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Georgia | Transportation
Georgian Railway
July 24, 2019

Georgian Railway
Dry cargo set to drive growth

FY18 & 1Q19

2018 turned out to be another challenging year for GR. The decline in freight transportation, particularly in liquid cargo, persisted in 2018, with the top line down 3.3% y/y to US$ 167.5mn. Freight transportation revenue (56.8% of total) was down 9.1% y/y to US$ 95.2mn, driven by significant drop in oil products transportation, while dry cargos going through Georgia increased for the first time in the last 4 years (up 7.5% y/y). Logistic service revenue was also down 5.7% y/y to US$ 27.7mn. Other revenue streams increased in 2018, namely freight car rental was up 49.6% y/y to US$ 10.0mn and passenger traffic was up 18.7% y/y to US$ 10.8mn. Due to significant drop in its main revenue line (freight) over the last 5 years, the company carried out impairment testing of its PPE. The recoverable value was based on its value in use and resulted in a recognition of GEL 691.4mn or US$ 272.8mn impairment loss in 2018. Significant drop in EBITDA caused the net debt-to-EBITDA ratio to reach 6.2x in 2018, far above the Eurobond incurrence covenant of 3.5x.

FY18 revenue was down 3.3% y/y to US$ 167.5mn, from last year's low base of US$ 173.2mn. Freight transportation revenue, largest revenue category, was the main reason behind the decline in 2018. Oil products transportation (39.9% of total freight transportation) was also down 11.4% y/y to US$ 38.0mn, while crude oil transported was negligible. On the positive note, dry cargo transportation increased for the first time in the last 4 years, up 7.5% y/y to 6.9 tons, however reduced tariffs and changed product mix caused revenues to fall 5.0% y/y to US$ 55.7mn. Logistic service revenue was also down 5.7% y/y to US$ 27.7mn. Other revenue sources posted growth in 2018, particularly freight car rental revenue up 49.6% y/y to US$ 10.0mn. In addition, GR managed to increase passenger traffic revenues.

Operating expenses (excluding impairment loss on PPE) were up 2.8% y/y to US$ 152.1mn in 2018. This growth was mostly due to increased employee, fuel and other expenses. Reduced revenues and increased operating expenses caused the 14.4% y/y decrease in adjusted EBITDA to US$ 61.9mn in 2018, which translated into an adjusted EBITDA margin of 36.9% compared to 41.8% in 2017.

US$ 272.8mn impairment loss was recognized in 2018. Due to continued decline in freight transportation volumes, the company carried out impairment testing of its assets in 2018. The recoverable value was calculated by discounting forecasted revenues for 2019-37. Therefore, US$ 272.8mn impairment loss was applied to the PPE categories on pro-rata basis. As a result, the PPE balance reduced 25.3% y/y to US$ 682.4mn in 2018. Significant non-cash impairment loss resulted in negative bottom line of US$ 282.7mn.

Deteriorated operating performance worsened net debt-to-EBITDA ratio, which came in at 6.2x far above the Eurobond covenant of 3.5x. The company's net debt-to-EBITDA ratio has been above the covenant for the last two years, limiting the company's ability to incur any financial indebtedness in the medium-term.

Main Line Modernization Project is the only ongoing capital project by GR. As the company has renegotiated the payment structure with the construction company, the operating cash generated will be enough to cover the Capex requirements in the coming years.

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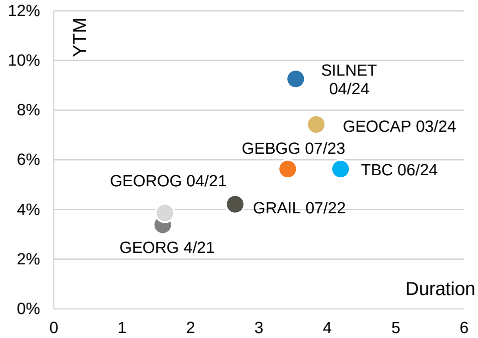
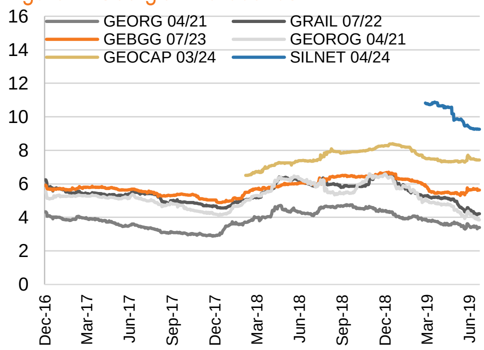
Figure 1: Georgian Eurobond universe



Source: Bloomberg

Figure 2: Georgian Eurobonds



Source: Bloomberg

Table 1: Key financials (US$ '000) and margins

	FY17	FY18	Change, y/y
Revenue	173,215	167,531	-3.3%
EBITDA	84,449	67,989	-19.5%
EBITDA margin	*48.7%*	*40.6%*	*-8.2pps*
Adjusted EBITDA	72,321	61,883	-14.4%
Adjusted EBITDA margin	*41.7%*	*36.9%*	*-4.8bps*
Net income	-141,152	-282,709	-100.3%
Net profit margin	*-81.5%*	*-168.8%*	*-87.3pps*
Assets	1,104,173	845,854	-23.4%
Liabilities	623,944	648,134	3.9%
Equity	480,229	197,719	-58.8%
Net debt to EBITDA	4.9x	6.2x	

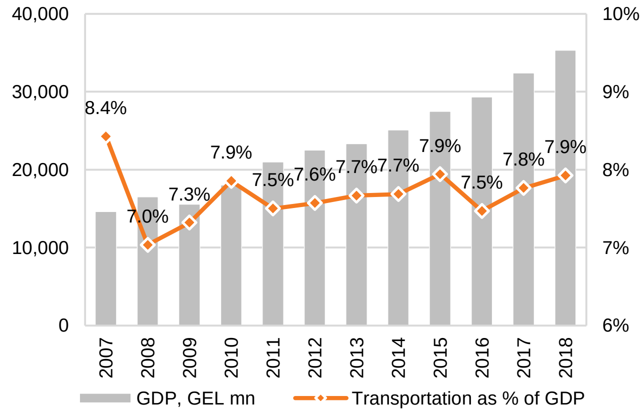
Georgian Railway credit ratings

S&P Global Ratings	Fitch Ratings
B+	BB-
Positive	Stable
Affirmed	Affirmed
Apr-2019	Mar-2019

Georgia's transit potential

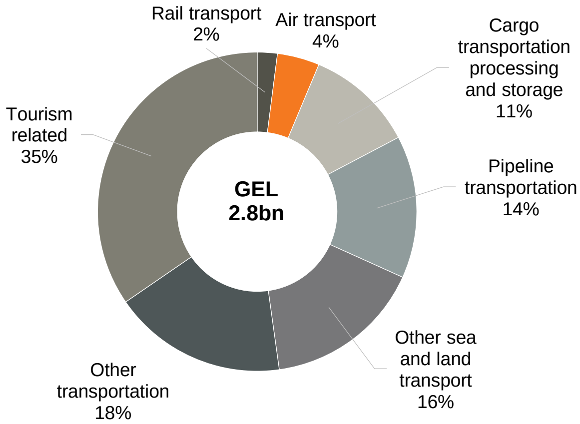
Georgia's strategic location makes it a natural transport and logistics hub, connecting resource-rich Central Asian countries with Europe. Despite many improvements in the sector, the lack of logistics and transit infrastructure hinders full utilization of its potential. Importantly, upcoming infrastructure projects are putting Georgia back on world transit map. Transportation sector accounted for 7.9% of GDP in 2018 and its total output reached US$ 1.8bn, up 12.6% y/y.

