nationwide railway system providing freight and passenger traffic, maintenance of railway infrastructure and construction of railway lines within Georgia.

The Company controls a number of entities operating in Georgia. These entities are consolidated subsidiaries for the purposes of reporting under International Financial Reporting Standards ("IFRS").

These entities as at 31 December 2007 and 2006 were as follows:

Name	Legal form	Nature of business	Ownership interest	
			2007	2006
Railway Telecom	LLC	Communication	100%	100%
Refrigerated and Isothermal Transportation Company	LLC	Transportation	100%	100%
Sak Rkinigza Project	LLC	Construction	100%	100%
Mikheil Meskhi Stadium	LLC	Sport	-	100%
Reinforced Concrete Tie Factory	LLC	Manufacturing	-	100%
Chkhenisi Crushed Stone Factory	LLC	Manufacturing	-	100%
Public Clinical Hospital	LLC	Medical	-	100%
Tbilisi Cross Melding Factory	LLC	Manufacturing	-	100%

The Company discontinued several immaterial subsidiaries in 2007.

The Group employed approximately 15 thousand employees in 2007 and 2006, respectively.

Pricing policy

Railroad transportations in Georgia is a natural monopoly, however the pricing policy is not subject to government regulation: according to the 64th clause (came into force on 1st July 2005) of Railway Code of Georgia, government of Georgia has delegated "Georgian Railway" LLC to set up the pricing policy independently for all types of services provided, including freight transportation, freight transportation related additional services, passenger and luggage transportation.

A. Tariffs for freight transportation and related additional services

Tariffs for freight transportation are based on the International Rail Transit Tariff. Georgian Railway is the co-signatory of Tariff Agreement (concluded on 17 February 1993) together with CIS and Estonian railways. The member parties of the agreement hold annual conferences to work out the tariff policy for the next year: each party declares tariffs denominated in Swiss Francs for railway transportation and states general rules that apply to and modify tariffs. Mentioned tariffs indicate maximum level. Based on the shared information and decisions made on the conference Georgian Railway establishes the pricing policy for the next year that is published on the official web site of the Company.

According the pricing policy of the company local and international freight (import, export, transit) transportation tariffs and related additional service fees are based on unified base parameters.

During 2007 base tariffs for freight transportation and related additional services (except fees for station service above 24 hour, that were stated in Georgian Lari and annual revenue of which amounts to 5% of total freight revenue) were stated in US Dollar by converting Swiss Franc at the last three months CHF/USD average exchange rate of the previous year.

According to the Georgian Legislation, residents of the country must pay in national currency – Georgian Lari, but non-residents are allowed to pay in foreign currencies: USD, Euro, Pound Sterling or Swiss Franc. Georgian resident clients of the company pay in national currency at the actual USD/GEL exchange rate established by the National Bank of Georgia every business day.

B. Tariffs for transportation of passengers and luggage

Pricing policy for passenger transportation and luggage as well as for freight transportation fees is not subject to government regulation.

Tariffs for domestic transportation of passengers and luggage

Tariffs for domestic transportation of passengers and luggage are prescribed by Decrees approved by the General Director of the Georgian Railway,

Tariffs are denominated in Georgian Lari.

Tariffs for international transportation of passengers and luggage

International tariff base for CIS countries are determined by the CIS Rail Transport Tariffs Conference; tariffs for non-CIS countries ("East-West" tariffs) are determined by specific international agreements.

All tariffs are denominated in Swiss Franc.

2. IFRS FIRST TIME ADOPTION AND ADOPTION OF NEW AND REVISED STANDARDS

Before 1 January 2007 the Group's management was unable to make a statement of unreserved compliance with International Financial Reporting Standards ("IFRS").

The Group takes IFRS as a base for its transitional consolidated financial statements preparation. With this purpose the Group prepared its opening balance sheet as of 1 January 2007 ("the date of full transition to IFRS") in accordance with the requirements of IFRS 1, "First-time Adoption of International Financial Reporting Standards". This standard requires that the opening balance sheet as of the date of transition to IFRS be prepared in accordance with accounting policies that comply with each IFRS effective as of the date of preparation of the first complete set of IFRS consolidated financial statements. The first complete set of consolidated financial statements of the Group in accordance with IFRS comprising the balance sheet, respective income statement, statements of cash flows and changes in equity, as well as comparative information for the previous year, will be prepared for the year ending 31 December 2008.

The accompanying transitional consolidated financial statements have been prepared in accordance with the requirements of all IFRSs, International Accounting Standards ("IAS") and Interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") which has been issued and effective or issued and early adopted at the time of preparing these transitional consolidated financial statements. There is a possibility that the Group will have to adjust amounts stated in the accompanying transitional consolidated financial statements in order to comply with requirements of all IFRS that will be issued and effective as of 31 December 2008, i.e. till the date of preparation of the first complete consolidated financial statements in accordance with IFRS.

Reconciliation and descriptions of the effect of transition to IFRS are presented in note 5.

At the date of authorisation of these transitional consolidated financial statements, the following Standards and Interpretations were in issue but not yet effective:

- IFRS 3 (Revised) Business Combinations (effective for annual periods beginning on or after 1 July 2009);
- IFRS 8 Operating Segments (effective for annual periods beginning on or after 1 January 2009);
- IFRS 9 Financial Instruments (effective for annual periods beginning on or after 1 January 2013);
- IAS 1 (Revised) Presentation of Financial Statements (effective for annual periods beginning on or after 1 January 2009);
- IAS 23 (Revised) Borrowing Costs (effective for annual periods beginning on or after 1 January 2009);
- IAS 24 (Revised) Related Party Disclosures (effective for annual periods beginning on or after 1 January 2011);
- IAS 27 (Revised) Consolidated and Separate Financial Statements (effective for annual periods beginning on or after 1 July 2009);
- IFRIC 11: IFRS 2: Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 13 Customer Loyalty Programmes (effective for annual periods beginning on or after 1 July 2008);
- IFRIC 14: IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for annual periods beginning on or after 1 January 2008);
- IFRIC 15: Agreements for the Construction of Real Estate (effective for annual periods beginning on or after 1 January 2009);
- IFRIC 16: Hedges of a Net Investment in a Foreign Operation (effective for annual periods beginning on or after 1 October 2008);
- IFRIC 17: Distributions of Non-cash Assets to Owners (effective for annual periods beginning on or after 1 July 2009);
- IFRIC 18: Transfer of Assets from Customers (effective for annual periods beginning on or after 1 July 2009).

The management anticipates that the adoption of these Standards and Interpretations in future periods will have no material effect on the consolidated financial statements of the Group.

3. SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The transitional consolidated financial statements, hereafter "consolidated financial statements" have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Basis of preparation

The consolidated financial statements have been prepared on the historical cost and accrual basis. The principal accounting policies are set out below.

The Group maintains its accounting records in accordance with the Georgian tax code. Georgian tax code accounting principles differ from IFRS. Accordingly, the accompanying consolidated financial statements, which have been prepared from the Group's accounting records, reflect adjustments necessary for such consolidated financial statements to be presented in accordance with IFRS.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.
Where necessary, adjustments are made to the consolidated financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Revenue recognition

Revenues are recognised when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of revenues can be measured reliably.

Revenues are accounted for at the time the actual flow of related goods and services occurs and transfer of risks and rewards has been completed, regardless of when cash or its equivalent is received or paid, and are reported in the statement of operations in the period to which they relate.

Revenue related to international freight and passenger transportations is recognised when the border of Georgia is been crossed.

For the services related to freight transportation, revenue is recognised upon completion of the respective services.
Revenues are measured at the fair value of the consideration received or receivable.

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

Operating leases

The Group as a lessor

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and charged on a straight-line basis over the lease term.

The Group as a lessee

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

Property, plant and equipment

Land and buildings held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet at their deemed cost, less any subsequent accumulated depreciation. Depreciation on buildings is charged to profit or loss. Freehold land is not depreciated.

Properties in the course of construction for production or for purposes not yet determined, are carried at cost. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Fixtures and equipment are stated at cost less accumulated depreciation.

Depreciation is charged so as to write off the deemed cost of assets, other than freehold land and properties under construction, over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

The following depreciation rates are used:

Group of assets	**Useful life**
Buildings and construction	15 – 100
Rail Track infrastructure	20 – 90
Transport, machinery, equipment and other	5 – 40

The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

Investment property

Investment property, which is property held to earn rentals, is measured initially at its deemed cost, including transaction costs. Subsequent to initial recognition, investment property is measured at fair value. Gains and losses arising from changes in the fair value of investment property are included in profit or loss in the period in which they arise.

Equity investments

Equity investments represented by investments in subsidiaries and associate are carried in the balance sheet at cost, less any impairment in the value of individual investments.

A subsidiary is an entity controlled by the Company. Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

An associate is an entity over which the Company has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

Intangible Assets

Intangible assets acquired separately are reported at cost less accumulated amortisation and accumulated impairment losses. Amortisation is charged on a straight-line basis over their estimated useful lives. The estimated useful life and amortisation method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Cash and cash equivalents

Cash and cash equivalents include cash on hand and cash at bank. Cash equivalents include all highly liquid investments with original maturity of three months or less at the time of purchase.

Restricted cash

Restricted cash represent funded letter of credits arrangements and are separately noted in the consolidated financial statements of the Group.

Receivables and prepayments

Receivables and prepayments are stated at their nominal value as reduced by appropriate allowance for doubtful debts or irrecoverable amounts, respectively. Such allowance reflects either specific cases or estimates based on evidence of recoverability.

Inventories

Inventories are stated at the lower of cost and net realisable value. Costs, including an appropriate portion of fixed and variable overhead expenses, are assigned to inventories by the method most appropriate to the particular class of inventory, with the majority being valued on a weighted average basis.

Equity

Inputs and withdrawals of capital are based upon decrees of the Government. They are in the form of property, plant and equipment, inventory, and investments in subsidiaries. The value of the input or withdrawal of the capital is based upon the net book value of assets given or withdrawn or the net assets of subsidiaries given or withdrawn

Dividends

Dividends are declared and paid based upon the decree from the Government. Dividends decrees occur throughout the year based upon Government policy.

Borrowings

Borrowings are initially recorded at the proceeds received, net of direct issue costs. Borrowings comprise short-term and long-term loans. Finance charges are accounted for on an accrual basis and are added to the carrying amount of the borrowings to the extent that they are not settled in the period in which they arise.

Borrowing costs

Borrowing costs are charged to the income statement in the period in which they are incurred.

Provisions

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

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Payables

Payables are initially recognised at nominal value, which represents the fair value of consideration received. Subsequently, instruments with fixed maturity are re-measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any transaction costs, and any discount or premium on settlement. Financial liabilities, which do not have a fixed maturity, are subsequently carried at cost.

Corporate taxes

Income tax

Income tax expense is based on the taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated in accordance with the tax regulations of Georgia by applying the statutory tax rate of 20%. Current tax is recognised as an expense or benefit in the Statement of Operations, except when they relate to items credited or debited directly to equity, in which case the tax is also recognised directly in equity.

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Value added tax

Value added tax ("VAT") payable represents VAT related to sales payable to tax authorities upon collection of receivables from customers net of VAT on purchases which have been settled at the balance sheet date. In addition, VAT related to sales which have not been settled at the balance sheet date (VAT deferred) is also included in VAT payable. Where allowance has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT. The related VAT deferred liability is maintained until the debtor is written off for tax purposes.

VAT recoverable relates to purchases which have not been settled at the balance sheet date. VAT recoverable is reclaimable against sales VAT upon payment for the purchases.

The tax authorities permit the settlement of sales and purchases VAT on a net basis.

Financial assets

Investments are recognised and derecognised on settlement date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following specified categories: cash and cash equivalents, trade accounts receivable, short-term loans disbursed, trade and other receivables ("loans and receivables"), and Held-to-maturity investments. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments and that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Held-to-maturity investments

Bills of exchange and debentures with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis.

Impairment of financial assets

Financial assets are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Objective evidence of impairment could include:

- Significant financial difficulty of the issuer or counterparty; or
- Default or delinquency in interest or principal payments; or
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 90 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amounts of the financial assets are reduced by the impairment loss through the use of allowance accounts. When a financial asset is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralized borrowing for the proceeds received.

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- The amount of the obligation under the contract, as determined in accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets"; and

- The amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies set out above.

Financial liabilities

Financial liabilities are classified as loans and borrowings, trade accounts payable, other current liabilities and accrued expenses.

Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Commitments and contingencies

Commitments and contingencies are not recognised in the consolidated financial statements. They are disclosed in the consolidated financial statements unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the consolidated financial statements but disclosed when an inflow of economic benefits is probable.

Foreign currencies

The functional and presentation currency of the Group is the Georgian Lari ("GEL"). These consolidated financial statements are presented in thousands of Georgian Lari, unless otherwise indicated. Transactions in currencies other than the Lari are treated as transactions in foreign currencies. Transactions in foreign currencies are initially recorded in the functional currency at the rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the statement of operations Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of initial transaction.

The exchange rates at the year-end used by the Group in the preparation of the consolidated financial statements were as follows:

	31 December 2007	31 December 2006
Georgian Lari/1 US Dollar	1.5916	1.7135
Georgian Lari/1 Euro	2.3315	2.2562
Georgian Lari/1 Swiss franc	1.4029	1.4042

(in Georgian Lari and in thousands)

Average exchange rates for the year ended 31 December 2007 and 2006 were as follows:

	Average for 2007	Average for 2006
Georgian Lari/1 US Dollar	1.6703	1.7764
Georgian Lari/1 Euro	2.2862	2.2297
Georgian Lari/1 Swiss franc	1.3920	1.4178

4. CRITICAL ACCOUNTING JUDGMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which are described in note 2, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Assessment of impairment of financial assets is based on actual collection of receivables in subsequent years.
Provisions are mainly represented by the provision for tax liabilities that is determined as the difference between the tax liability declared by the Group and the tax reconciliations act issued by the tax authorities.

Critical judgements in applying accounting policy

The following are the critical judgments, apart from those involving estimations (see below), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in consolidated financial statements.

Accounting for non-production property, plant and equipment

Included in property, plant and equipment are social infrastructure and other non-production assets, such as hostels, residencies etc. Management believes that expenditures incurred in respect of acquisition or construction of such assets qualify for the recognition as an asset on the premises that such expenditures are capable of contributing indirectly to the flow of cash and cash equivalents to the Group through a reduction of cash outflows related primarily to wages and salaries expenses. This is driven by the fact that such non-production assets are employed by the Group to provide in-kind benefits to its employees, which replace cash outflows on wages and salaries.

Key sources of estimation uncertainty

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

Trade and other accounts receivable

During the year management reconsidered the recoverability of its trade and other accounts receivable arising from the Group's operations which is included in its balance sheet at 31 December 2007 at GEL 7,968 thousand. Since the majority of the receivables were generated more than 180 days ago, management questioned their recoverability and investigated all debtors on a case-by-case basis. Amounts identified as non-recoverable were provisioned for. This situation will be closely monitored and future adjustments will be made if future development of this issue indicates that such adjustments are appropriate.