Figure 3: Transportation sector in GDP



Source: GeoStat

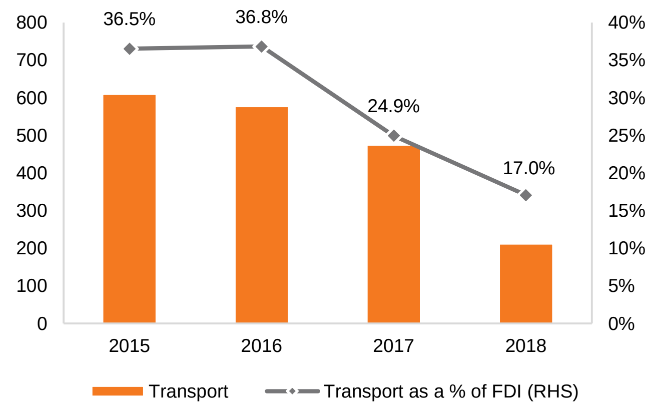
Figure 4: Transportation sector composition in 2018



Source: GeoStat

Transport and logistics was the 2nd largest FDI recipient in 2018. The sector attracted over US$ 3.7bn, nearly a quarter of total FDI received by Georgia during 2007-18. Foreign investments were mostly related to BP gas pipeline construction, completed in 2H18. Public investments in the sector were also substantial with c. US$ 1.6bn invested on only road reconstruction over 2013-18.

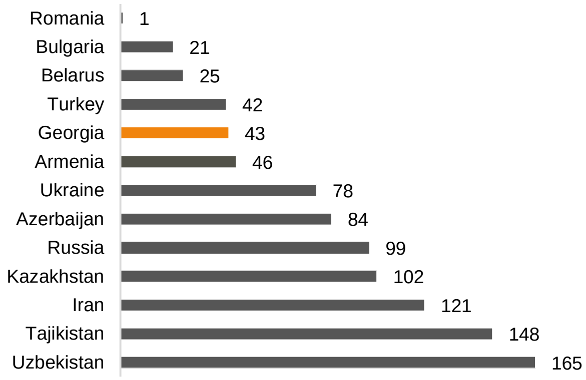
Figure 5: FDI in transport and communications sector, US$ mn



Source: GeoStat

Georgia ranks 43rd out of 190 countries on the ease of trading across borders according to World Bank Doing Business report 2019. Georgia has managed to improve its processes for trading across borders over the last decade thanks to its flexible time and cost required for importing and exporting goods. This was translated into improved position in overall ranking from 95 in 2007 to 43 in 2019.

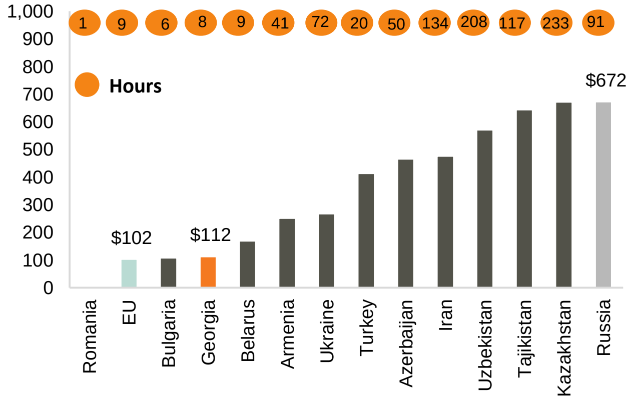
Figure 6: Rank on the ease of trading across borders, 2019



Source: World Bank – Doing Business

Georgia ranks 31st globally by time to export (border compliance and documentary compliance) and 27th by cost to export among 190 countries studied in 2019 Doing Business. Only 8 hours are needed to export goods from Georgia, far below the time needed in Russia (30 hours) or EU (average 9.2 hours). In addition, costs associated with exports stood at US$ 112 in Georgia in 2018, compared to US$ 672 in Russia and US$ 102.2 in EU.

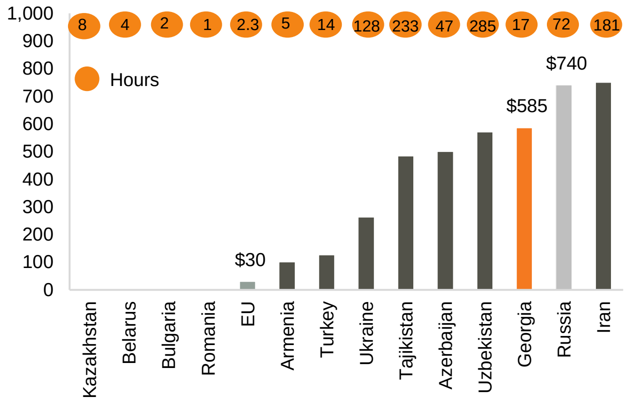
Figure 7: Export border compliance (hours, USD)



Source: World Bank – Doing Business

Georgia ranks 47th by import time and 113th by cost to import among 190 countries according to Doing Business report. Notably, 17 hours are needed to import products to Georgia, compared to 73 hours found in Russia (main competing transport route). However, with only 2.3 hours needed to import to EU, there is significant room for further improvement. Additionally, the costs associated with imports stood at US$ 585 in Georgia, compared to US$ 740 in Russia and average US$ 29.8 in EU.

Figure 8: Import border compliance (hours, USD)



Source: World Bank – Doing Business

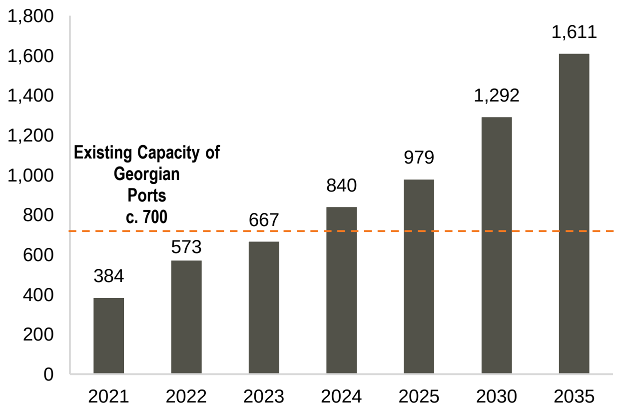
Large infrastructural projects in the pipeline

US$ 620mn is required to finance the first phase of Anaklia Deep Sea Port development. The company plans to attract US$ 400mn from IFIs (EBRD, OPIC, ADB, AIIB). Notably, Anaklia project is in the list of priority projects under the European Commission and the World Bank's Trans-European Transport Network (TEN-T) Investment Action Plan. Under this plan EUR 233mn is earmarked for port construction and EUR 100mn for a new railroad connection to the port. In addition, the Government of Georgia has pledged to build an 18-km railway line to link Anaklia port with existing railway network.