Prepayment and other current assets

During the year management reconsidered the recoverability of its prepayment and other current assets arising from Group's operations which are included in its balance sheet at 31 December 2007 at GEL 33,178 thousand. Since the majority of the assets were generated more than 180 days ago, management questioned their recoverability and investigated them on case-by-case basis. Amounts identified as non-recoverable were provisioned for. This situation will be closely monitored and future adjustments will be made if future development of this issue indicates that such adjustments are appropriate.

Taxes – de-installed equipment

As part of the operations of the Group, old used equipment is often de-installed. Equipment that is subsequently found to be re-usable is transferred to inventory class "other" and carried at a nominal value of GEL 1 for IFRS purposes. However as per the ruling of the Georgian Tax Authorities, for tax purposes the inventory should be valued at fair value. As a result the Group hired a local audit company to evaluate de-installed inventory as of 31 December 2007. Valuation of the de-installed inventory was determined to be GEL 14,585 thousand for tax purposes, with a subsequent resulting deferred tax asset of GEL 2,917 thousand for financial statement purposes. However, the tax authorities reserve the right to re-determine this valuation at the time of their tax inspection, with the result that future adjustments may be appropriate.

Useful lives of property, plant and equipment

The most significant estimates relate to the estimation of useful lives of property, plant and equipment, assessment of impairment of financial assets and assessment of provisions.

The estimation of the useful life of an item of property, plant and equipment is a matter of management judgement based upon experience with similar assets. In determining the useful life of an asset, management considers the expected usage, estimated technical obsolescence, physical wear and tear and the physical environment in which the asset is operated. Changes in any one of these conditions or estimates may result in adjustments to future depreciation rates.

As described in note 3 above, the Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognised in profit or loss.

(in Georgian Lari and in thousands)

5. RECONCILIATION BETWEEN CONSOLIDATED EQUITY AND NET RESULTS OF OPERATIONS FOR THE PERIOD

Reconciliation of equity upon adoption of IFRS 1 as of 31 December 2007 and 1 January 2007 and for the year ended 31 December 2007 is presented as follows:

	31 December 2007	Year ended 31 December 2007	1 January 2007
	Equity	Profit	Equity
Previous accounting	**1,389,126**	**(1,007)**	**1,305,941**
Deferred Tax benefit	40,030	40,030	-
Consolidation of subsidiaries	161	161	-
Correction of deferred tax expense related to prior years in PPE revaluation reserve	-	-	(159,629)
Correction of deferred tax expense related to prior years in investment property revaluation reserve	-	-	(1,894)
Correction of deferred tax expense related to prior years in retained earnings	-	-	14,967
Recognition of deemed cost in PPE revaluation reserve	-	-	(750,514)
Recognition of deemed cost in investment property revaluation reserve	-	-	(4,020)
Recognition of deemed cost in retained earnings	-	-	754,534
International Financial Reporting Standards	**1,429, 317**	**39,184**	**1,159,385**

The Group made a reclassification of the appropriate amount, GEL 754,534 thousand, from revaluation reserves to retained earnings within shareholders' equity as of 1 January 2007 to reflect the adjustment to "deemed cost," as defined by IFRS 1, for property plant and equipment and investment property, refer note 14 and 15.

6. REVENUE

An analysis of the Group's revenue for the year is as follows:

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Revenue		
Freight traffic	290,292	291,021
Passenger traffic	17,165	15,867
Total	**307,457**	**306,888**

(in Georgian Lari and in thousands)

7. INVESTMENT REVENUE

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Operating lease rental revenue:		
Carriages	11,520	8,727
Other	4,139	1,260
Investment properties	1,682	845
Buildings	688	552
	18,029	11,384
Interest revenue:		
Bank deposits	1,669	3,096
Total	**19,698**	**14,480**

8. OTHER GAINS AND LOSSES

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Other income	1,399	2,212
Gain on sale of investments in shares	534	-
Net foreign exchange gain/(losses)	208	(481)
Gain on investment property revaluation	41	-
Total	**2,182**	**1,731**

9. PROFIT FOR THE YEAR

Profit for the year has been arrived at after charging (crediting):

9.1 Depreciation and amortisation

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Depreciation of Property, Plant and Equipment	(106,649)	(27,589)
Amortisation of intangible assets	(9)	(11)
Total	**(106,658)**	**(27,600)**

(in Georgian Lari and in thousands)

9.2 Employee benefit expense

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Salary and bonuses expenses	(99,725)	(81,439)
Other related expenses	(5,582)	(3,634)
Total	**(105,307)**	**(85,073)**

9.3 Movement in provision for impairment

	Year ended 31 December 2007	Year ended 31 December 2006
Movement of provisions for impairment	(2,476)	2,669
Total	**(2,476)**	**2,669**

10. RAW MATERIALS AND CONSUMABLES USED

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Materials	(24,662)	(24,712)
Electricity	(18,192)	(17,169)
Fuel	(9,530)	(9,187)
Total	**(52,384)**	**(51,068)**

11. OTHER EXPENSES

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Repair and maintenance	(12,323)	(12,865)
Freight car rental	(9,371)	(9,506)
Taxes other than income tax	(7,527)	(6,251)
Security	(6,857)	(7,204)
Other provisions	(1,999)	(9,892)
Tax fines	(1,433)	(571)
Passenger transportation cost	(732)	(798)
Total	**(40,242)**	**(47,087)**

(in Georgian Lari and in thousands)

12. FINANCE COSTS

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Interest on bank loans	(792)	(1,016)
Total	**(792)**	**(1,016)**

13. INCOME TAXES

The corporate income tax rate for 2007 and 2006 was 20%. In July 2007 the corporate income tax rate was decreased from 20% to 15%, effective 1 January 2008.

The main components of the income tax for the years ended 31 December 2007 and 2006 were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Income tax expense	(22,324)	(23,747)
Deferred tax benefit	40,030	-
Total	**17,706**	**(23,747)**

The reconciliation between profit before tax multiplied by the statutory tax rate and income tax expense for the years ended 31 December 2007 and 2006 were as follows:

	Year ended 31 December 2007	Year ended 31 December 2006 Reserved IFRS
Profit before tax	21,478	113,924
Tax at applicable rate of 20%	(4,296)	(22,785)
Tax effect of:		
Effect of change in income tax rate from 20% to 15%	36,254	-
Effect of revaluations of assets for taxation purposes and non-deductible expenses	(14,403)	(1,013)
Non-taxable income	151	51
Income tax benefit/(expense)	**17,706**	**(23,747)**

(in Georgian Lari and in thousands)

As of 31 December 2007 and 1 January 2007 deferred tax assets and liabilities were as follows:

	31 December 2007	1 January 2007
Temporary differences related to deferred tax assets, due to:		
Allowance for doubt full debts	53,377	51,282
Inventory	16,843	3,380
Provisions	7,414	6,597
Other current assets	3,131	-
Allowance for inventory obsolete	2,722	5,260
Other short-term liabilities	2,503	1,153
Allowance for other non current assets	448	7,241
Trade receivables	-	275
Impairment of investments	-	1,620
Total deferred tax asset	86,438	76,808
Temporary differences related to deferred tax liabilities, due to:		
Property, plant and equipment and investment property	(796,594)	(807,611)
Other receivables	(17)	-
Trade payables	-	(1,329)
Other short-term liabilities	-	(650)
Total deferred tax liability	(796,611)	(809,590)
Total temporary difference, net	**(710,173)**	**(732,782)**
Deferred tax liability at 15% (2006: 20%)	**(106,526)**	**(146,556)**

As disclosed in note 4, there is a key source of estimation uncertainty, in regards to the deferred tax asset on Inventory.