Maritime construction started at Anaklia port in 2H18. Since the launch of the project in 2016, 5.0mn sq.m of sand has been dredged with investment cost of US$ 70mn. The Dutch maritime contractor Van Oord NV has been carrying out dredging and reclamation works.

Anaklia Deep-Sea Port expected to enhance Georgia's transit potential. Construction works for Anaklia port started in 2017 and expected to receive first cargo in 2021. Anaklia port's throughput potential is expected to reach 100mn tons annually. Launch of Anaklia will open the region to international shipping, as 75% of Black Sea vessels cannot dock on the eastern side, except for Russia.

Figure 9: Anaklia port TEU capacity forecast, '000 TEUs



Source: Anaklia Development Consortium

EUR 3.4bn investments earmarked by EU for the development of major infrastructure projects in Georgia by 2030. According to the European commission and World Bank's investment action plan, priority investments of around EUR 12.8bn were identified across Eastern Partnership countries, including Georgia. A total of 18 infrastructural projects with an estimated investment of EUR 3.4bn will be implemented in Georgia (6 of which are underway), backed by international financial institutions and PPPs. The investments target development of 370km of road and rail network, one port and 2 logistics centers in Georgia, namely:

- EUR 1.5bn for development of road section throughout Georgia, including East-West highway gorge section;
- Anaklia deep sea port (2nd phase) with total investment value of EUR 233mn, in addition to financing road and rail to Anaklia with total cost of EUR 100mn;
- Kutaisi Airport Cargo Terminal, with total investment value of EUR 61.5mn;
- Two logistics centers in Kutaisi and Kumisi (near Tbilisi), with total space of 268,200 sq.m and total investment value of EUR 144mn.

Map 1: Priority projects in Georgia

Source: EU, the World Bank Group, Galt & Taggart Research

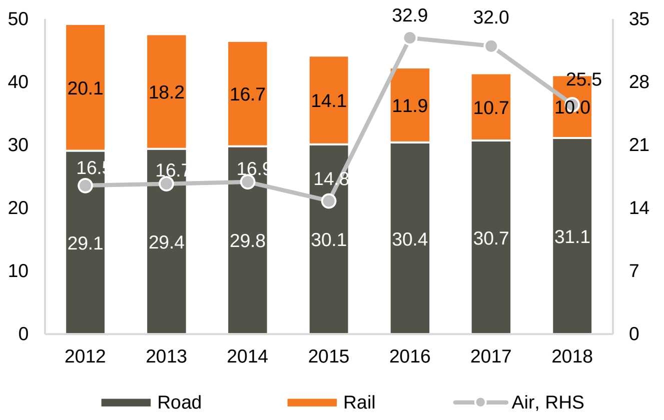
New multimodal corridor project for Georgia - In March 2019 Georgia, Azerbaijan, Romania and Turkmenistan established a multimodal corridor for the transportation between Caspian Sea and Black Sea (Caspian Sea – Black Sea International Transport Corridor project – ITC-CSBS). The corridor is expected to connect central Asia and southern Caucasus to Europe by creating intermodal transport route.

Baku-Tbilisi-Kars (BTK) railway line operation delayed. The construction of railway line, connecting Azerbaijan to Turkey via Georgia, was completed in October 2017. However, the launch of the project was delayed. The BTK line is expected to be fully operational from 2019, with the initial capacity of 5.0mn tons annually.

Cargo transit on downward trajectory since 2013

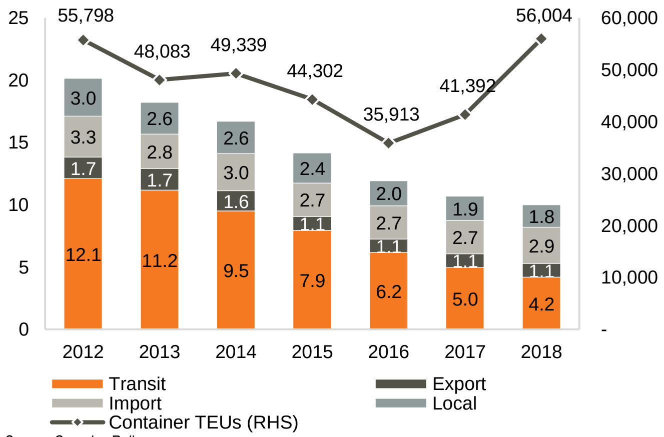
Cargo flows going through Georgia have been declining since 2013, with levels somewhat flat during 2016-18. A 0.9% y/y reduction in 2018 was solely related to reduced rail cargo transportation (down 6.6% y/y) as transit cargo dropped significantly, while freight volumes transported by road remained stable. Road transportation made up 75.7% of total cargo flows in 2018.

Figure 10: Freight transportation by modes, mn tons



Source: Ministry of Economy

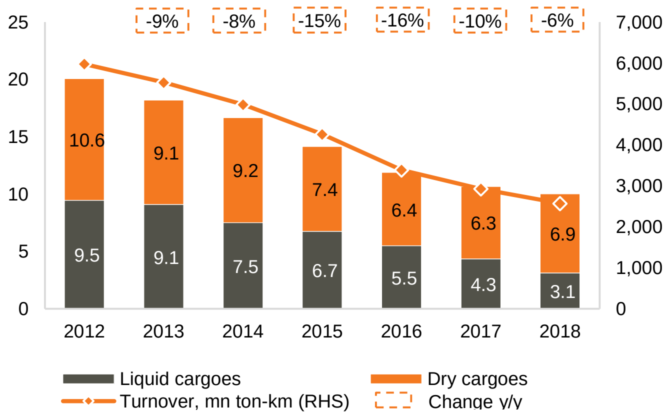
Figure 11: Rail cargo by type, mn tons



Source: Georgian Railway

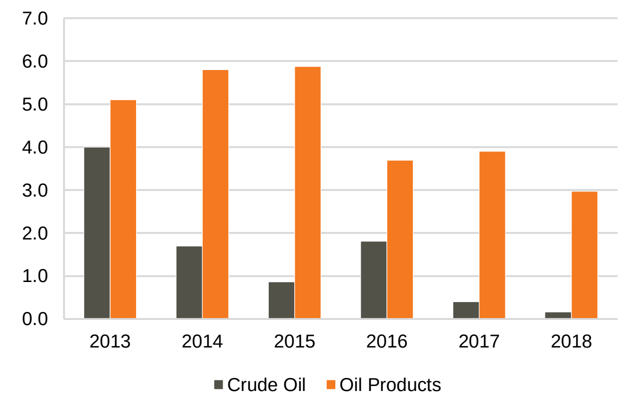
Liquid cargo transportation facing increased completion from pipelines continued to fall, down 27.0% y/y in 2018. Crude oil transportation decreased by 58.1% y/y and made up only 5.4% of total liquid cargo transported as major competitor CPC pipeline gained 10.8% y/y in 2018. Oil products transportation also fell 24.7% y/y due to reduced transportation volumes from Kazakhstan.

Figure 12: Rail cargo by type, mn tonnes



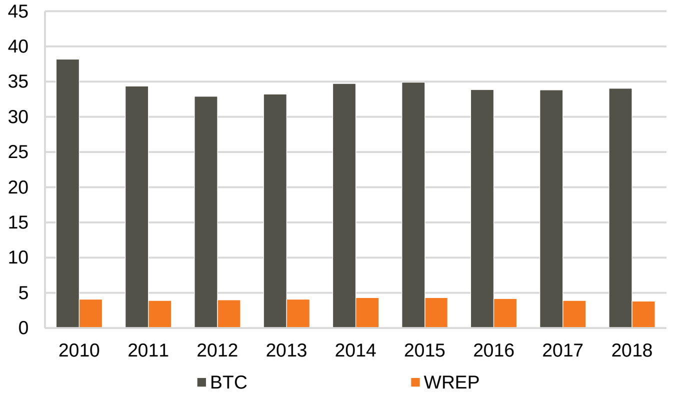
Source: Georgian Railway

Figure 13: Liquid cargo transportation, mn tons



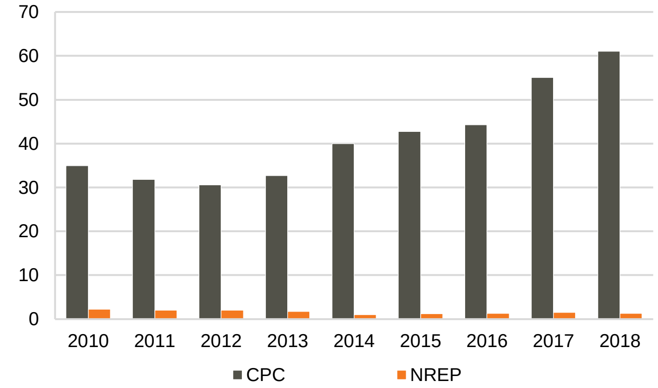
Source: Georgian Railway

Figure 14: BTC pipeline



Source: Georgian Railway
Note BTC pipeline Baku–Tbilisi–Ceyhan pipeline connecting Azerbaijan and Turkey through Georgia
WREP - Western Route Export Pipeline connecting Baku to Supsa terminal in Georgia

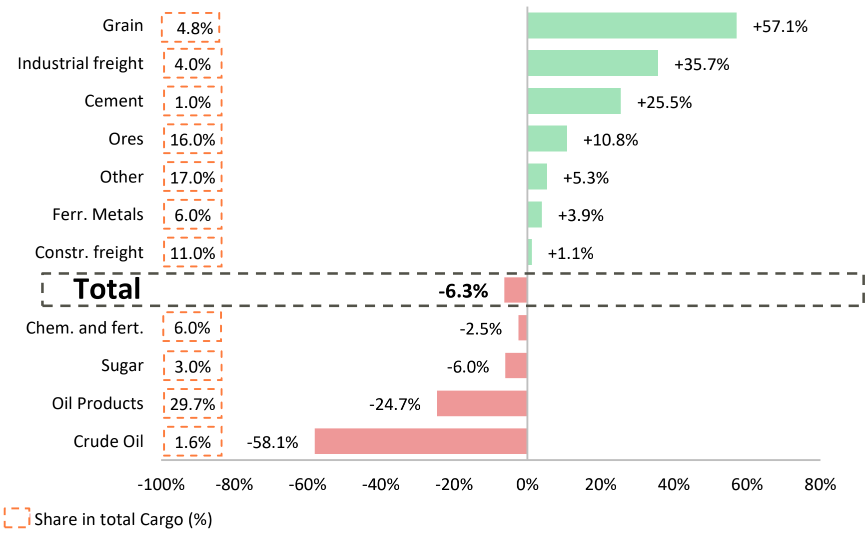
Figure 15: CPC pipeline



Source: Georgian Railway
Note: CPC pipeline - Caspian Pipeline Consortium connecting Kazakhstan to Russia
NREP Baku–Novorossiysk pipeline connecting Azerbaijan to Russia

For the first time in the last 4 years, dry cargo transported by rail was up 8.5% y/y and made up 68.4% of total cargo in 2018. However, this was not enough to compensate reduced liquid cargo volumes. Improved economic environment in the region is the likely reason for increased dry cargo transportation volumes. The major dry cargo products were ore and construction freight accounting for 39.6% of total dry cargo transportation in 2018.

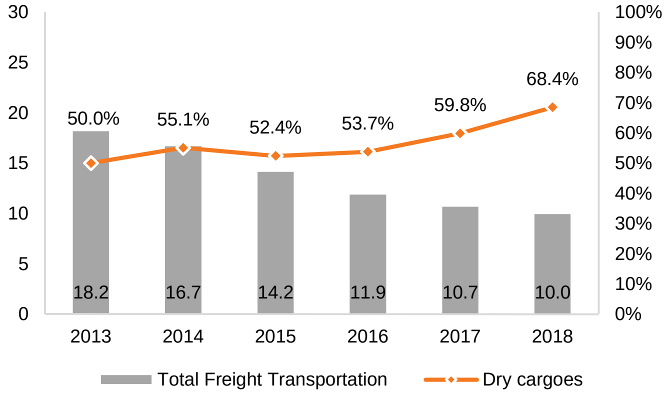
Figure 16: Cargo transportation volume, y/y change in 2018



Source: Georgian Railway

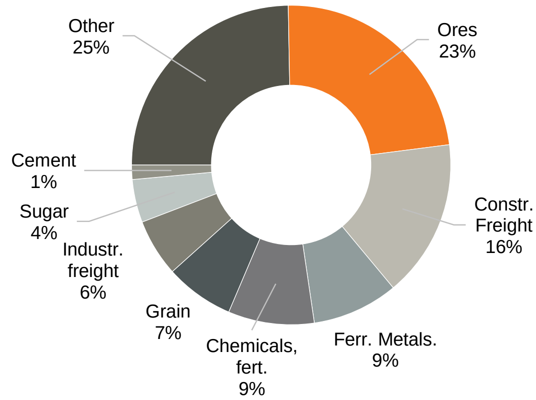
Ore products transportation, which made up 23.2% of total dry cargo grew 10.8% y/y, due to increased transportation from Armenia and Russia up 75,000 and 264,000 tons, respectively. Grain and grain products transportation was also up 57.1% due to increased transportation volumes from Kazakhstan.