The movement in deferred tax liability for the years ended 31 December 2007 and 31 December 2006 were as follows:

	31 December 2007
Deferred tax liability at beginning of the year	-
Recognition of deferred tax liability at 1 January 2007 (note 5)	(146,556)
Deferred tax benefit	40,030
Deferred tax liability at end of the year	**(106,526)**

(in Georgian Lari and in thousands)

14. PROPERTY, PLANT AND EQUIPMENT

The movement on property, plant and equipment for the year ended 31 December 2007 was as follows:

	Land	Buildings and construction	Rail track infrastructure	Transport, machinery, equipment and other	Capital construction in progress	Total
Cost or valuation						
Balance as at 31 December 2005	274	81,725	180,963	133,060	21,969	417,991
Additions	50,315	10,173	5,815	40,489	31,559	138,351
Disposals	(3,667)	(28,377)	(77)	(3,078)	-	(35,199)
Depreciation charge for the Year	-	(1,724)	(12,600)	(13,265)	-	(27,589)
Carrying amount as at 31 December 2006	46,922	61,797	174,101	157,206	53,528	493,554
Transfer to investment property	(1,426)	(2,126)	-	-	-	(3,552)
Revaluation increase	-	101,929	519,606	281,793	6,815	910,143
Restatement of Impairment loss	(51)	(32,143)	(54,593)	(41,257)	(6,211)	(134,255)
Revalued amount as at 31 December 2006	45,445	129,457	639,114	397,742	54,132	1,265,890
Deemed cost as at 1 January 2007	45,445	129,457	639,114	397,742	54,132	1,265,890
Additions	373,005	30	71	20,073	77,274	470,453
Addition to land fund	9,384					9,384
Disposals		(54)	(44)	(50)	-	(148)
Depreciation charge for the year	-	(3,748)	(36,631)	(66,270)	-	(106,649)
Transfer to investment property (note 15)	-	(3,740)	-	-	-	(3,740)
Carrying amount as at December 31, 2007	**427,834**	**121,945**	**602,510**	**351,495**	**131,406**	**1,635,190**

On the 1 January 2007 GR became a first time adopter of IFRS. As such GR elected, as allowed under IFRS 1 "First-time Adoption of International Financial Reporting Standards", to use the fair value, as derived at 31 December 2006 as deemed cost as at 1 January 2007.

The revaluation of the Group's property, plant and equipment was performed as at 31 December 2006 by an independent appraiser by Grant Thornton Amyot LLC according to International Valuation Standards.

The fair value was determined using a depreciated replacement cost approach for buildings and constructions, rail track infrastructure and machinery. Equipment was revalued using market value approach. Transport, consisting of wagons and locomotives, and land are revalued using sales comparison method.

(in Georgian Lari and in thousands)

15. INVESTMENT PROPERTY

	31 December 2007	31 December 2006 Reserved IFRS
Balance at the beginning of the year	9,466	-
Transfer from property, plant and equipment	3,740	3,552
Gain from fair value adjustment	41	5,914
Balance at the end of the year	**13,247**	**9,466**

On the 1 January 2007 GR became a first time adopter of IFRS. As such GR elected, as allowed under IFRS 1 "First-time Adoption of International Financial Reporting Standards", to use the fair value, as derived at 31 December 2006 as deemed cost at GEL 13,206 thousand as at 1 January 2007.

The fair value of the Group's investment property at 31 December 2007 has been arrived at on the basis of a valuation carried out at that date by Grant Thornton Amyot LLC, independent valuer that is not related to the Group. The valuation, which conforms to International Valuation Standards, was arrived at by reference to discounted cash flows of lease agreements.

Investment properties of the Group are land and buildings that are leased to LLC Tbilisi Central till the Year 2055 and to JSC Elit Electronics till the Year 2056. And container terminal leased to LLC Intertrans till year 2016.

16. OTHER NON-CURRENT ASSETS

	31 December 2007	31 December 2006 Reserved IFRS
Advances paid for acquisition of non-current assets	7,710	8,875
Intangible assets	26	23
Loan to subsidiary	-	103
	7,736	9,001
Less: provision for impairment	(448)	(7,241)
Total	**7,288**	**1,760**

17. INVESTMENTS

	31 December 2007	31 December 2006 Reserved IFRS
Investments in shares	2,021	35,040
Short term cash deposits in bank	-	2,100
Total	**2,021**	**37,140**

(in Georgian Lari and in thousands)

Investments as at 31 December 2007 and 31 December 2006 were as follows:

	Nature of business	Ownership interest in 2007	31 December 2007	Ownership interest in 2006	31 December 2006
					Reserved IFRS
Sak Rkinigza Project LLC	Construction	100%	-	100%	36
Refrigerated and Isothermal Transportation Company LLC	Transportation	100%	-	100%	15
Railway Telecom LLC	Communication	100%	-	100%	2
JSC Chitakhevi-Borjomi	Energy	25%	2,021	25%	2,021
JSC Absolute Bank	Banking	-	159	-	171
Mikheil Meskhi Stadium	Sport	-	-	100%	25,925
Reinforced Concrete Tie Factory LLC	Manufacturing	-	-	100%	5,887
Chkhenisi Crushed Stone Factory LLC	Manufacturing	-	-	100%	2,200
Academician E.Pipia Public Clinical Hospital LLC	Medical	-	-	100%	751
Tbilisi Cross Melding Factory LLC	Manufacturing	-	-	100%	403
			2,180		37,411
Less: allowance for impairment			(159)		(2,371)
Total			**2,021**		**35,040**

During 2007 Sak Rkinigza Project LLC, Refrigerated and Isothermal Transportation Company LLC, and Railway Telecom LLC were consolidated and thus are not recorded as investments as at 31 December 2007.

During 2006 the Government decided to transfer out of the Company's charter capital M. Meskhi Stadium (GEL 25,925 thousand) and other fixed assets (GEL 3,040 thousand) by decrees. However the legal transfer only occurred during 2007, refer note 28.

As at 31 December 2007 JSC Chitakhevi-Borjomi is not an associate to the Group, as in November 2007 JSC Energo-Pro Georgia purchased 71% of the share of Chitakhevi-Borjomi JSC and the Company has lost significant influence over Chitakhevi-Borjomi JSC. As a result the investment in Chitakhevi-Borjomi JSC is held at cost.

18. CASH AND CASH EQUIVALENTS

	31 December 2007	31 December 2006
		Reserved IFRS
Cash at banks	3,905	21,262
Cash on hand	306	295
Total	**4,211**	**21,557**

(in Georgian Lari and in thousands)

19. RESTRICTED CASH

	31 December 2007	31 December 2006 Reserved IFRS
Restricted cash	9,868	4,073
Total	**9,868**	**4,073**

Group has restricted cash in the form of funded letters of credit with TBC bank.

20. TRADE AND OTHER RECEIVABLES

	31 December 2007	31 December 2006 Reserved IFRS
Trade receivables	57,803	59,649
Other receivables	4,330	3,918
	62,133	63,567
Allowance for doubtful debts	(54,165)	(52,530)
Total	**7,968**	**11,037**

Movement in the allowance for doubtful debts were as follows for the years ended December 31:

	31 December 2007	31 December 2006 Reserved IFRS
Balance at beginning of the year	(52,530)	(49,285)
Accrued during the year	(1,635)	(3,245)
Balance at end of the year	**(54,165)**	**(52,530)**

The Group has provided fully for all receivables over 6 months because historical experience is such that receivables that are past due beyond 1 year are generally not recoverable.