Figure 17: Dry cargo transportation, mn tons



Source: Georgian Railway

Figure 18: Dry cargo mn tons, 2018

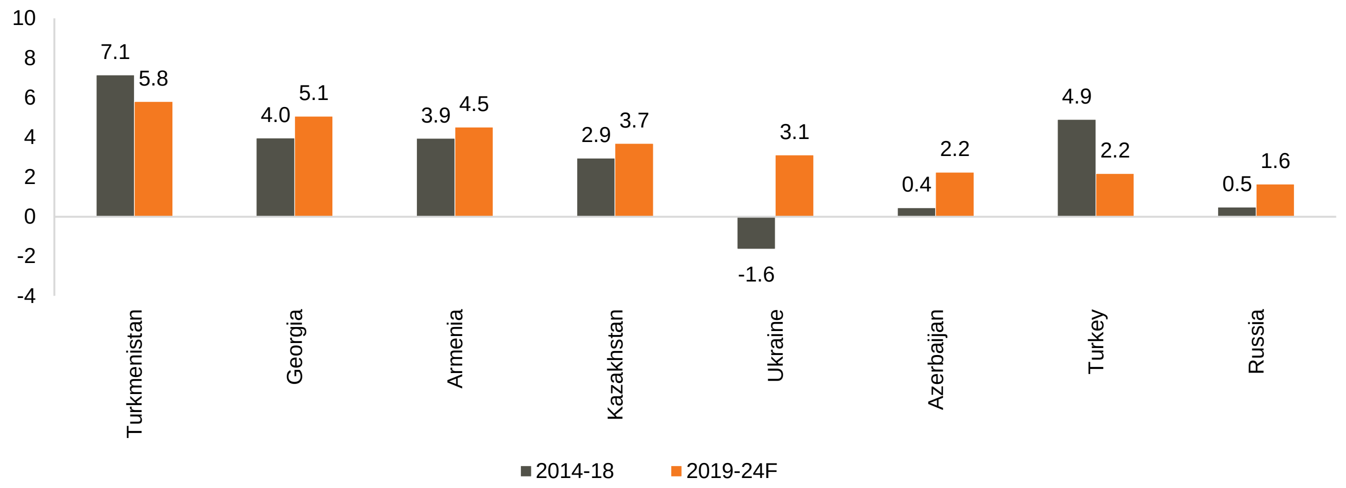


Source: Georgian Railway

Regional macro overview

During 2014-16, economic growth in the region was reduced significantly, reflecting the recession in Russia and its negative spillovers. Apart from these, growth was weighed by deteriorated confidence in Kazakhstan, weak public investment in Azerbaijan and Turkmenistan, and lower remittances and export revenues in the oil-importing countries. In 2017-18 economic growth rebounded in the region in part due to firmed oil prices, growing remittances and strengthened external demand. IMF projects growth to slow in most regional countries in 2019, however the medium term growth outlook is favorable capturing possibilities from strengthened global and regional trade integration as well as ongoing policies related to repair financial systems, remove structural rigidities, and improve governance.

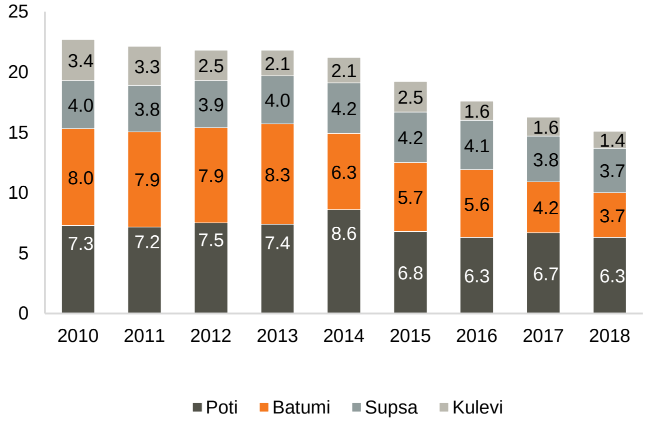
Figure 19: Average real GDP growth, %



Source: IMF, Galt & Taggart Research

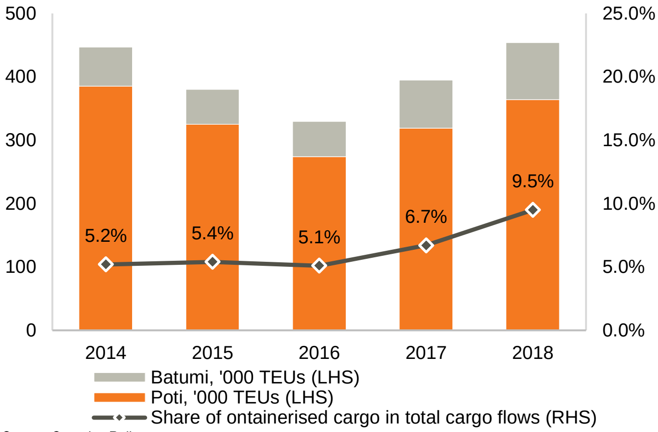
Georgia's sea ports handled 15.1mn tons of cargo in 2018 down 7.2% y/y. Poti port remains the major port on the Georgian coast accounting for 41.7% of total freight cargo handled or 6.3mn tons in 2018. However, due to continued reduction in cargo flows going through Georgia, the turnover in Poti port was down 5.8% y/y. Over 2017-2018 cargo flows in Batumi and Kulevi decreased 12.3% and 11.0%, respectively. On a positive note, in March 2018, Batumi Sea Port and Wondernet Express International Logistics Company agreed to build a new terminal in Batumi port. This terminal is for transporting mineral fertilizers from Central Asia. The terminal will be a new logistic corridor and most effective route from Central Asia to the Black Sea.

Figure 20: Freight handled at Georgian sea ports, mn tons



Source: Georgian Railway

Figure 21: Containers handled at Georgian sea ports

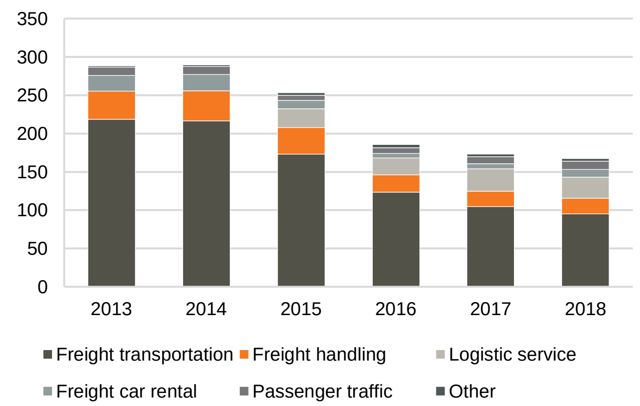


Source: Georgian Railway

Top line continues to decline

GR's revenue in 2018 decreased 3.3% y/y to US$ 167.5mn. Significant reduction in freight transportation and logistics service revenues dragged the positive trends in other revenue streams. Freight transportation revenue, which made up 56.8% of total, was down 9.1% y/y to US$ 95.2mn in 2018. Revenue from logistic services was down 5.7% y/y to US$ 27.7mn. Other revenue streams posted positive results in 2018, with freight handling and car rental revenue growing 1.9% y/y to US$ 20.4mn and 49.6% y/y to US4 10.0mn, respectively. Passenger revenue experienced another strong year, with revenue growing 18.7% y/y to US$ 10.8mn in 2018.

Figure 22: Revenue, US$ mn



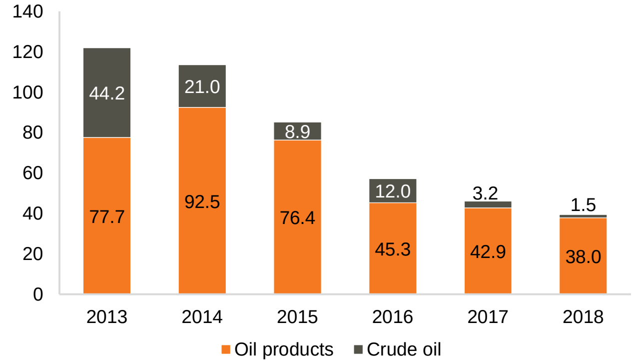
Source: Georgian Railway, Galt & Taggart Research

Freight transportation revenue, largest revenue category, continued to decline as a result of reduced freight cargo, particularly liquid cargo. Total freight revenue drop was effected by significant drop in oil products transportation.

Crude oil transportation going through Georgia dropped to almost zero (0.16mn tons) in 2018. Resulting transportation revenues also dropped 52.1% y/y to US$ 1.5mn in 2018. Notably, transportation of crude oil from Turkmenistan through Georgia stopped in 2018, while in 2017 its share stood at 23% in total crude oil going through Georgia.

Revenue from oil products transportation declined 11.4% y/y to US$ 37.9mn in 2018, effecting most GR revenues. Changed destinations were the main reason for reduced revenues. Namely, the share of Kazakhstan, more profitable direction, decreased from 34% of total oil products transportation in 2017 to 11% in 2018, while less profitable directions (Azerbaijan, Russia and Turkmenistan) gained the position in the mix (from 45% in 2017 to 66% in 2018).

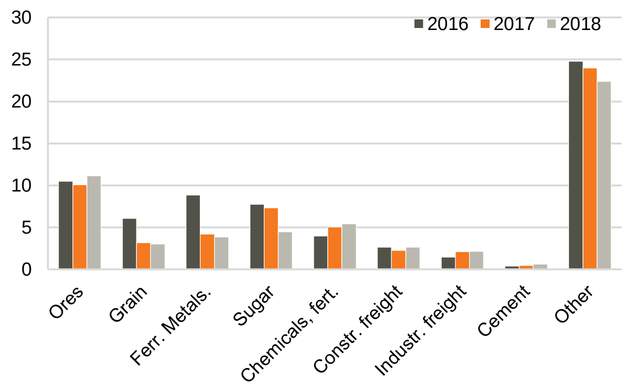
Figure 23: Liquid cargo transportation, US$ mn



Source: Georgian Railway, Galt & Taggart Research

Dry cargo transportation volumes were up while revenues declined 5.0% y/y to US$ 55.7mn in 2018. Reduced sugar transportation (down 39.0% y/y to US$ 4.5mn in 2018) effected most this revenue category as tariffs were down and cane sugar transportation (more profitable product) dropped. Meanwhile, the ore products transportation growth (up 10.5% y/y to US$ 11.1mn) partly offset this negative impact.

Figure 24: Dry cargo transportation volume, US$ mn



Source: Georgian Railway

Freight car rental and passenger traffic revenues increased to US$ 20.8mn in 2018 (up 49.6% y/y and 18.7% y/y, respectively). The former was related to increased usage of the company's tank cars, open-wagons and grain carriers, by its daughter company. While the latter was effected by increased revenues per person (from GEL 8.5 or US$ 3.4 in 2017 to GEL 9.6 or US$ 3.8 in 2018) as passengers shifted to more profitable, main line, direction.

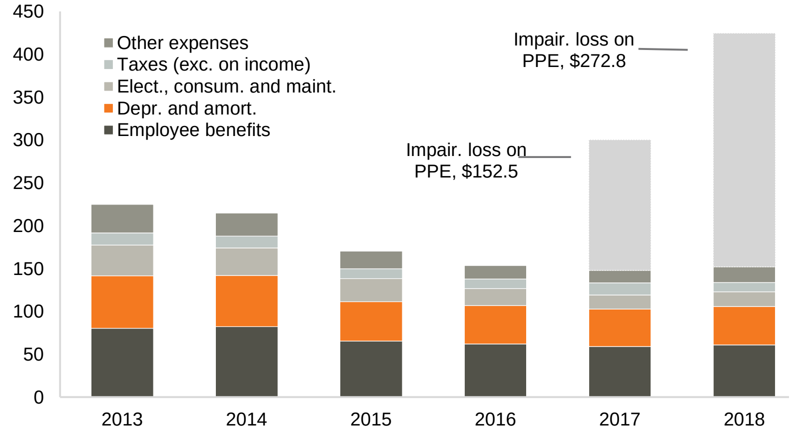
Significant impairment loss hit the bottom line

Operating expenses (excluding the PPE impairment) remained relatively flat, up 2.8% y/y to US$ 152.1mn in 2018. The major expense categories which were up in the reporting period were:

- Employee benefits increased 3.0% y/y to US$ 60.9mn due to increased business trip expenses, as well as change in capitalized employee expense calculation
- Electricity, consumables and maintenance expenses increased 4.3% y/y to US$ 17.2mn, mostly related to increased fuel expenses
- Other expenses increased 25.3% y/y to US$ 18.5mn as growing cargo containerization increased logistical services expenses

Meanwhile, taxes other than taxes on income reduced 23.7% y/y to US$ 10.6 in 2018 (in 2017 other taxes included one-off US$ 3.1mn difference between accounting and tax base).

Figure 25: Operating expenses, US$ mn



Source: Georgian Railway, Galt & Taggart Research

GR recognized a significant GEL 691.3mn (US$ 272.8mn) impairment loss on PPE in 2018, in addition to GEL 382.6mn (US$ 152.5mn) impairment loss recognized by the company in 2017 (related to the Tbilisi Bypass project). Impairment was related to the significant reduction in transportation volumes of the company. As the company's largest revenue source – freight transportation (representing 56.8% of total revenue in 2018) – has experienced significant reduction over the last 4 years (cumulative drop of 56.1% in 2018 vs. in 2014) the company carried out impairment testing of property, plant and equipment (excluding Tbilisi Bypass Project) in 2018.