As at December 31, the Group trade accounts receivable were denominated in foreign currencies as follows:

	31 December 2007	31 December 2006 Reserved IFRS
CHF	3,489	2,157
EUR	-	377
Total	**3,489**	**2,534**

(in Georgian Lari and in thousands)

Ageing of receivables:

	31 December 2007	31 December 2006 Reserved IFRS
Up to 3 months	7,846	2,157
From 3 months to 6 months	97	377
Over 6 months	54,190	61,033
Total	**62,133**	**63,567**

21. PREPAYMENTS AND OTHER CURRENT ASSETS

	31 December 2007	31 December 2006 Reserved IFRS
Refundable VAT	35,600	21,871
Advances paid to suppliers	17,272	13,285
Prepaid taxes other than income tax	6,911	4,811
Other current assets	20	156
Social tax	-	569
	59,803	40,692
Allowance for irrecoverable amounts	(26,625)	(15,810)
Total	**33,178**	**24,882**

22. INVENTORIES

Inventories as at 31 December 2007 comprised of:

	31 December 2007	31 December 2006 Reserved IFRS
Materials	25,240	20,346
Fuel	3,548	1,512
Rails	1,396	8,253
Other	396	2,538
	30,580	32,649
Less: allowance for inventory obsolete	(2,722)	(5, 260)
Total	**27,858**	**27,389**

(in Georgian Lari and in thousands)

23. CHARTER CAPITAL

The charter capital contributed by the State of Georgia was equal to GEL 935,588 thousand and GEL 586,481 thousand as at 31 December 2007 and 2006, respectively.

	Capital	Description
Balance at 1 January 2006	**362,764**	
5 January 2006	8,977	Share capital increased
21 February 2006	(9)	Share capital decreased
21 February 2006	7,330	Share capital increased
27 February 2006	(2,014)	Share capital decreased
27 February 2006	123	Share capital increased
3 May 2006	8,203	Share capital increased
3 May 2006	2,561	Share capital increased
8 June 2006	11,339	Share capital increased
8 June 2006	1,631	Share capital increased
8 June 2006	3,585	Share capital increased
15 June 2006	15,615	Share capital increased
17 July 2006	(504)	Share capital decreased
16 August 2006	(533)	Share capital decreased
16 August 2006	(175)	Share capital decreased
16 August 2006	(940)	Share capital decreased
16 August 2006	1,001	Share capital increased
16 August 2006	846	Share capital increased
16 August 2006	71	Share capital increased
16 August 2006	2,617	Share capital increased
16 August 2006	127,060	Share capital increased
16 August 2006	424	Share capital increased
16 August 2006	(228)	Share capital decreased
16 August 2006	(15)	Share capital decreased
16 August 2006	20	Share capital increased
17 August 2006	3,150	Share capital increased
6 September 2006	35	Share capital increased
6 September 2006	258	Share capital increased
13 December 2006	(523)	Share capital decreased
13 December 2006	33,812	Share capital increased
Balance at 31 December 2006	**586,481**	
Contribution of land	372,994	Share capital increased
Contribution of Property, plant and equipment	10,910	Share capital increased
Withdrawal of investments	(34,797)	Share capital decreased
Balance at 31 December 2007	**935,588**	

During 2007 the State of Georgia, the 100% shareholder, withdrew from Georgia Railways investments and property, plant and equipment by decree of the State Property Management Agency.

(in Georgian Lari and in thousands)

Land Fund

During 2007 the Company received from the government plots of land nominally valued at GEL 372,994 thousand, which were subsequently valued at fair value by normative cost. The gain after valuation at the amount of GEL 9,397 thousand were transferred to land fund.

24. DIVIDENDS DECLARED

Description	Amount of dividend	Declaration date	Payment date
Government decree on dividends 2006 declared	350	13 February 2007	26 February 2007
Government decree on dividends 2006 declared	300	13 February 2007	23 March 2007
Government decree on dividends 2007 declared	400	13 April 2007	25 April 2007
Government decree on dividends 2007 declared	650	15 March 2007	23 May 2007
Government decree on dividends 2007 declared	650	15 June 2007	25 June 2007
Government decree on dividends 2007 declared	650	11 Jul 2007	25 July 2007
Government decree on dividends 2007 declared	700	15 August 2007	17 August 2007
Government decree on dividends 2007 declared	300	15 August 2007	17 August 2007
Government decree on dividends 2007 declared	3,060	15 August 2007	17 August 2007
Government decree on dividends 2007 declared	40	15 August 2007	16 August 2007
Government decree on dividends 2007 declared	650	24 September 2007	27 September 2007
Government decree on dividends 2007 declared	450	19 October 2007	24 October 2007
Government decree on dividends 2007 declared	1,000	19 October 2007	24 October 2007
Government decree on dividends 2007 declared	1,450	7 November 2007	22 November 2007
Government decree on dividends 2007 declared	550	20 December 2007	28 December 2007
Government decree on dividends 2007 declared	800	20 December 2007	28 December 2007
Government decree on dividends 2007 declared	100	20 December 2007	28 December 2007
Government decree on dividends 2007 declared	100,000	26 December 2007	24 January – 26 December 2008
Total	**112,100**		

During 2007 the Company declared dividends of GEL 112,100 thousand. As at 31 December 2007 only GEL 12,100 thousand had been paid, refer note 33.

(in Georgian Lari and in thousands)

25. REVALUATION RESERVES

	31 December 2007	31 December 2006 Reserved IFRS
Property, plant and equipment revaluation reserve	-	910,143
Investment property revaluation reserve	-	5,914
Total	**-**	**916,057**

On the 1 January 2007 GR became a first time adopter of IFRS. As such GR elected, as allowed under IFRS 1 "First-time Adoption of International Financial Reporting Standards", to use the fair value, as derived at 31 December 2006 as deemed cost as at 1 January 2007, refer notes 14 and 15.

Property, plant and equipment reserve

Balance at 1 January 2006	-
Increase arising on revaluation of property, plant and equipment	910,143
Balance at 31 December 2006	910,143
Restatement of deferred tax on reserve, note 5	(159,629)
Recognition of deemed cost, note 14	(750,514)
Balance at 1 January 2007	-
Movement in reserve	-
Balance as at 31 December 2007	**-**

Investment property reserve

Balance at 1 January 2006	-
Increase arising on revaluation of investment property	5,914
Balance at 31 December 2006	5,914
Restatement of deferred tax on reserve, note 5	(1,894)
Recognition of deemed cost, note 15	(4,020)
Balance at 1 January 2007	-
Movement in reserve	-
Balance as at 31 December 2007	**-**

(in Georgian Lari and in thousands)

26. RETAINED EARNINGS CAPITALISATION

As a result of a decree by the government, in 2007 retained earnings of the Company, as per local accounting standards, were capitalised into charter capital in the amount of GEL 15,656 thousand (2006: GEL 199,838 thousand).

27. BORROWINGS

Non-current borrowings as at 31December 2007 and 2006 comprised an outstanding balance of a USD denominated loan obtained by the Company under a non-revolving credit line agreement signed with the European Bank for Reconstruction and Development ("EBRD") on 22 December 1998 and ratified by the Parliament of Georgia on 30 July 1999. The total amount of the credit line was equal to USD 20 million.