The key assumptions made by company for discounting cash flow analysis up to 2037 were:

- Cash flows up to 2037 were discounted, as the company took into consideration stabilization of cargo flows going through Georgia on the back of launch of Anaklia Deep sea port
- Cargo flows were projected to grow by 4.6% annually through 2022 matched with Georgia's 2018 economic growth. No volume growth was projected from 2023 taking into consideration launch of Anaklia port
- 1.9% was taken as a terminal growth rate for the company (based on US long-term inflation forecast)
- Tariffs were increased by 2.25% during the first two years and 1.7% over the remaining period, considering the US CPI forecast
- US$ 80mn Capex on Modernization project and associated reduction in electricity and material costs by 10% during 2020 and 2021
- A pre-tax discount rate of 12.91% was applied on the cash flows

The above-mentioned assumptions resulted into an impairment of GEL 691.3mn (US$ 272.8mn), which represented 29.2% of the beginning value of the PPE. Impairment loss was allocated to items of property, plant and equipment on a pro-rata basis. As a result the PPE balance reduced from US$ 913.7mn as of end-17 to US$ 682.4mn as of end-18.

The company also carried out sensitivity analysis of the key assumptions made during the impairment testing. Namely, the revenue growth up to 2022 and various discount rates were analyzed. The table below provides amount of impairment losses if key assumptions change.

Figure 26: Sensitivity analysis of key assumptions, US$ mn

Discount rate/ Revenue growth	+2.6%	+3.6%	+4.6%	+5.6%	+6.6%
10.9%	-203.7	-162.7	-120.8	-78.1	-34.6
11.9%	-290.7	-254.5	-217.6	-180.0	-141.7
12.9%	-360.9	-328.7	-295.9	-262.5	-228.4
13.9%	-418.7	-389.8	-360.4	-330.4	-299.9
14.9%	-467.0	-440.9	-414.3	-387.2	-359.6

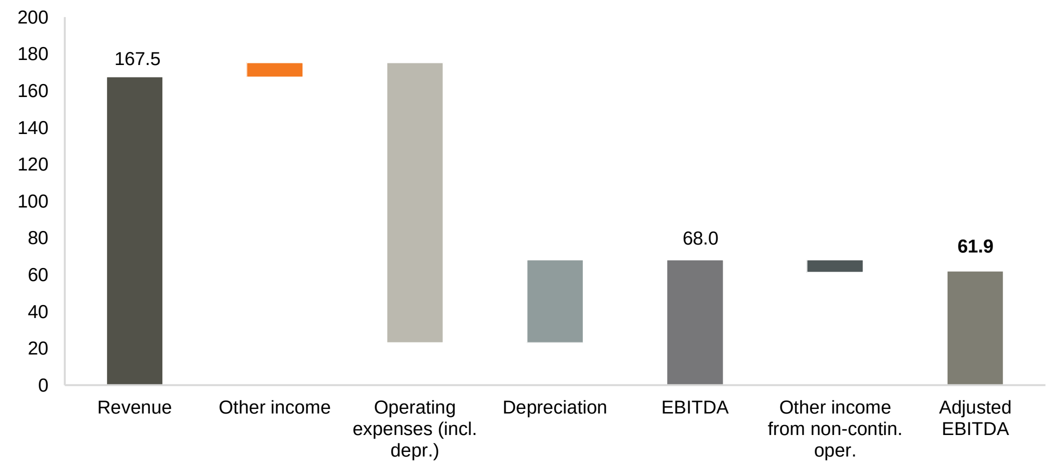
Source: Georgian Railway
Note: The difference between the actual impairment and the data in the table is related to the other assumptions not considered in the preparation of sensitivity analysis

The above analyses include addition of cargoes from Anaklia deep sea port. Its exclusion would result an additional impairment loss of GEL 293mn (US$ 115mn) in 2018.

Net debt-to-EBITDA ratio above the Eurobond covenant

FY18 EBITDA stood at US$ 68.0 vs US$ 84.4mn in 2017 as revenues reduced and operating expenses up. Adjusted EBITDA decreased 14.4% y/y to US$ 61.9mn in 2018. Consequently, adjusted EBITDA margin came in at 36.9% compared to 41.8% in 2017.

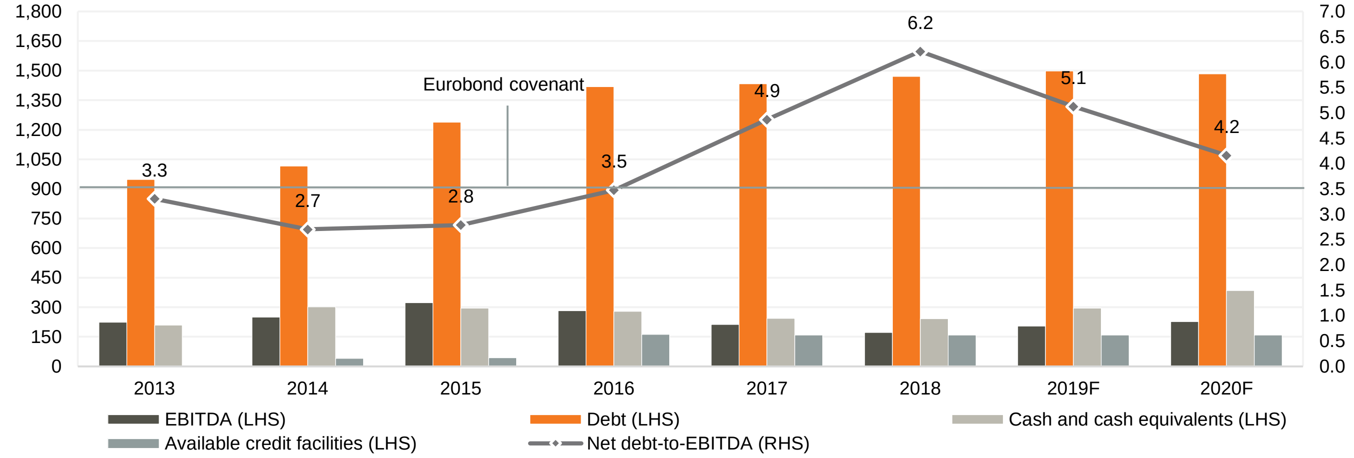
Figure 27: Calculation of EBITDA and adjusted EBITDA, 2018



Source: Georgian Railway, Galt & Taggart Research

Decreased EBITDA worsened net debt-to-EBITDA ratio, which reached 6.2x in 2018, much higher than the Eurobond covenant of 3.5x. In addition to Eurobonds, GR took a bank loan for the acquisition of trains, which also has the covenant of net debt-to-EBITDA of 4.0x. As 2018 debt-to-EBITDA ratio was over the bank covenant, the loan was reclassified as a short-term borrowing in end-2018. In January 2019, the company and the lender agreed on one year waiver of the covenant.