The outstanding balances as at 31December 2007 and 2006 were as follows:

	31 December 2007	31 December 2006 Reserved IFRS
Long-term portion of loan from EBRD	7,068	11,413
Current portion of loan from EBRD	3,832	4,215
Total	**10,900**	**15,628**

The repayment schedule set forth under the loan agreement requires payment of semi-annual equal instalments of USD 1,110 thousand. The final instalment is due in August 2010.

The interest rate is LIBOR + 1%. The loan is secured by a guarantee from the State of Georgia represented by the Ministry of Finance.

The carrying amount of long-term bank borrowings is considered to be a reasonable estimate of their fair value as the nominal interest rate on long-term bank borrowings is considered to be a reasonable approximation of the fair market rate with reference to loans with similar credit risk level and maturity period at the reporting date.

According to the abovementioned loan agreement, the Company has to comply with the following financial covenants at all times beginning from the year of 2000: "debt service coverage ratio" at a minimum of 1.5, "working ratio" at a maximum of 0.9, and "borrower's debtor days" at a maximum of 90 days. The Company complies with all the financial covenants as at 31 December 2007.

Calculation of compliance with covenants is presented below:

	2007		2006	
Covenant	**Required**	**Actual**	**Required**	**Actual**
Debt to Service Coverage Ratio	At least 1.50	27.26	At least 1.50	21.72
Working Ratio	Maximum 0.90	0.62	Maximum 0.90	0.57
Borrower's Debtor Days	Maximum 90 days	74	Maximum 90 days	71

(in Georgian Lari and in thousands)

28. LIABILITY TO THE OWNERS

	31 December 2007	31 December 2006 Reserved IFRS
Liability to owners	32,389	28,965
Total	**32,389**	**28,965**

During 2007 Government decided to transfer out of the Company's charter capital investments worth GEL 34,797 thousand by decrees, refer note 23. However, some of these assets were not formally transferred to government as at 31 December 2007 and the Company has accrued a liability to owners as at 31 December 2007 in the amount of GEL 32,389 thousand (2006: GEL 28,965 thousand).

29. PROVISIONS

	31 December 2007	31 December 2006 Reserved IFRS
Employee disability benefits	4,142	4,062
Litigations	3,272	2,535
Total	**7,414**	**6,597**

As at 31 December 2007 provision for litigations at the amount of GEL 3,272 thousand (2005: GEL 2,535 thousand) consists of court cases that management believes that it is probable that they will not successfully defend.

30. TRADE PAYABLES AND ADVANCES RECEIVED

	31 December 2007	31 December 2006 Reserved IFRS
Trade payables	24,563	16,100
Advances received from customers	8,148	11,070
Total	**32,711**	**27,170**

As at 31 December 2007 advances received from customers mainly relates to advances received for freight transportation in the amount of GEL 7,416 thousand.

(in Georgian Lari and in thousands)

Trade payables consisted of the following as at 31 December 2007 and 2006:

	31 December 2007	31 December 2006 Reserved IFRS
Current payables	23,739	15,302
Balance of settlement accounts with other railways	824	798
Total	**24,563**	**16,100**

Ageing of trade payables and advance received are following as at 31 December 2007 and 2006:

	31 December 2007	31 December 2006 Reserved IFRS
Up to 3 months	19,017	16,381
3 month to 6 month	7,532	6,103
6 month to 1 year	2,852	2,311
More then 1 year	3,310	2,375
Total	**32,711**	**27,170**

31. OTHER TAXES PAYABLE

	31 December 2007	31 December 2006 Reserved IFRS
Provision for tax liability	9,406	-
Property tax Liability	3,303	-
Other tax	363	2,229
Personal income tax withheld	394	668
Total	**13,466**	**2,897**

32. CURRENT INCOME TAX PAYABLE

	31 December 2007	31 December 2006 Reserved IFRS
Current income tax payable	2,201	9,832
Total	**2,201**	**9,832**

(in Georgian Lari and in thousands)

33. OTHER LIABILITIES

	31 December 2007	31 December 2006 Reserved IFRS
Dividends payable	100,000	350
Salaries payable	5,579	4,393
Other short-term liabilities	326	1,421
Total	**105,905**	**6,164**

The Company has declared dividends in December 2007 at the amount of GEL 112,100 thousand based on retained earnings of 2006 and 2007 financial years. Based on this declaration the Company has paid dividends in 2007 year at the amount of GEL 12,100 thousand, refer note 24.

34. PENSIONS AND RETIREMENT PLANS

Employees of the Group receive pension benefits from the State in accordance with the laws and regulations of Georgia. No post-employment benefit liabilities exist for the Enterprise.

35. RELATED PARTY TRANSACTIONS

Related parties or transactions with related parties, as defined by IAS 24 "Related Party Disclosures", represent:

(a) Parties that directly, or indirectly through one or more intermediaries: control, or are controlled by, or are under common control with, the Company; and that have joint control over the Company

(b) Associates – enterprises on which the Company has significant influence and which is neither a subsidiary nor a joint venture of the investor

(c) Joint ventures in which the Company is a venturer

(d) Members of key management personnel of the Company or its parent

(e) Close members of the family of any individuals referred to in (a) or (d)

(f) Parties that are entities controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) Post-employment benefit plans for the benefit of employees of the Company, or of any entity that is a related party of the Company.

(h) In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form. The Company had the following balances outstanding as of 31 December 2007 with related parties:

	31 December 2007
Balances:	
Trade and other accounts receivable, net	954
Prepayments and other current assets	304
Trade payables and advances received	3,640
Transactions:	

Cargo and passenger revenues	1,014
Electricity, maintenance and other services purchased	12,805
Dividends	11,450
Settlement of liabilities by the entity on behalf of another party	2,558

Transfers of FA and other assets with Enterprise Management Agency :

Balances:	
Accounts payables for property transferred to Enterprise Management Agency, refer to note 28	32,389
Dividends payable, refer note 33	100,000
Transactions:	
Receipt of property, plant and equipment, refer note 23	383,904
Disposal of property	1,604
Transfer of investments	38,145
Uzufruct (gratuitous assignment)	545

Compensation of key management personnel

Total key management remuneration for the years ended 31 December 2007 comprised short-term compensation amounting to GEL 325,976 and was included into Employee benefit expense.

36. FINANCIAL RISK MANAGEMENT

Capital risk management - The Group manages its capital to ensure that entities of the Group will be able to continue as a going concern while maximising the return to the equity holder through the optimisation of the debt and equity balance. The management of the Group reviews the capital structure on a regular basis. Based on the results of this review, the Group takes steps to balance its overall capital structure through the payment of dividends, taking of new loans and borrowings or redemption of existing loans and borrowings.

Major categories of financial instruments - The Group's principal financial liabilities comprise loans and borrowings, trade payables, other current liabilities and accrued expenses. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group's principle financial assets are cash and cash equivalents, restricted cash and trade and other receivables.

The Group's major financial assets and liabilities as of 31 December 2007 and 2006 were as follows:

	31 December 2007	31 December 2006 Reserved IFRS
Financial assets		
Cash and cash equivalents	4,211	21,557
Restricted cash	9,868	4,073
Trade and other accounts receivable, net	7,968	11,037
Total financial assets	**22,047**	**36,667**

(in Georgian Lari and in thousands)

Financial liabilities		
Trade accounts payable	(24,563)	(16,100)
Current portion of borrowings	(3,832)	(4,215)
Other liabilities	(105,905)	(6,164)
Long-term loan	(7,068)	(11,413)
Total financial liability	**(141,368)**	**(37,892)**
Total net position	**(119,321)**	**(1,225)**

The main risks arising from the Group's financial instruments are foreign currency, interest rate, credit and liquidity risks.

Foreign currency risk – Currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group undertakes certain transactions denominated in foreign currencies. The Group does not use any derivatives to manage foreign currency risk exposure, at the same time the management of the Group is trying to mitigate such risk by managing monetary assets and liabilities in foreign currency at the same (more or less stable) level.

The carrying amounts of the Entity's foreign currency denominated monetary assets and liabilities as at 31 December 2007 were as follows:

	GEL	USD	EUR	CHF
Financial assets				
Trade and other accounts receivable, net	5,542	-	-	3,369
Restricted cash	-	6,200	-	-
Cash and cash equivalents	1,083	1,756	-	45
Total financial assets	**6,625**	**7,956**	**-**	**3,414**
Financial liabilities				
Trade accounts payable	(22,231)	-	(1,064)	(587)
Other liabilities	(4,045)	-	-	-
Current portion of borrowings	-	(2,222)	-	-
Long term loan	-	(4,441)	-	-
Total financial liabilities	**(26,276)**	**(6,663)**	**(1,064)**	**(587)**
Total net position	**(19,651)**	**1,293**	**(1,064)**	**2,827**

The carrying amounts of the Group's foreign currency denominated monetary assets and liabilities as at 31 December 2006 were as follows:

	GEL	USD	EUR	CHF
Financial assets				
Cash and cash equivalents	10,172	7,720	2	1
Restricted cash	-	2,377	-	-
Trade and other accounts receivable, net	8,035	-	377	159
Total financial assets	**18,207**	**10,097**	**379**	**160**

(in Georgian Lari and in thousands)

Financial liabilities				
Trade accounts payable	(12,786)	-	(1,482)	(1,016)
Other liabilities	(6,164)	-	-	-
Current portion of borrowings	-	(2,396)	-	-
Long term loan	-	(6,487)	-	-
Total financial liabilities	**(18,950)**	**(8,883)**	**(1,482)**	**(1,016)**
Total net position	**(743)**	**1,214**	**(1,103)**	**(856)**

The following table details the Group's Sensitivity to a 10% increase and decrease in the USD against the GEL. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 10% change in foreign currency rates.

Impact on net profit based on asset values as at 31 December 2007 and 31 December 2006:

	2007		**2006**	
	GEL/USD -10%	**GEL/USD +10%**	**GEL/USD -10%**	**GEL/USD +10%**
Profit or (loss)	129	(129)	121	(121)

	2007		**2006**	
	GEL/EUR -10%	**GEL/EUR +10%**	**GEL/EUR -10%**	**GEL/EUR +10%**
Profit or (loss)	(106)	106	(110)	110

	2007		**2006**	
	GEL/CHF -10%	**GEL/CHF +10%**	**GEL/CHF -10%**	**GEL/CHF +10%**
Profit or (loss)	283	(283)	(86)	86

Interest rate risk – Interest rate risk is the risk that changes in floating interest rates will adversely impact the financial results of the Group. The Group does not use any derivatives to manage interest rate risk exposure. The Group exposed to interest rate risk as entities in the Group borrow funds at both fixed and floating interest rates.

The following table presents a sensitivity analysis of interest rate risk, which has been determined based on "reasonably possible changes in the risk variable". The level of these changes is determined by management and is contained within the risk reports provided to key management personnel.

	2007		**2006**	
	Interest rate + 5%	**Interest rate – 5%**	**Interest rate + 5%**	**Interest rate – 5%**
Profit or (loss)	(530)	530	(761)	761

(in Georgian Lari and in thousands)

Limitations of sensitivity analysis - The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analyses do not take into consideration that the Group's assets and liabilities are actively managed. Additionally, the financial position of the Group may vary at the time that any actual market movement occurs.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Group's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

Credit risk – Credit risk is the risk that a customer may default or not meet its obligations to the Group on a timely basis, leading to financial losses to the Group.

The carrying amount of financial assets and other credit exposures recorded in the financial statements, which is net of impairment losses, represents the Group's maximum exposure to credit risk. The Group's policy is to provide services on prepayment basis and credit periods are usually no greater than 30 days.

The financial assets and other credit exposures of the Group are not rated i.e. do not have a rating issued by internationally recognised rating agencies.

The following table details the carrying value of assets that are impaired and the ageing of those that are past due but not impaired:

As of 31 December 2007:

		Financial assets and other credit exposures past due but not impaired					
	Neither past due nor impaired	0-3 months	3-6 months	6 months to 1 year	Greater than one year	Assets that have been impaired	Total
Cash and cash equivalents	4,211	-	-	-	-	-	4,211
Restricted cash	9,868	-	-	-	-	-	9,868
Trade accounts receivable	-	7,846	97	-	-	54,190	62,133
Prepayments and other current assets	33,178	-	-	-	-	26,625	59,803
Total	**47,257**	**7,846**	**97**	**-**	**-**	**80,815**	**136,015**

(in Georgian Lari and in thousands)

As of 31 December 2006:

	Neither past due nor impaired	Financial assets and other credit exposures past due but not impaired 0-3 months	3-6 months	6 months to 1 year	Greater than one year	Assets that have been impaired	Total
Cash and cash equivalents	21,557	-	-	-	-	-	21,557
Restricted cash	4,073	-	-	-	-	-	4,073
Trade accounts receivable	-	10,908	129	-	-	52,530	63,567
Prepayments and other current assets	24,882	-	-	-	-	15,810	40,692
Total	**50,512**	**10,908**	**129**	**-**	**-**	**68,340**	**129,889**

The Group's 10 largest customers in terms of sales for the year ended 31 December 2007:

	2007 Sales	31 December 2007 Outstanding balance
Georgia Transit	99,233	62
Pace Georgia	27,204	(1,182)
International Railway Expedition	8,794	44
Rail Trans Group	6,784	(475)
Mika Georgia	6,574	(256)
Intertrans	5,300	(150)
Castor Nautical Trading	5,036	(198)
Apaven	5,014	(396)
Energy Invest	4,846	(255)
Mezhtrans Service	3,569	(1)
	172,354	**(2,807)**

The Group's 10 largest customers in terms of sales for the year ended 31 December 2006:

	2006 Sales	31 December 2006 Outstanding balance
Georgia Transit	80,314	(3,110)
Pace Georgia	16,647	(1,135)
Apaven	2,666	(530)
Castor Nautical Trading	2,632	(450)
Tansgeorgia	2,121	-
Tero	2,019	(64)
Mika Georgia	1,873	(150)
Trans-Aliance-Poti	1,862	(186)
Bravil Black Sea	1,781	(607)
Intertrans	1,554	(428)
	113,469	**(6,660)**

The summary below shows outstanding balances and the turnover of top five counterparties as at 31 December 2007:

(in Georgian Lari and in thousands)

	31 December 2007 Outstanding balance	2007 Sales
Moravia Georgia	2,446	-
Alioni	1,749	-
Georgian Sugar	1,082	111
Silk Road Group	926	122
Inter	580	197
	6,783	**430**

The summary below shows outstanding balances and the turnover of top five counterparties as at 31 December 2006:

	31 December 2006 Outstanding balance	2006 Sales
Georgian Sugar	1,120	226
Alioni	1,076	7
Silk Road Group S.A.	862	201
Texaco	491	-
Tamarisi	482	-
	4,031	**434**

Liquidity risk – Liquidity risk is the risk that the Group will not be able to settle all liabilities as they are due. The Group's liquidity position is carefully monitored and managed. The Group has in place a detailed budgeting and cash forecasting process to help ensure that it has adequate cash available to meet its payment obligations.

An analysis of the liquidity risk of financial liabilities as of 31 December 2007 was as follows:

	Up to 3 months	3 months to 6 month	6 month to 1 year	More then 1 year	Maturity undefined	Total
Trade accounts payable	24,563	-	-	-	-	24,563
Current portion of borrowings	2,064	-	1,768	-	-	3,832
Other liabilities	105,905	-	-	-	-	105,905
Long-term loan	-	-	-	7,068	-	7,068
Total	**132,532**	**-**	**1,768**	**7,068**	**-**	**141,368**

An analysis of the liquidity risk of financial liabilities as of 31 December 2006 was as follows:

	Up to 3 months	3 months to 6 month	6 month to 1 year	More then 1 year	Maturity undefined	Total
Trade accounts payable	16,100	-	-	-	-	16,100
Current portion of borrowings	2,519	-	1,696	-	-	4,215
Other liabilities	6,164	-	-	-	-	6,164
Long-term loan	-	-	-	11,413	-	11,413
Total	**24,783**	**-**	**1,696**	**11,413**	**-**	**37,892**

(in Georgian Lari and in thousands)

37. COMMITMENTS AND CONTINGENCIES

Capital commitments

As at 31 December 2007 and 2006 the Group had capital commitments as follows.

	31 December 2007	31 December 2006
Within 1year	30,044	21,195
Longer than 1 year and not longer than 5 years	-	-
Longer than 5 years	-	-
Total	**30,044**	**21,195**

Capital commitments are primarily the construction of stations and a railway line to Tbilisi airport; modernisation of rail track infrastructure in Kaspi; modernisation of wagons; finishing of commercial service centre; locomotives and wagon capital repairs.

Contingent liabilities

	31 December 2007	31 December 2006
Litigation	2,099	-
Total	**2,099**	-

Contingent assets

	31 December 2007	31 December 2006
Taxes	32,403	-
Litigation	24,433	-
Total	**56,836**	-

Operating environment

The Group's principal business operations are within Georgia. Due to the recent conflict between Georgia and the Russian Federation, the business environment is uncertain and may be subject to rapid change. The Group's operations and assets could be at risk due to negative changes in the political, economic or business environment within Georgia and between Georgia and the Russian Federation. These consolidated financial statements do not contain any adjustments, if any, that may arise from the realisation of this uncertainty.

Leasing agreements

Operating leases relate to the investment property owned by the Group with lease terms of between 10 to 50 years. The lessee does not have an option to purchase the property at the expiry of the lease period.

(in Georgian Lari and in thousands)

The property rental income earned by the Group from its investment property for the year ended 31 December 2006, all of which is leased out under operating leases, amounted to GEL 1,682 thousand (2006: GEL 845 thousand).

As at 31 December 2007 and 2006 non-cancellable operating lease receivables of the Group were as follows:

	31 December 2007	31 December 2006
Within 1year	3,800	3,534
Longer than 1 year and not longer than 5 years	17,579	19,339
Longer than 5 years	85,404	95,427
Total	**106,783**	**118,300**

Litigation

The Group is involved in litigations and other claims that are in the ordinary course of its business activities. Management believes that the resolution of matters, other than the matters already provided for, refer note 29, will not have a material impact on its financial position or operating results.

Taxation

The Georgian tax authorities are increasingly directing their attention to the business community as the result of overall economic environment in Georgia. Because of that, local and national tax environment in Georgia is constantly changing and is subject to inconsistent application, interpretation, and enforcement. Non-compliance with Georgian laws and regulations can lead to the imposition of severe penalties and interest. Future tax inspections could result in additional commitments being revealed, which do not comply with the Group's tax records. Such commitments could be represented by taxes, penalties, and interest and their amounts could be material. While the Enterprise believes that it has complied with local tax legislation, there have been many new tax laws introduced in recent years, which are not always clearly written.

38. EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

Recent volatility in global and Georgian financial markets

In 2008 and 2009 a number of major economies around the world have experienced volatile capital and credit markets. A number of major global financial institutions have been taken over by other financial institutions and/or supported by government funding. As a consequence of the recent market turmoil in capital and credit markets both globally and in Georgia, notwithstanding any potential economic stabilisation measures that may be put into place by the Georgian government and the National bank of Georgia, there exists as at the date these consolidated financial statements are authorised for issue economic uncertainties surrounding the continual availability, and cost, of credit both for the Group and its counterparties, the potential for economic uncertainties to continue in the foreseeable future and, as a consequence, the potential that assets may be not be recovered at their carrying amount in the ordinary course of business, and a corresponding impact on the Group's profitability.

(in Georgian Lari and in thousands)

In the year of 2008 the following subsidiaries were disposed to the State of Georgia (100% shareholder of the Company):

	Nature of business	Ownership interest	Carrying amount as at 31 December 2007	Price	Change in equity
Refrigerated and Isothermal Transportation Company LLC	Transportation	100%	15	-	15

Subsequent to 31 December 2007 but before the issuance of this report, the Company has reduced declared dividends amount in the total amount of GEL 40,000 thousand in 2008, refer not 23.

In August of 2008, the conflict between Georgia and Russia damaged the infrastructure of the Group and also caused losses due to inability to conduct transportation services during the conflict. However this event does not have any impact on financial statement as at 31 December 2007.

In September of 2008, High Professional Education College of Railway Transport of Georgia LLC was founded by 100% shareholding on the basis of one of the branches of the Company. This subsidiary in amount of GEL 656 thousand was disposed to the State of Georgia in October of 2008.

In December 2008, two agreements amounting to USD 51,696,292 were signed with the Wagon Repairs Company LLC for capital renovation and repairs of 1,473 wagons.

In December 2008, the Company obtained credit line at the amount of USD 14,500 thousand in Bank of Georgia.

In June 2009, the Company signed agreement on transfer to Vagonmshenebeli Company LTD receivable from Eleqtrovagonshemketebeli Factory JSC at the amount of GEL 30,798 thousand. And "TBC Bank" JSC, "Bank Republic" JSC and "Bank of Georgia" JSC transferred their receivable rights (by factoring) with Eleqtrovagonshemketebeli Factory JSC to the Company at the total amount of GEL 30,798 thousand. Therefore, the Company takes on the liability of paying the receivables amount of GEL 30,798 thousand to the Banks. In case if payment to any of the banks becomes overdue for more than 60 days, or the payment schedule is violated twice, banks are permitted to cancel the agreement and demand remuneration of the unpaid amount immediately. In addition to all these conditions, all Eleqtrovagonshemketebeli Factory JSC property mortgage rights shall be transferred to the Company and appropriate agreements shall be concluded with the Factory. In turn, the Company mortgages its own real estate (land and buildings), located at Queen Tamar Avenue, Tbilisi.

In July 2009, the Company signed agreement with Eleqtrovagonshemketebeli Factory JSC on netting off mutual receivables at the amount of GEL 3,345. Besides, the Company transfers the right to demand this amount from Eleqtrovagonshemketebeli Factory JSC to Vagonmshenebeli Company LTD, along with mortgaging rights. Hence, Vagonmshenebeli Company LTD becomes listed, as a secured creditor.

39. APPROVAL OF CONSOLIDATED FINANCIAL STATEMENTS

These consolidated financial statements were approved by the management board and authorised for issue on 7 December 2009.