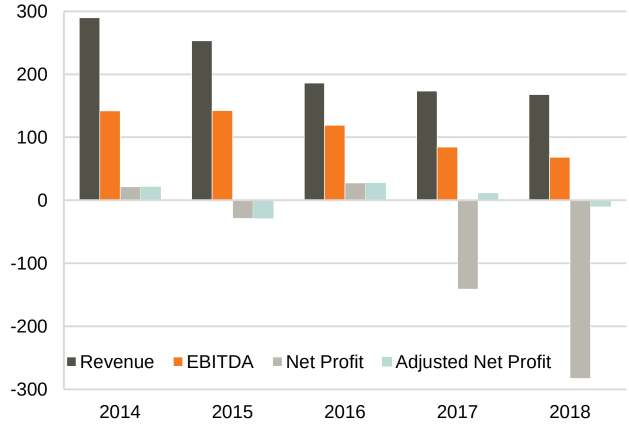
Figure 28: Net debt-to-EBITDA breakdown, GEL mn



Source: Georgian Railway, Galt & Taggart Research

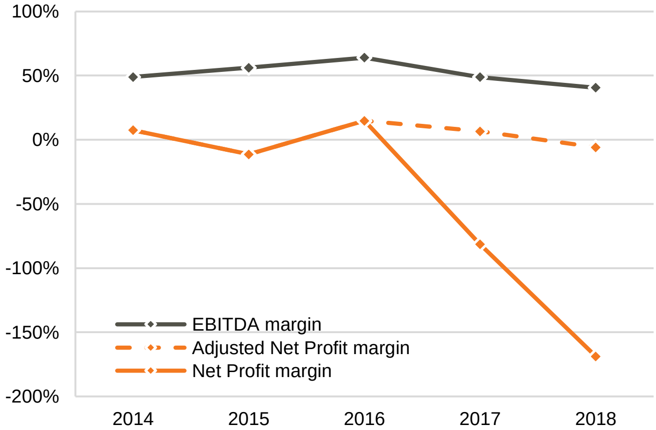
GR's net loss almost doubled in 2018 due to recognized impairment. GR recognized US$ 272.8mn impairment loss on PPE in addition to US$ 4.7mn impairment loss on trade receivables in 2018. As a result, the company's net loss doubled in 2018 compared to the previous year and stood at US$ 282.7mn.

Figure 29: Income statement highlights, US$ mn



Source: Georgian Railway
Note: Adjusted Net Profit excludes impairment costs

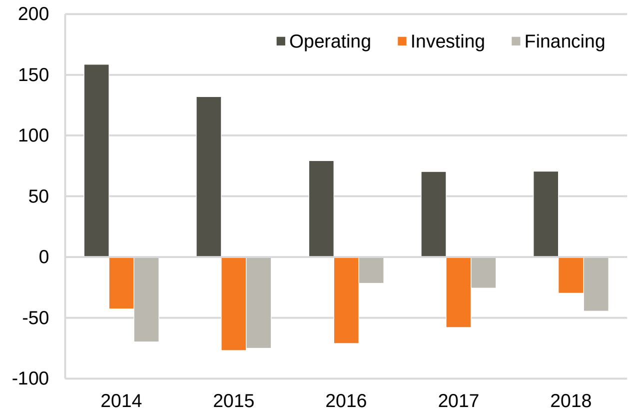
Figure 30: Profitability margins



Source: Georgian Railway

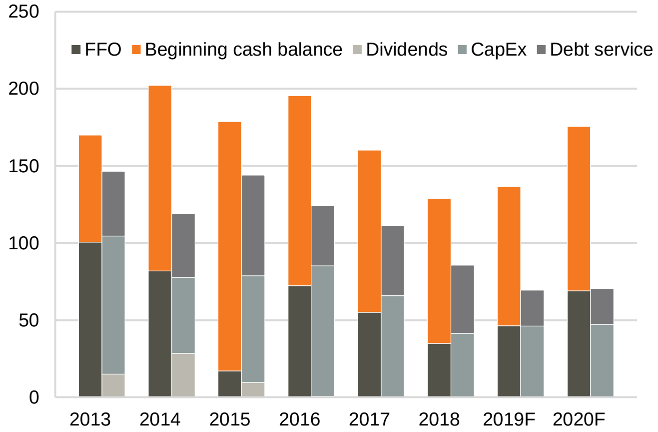
FY18 operating cash decreased 0.6% y/y to US$ 70.6mn. Cash outflows from investing activities (mainly related to purchase of two new double-decker trains in 1H17) were down 48.6% y/y to US$ 29.7mn. Cash flow from financing activities increased 74.1% y/y to US$ 44.3mn in 2018.

Figure 31: Cash flows, US$ mn



Source: Georgian Railway

Figure 32: Available cash vs. cash outflows, US$ mn

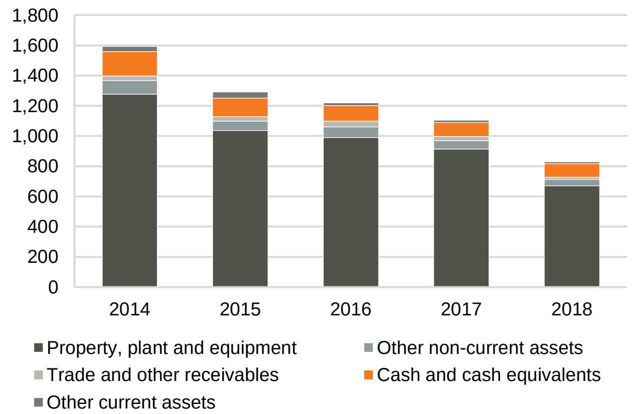


Source: Georgian Railway, Galt & Taggart Research

Balance sheet hit by the impairment loss

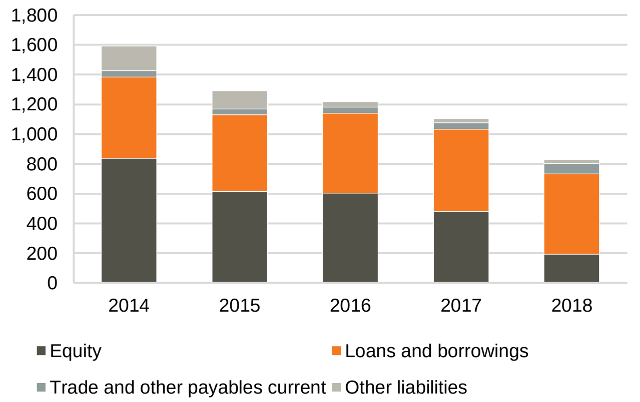
The impairment loss on PPE of US$ 272.8mn caused the decrease of PPE balance by 25.3% y/y to US$ 682.4mn. This combined with the US$ 4.7mn impairment loss on trade and other receivables resulted in 23.4% y/y decline in the company's asset base. On the liabilities side, substantial increase in the company's trade payables as well as short term borrowings worsened the company's debt to invested capital (0.7x in 2018) and debt to equity ratios (2.8x).

Figure 33: Asset composition, US$ mn



Source: Georgian Railway

Figure 34: Liabilities and equity composition, US$ mn



Source: Georgian Railway

Georgian Railway – 1Q19 update

Along with the FY18 financial results, GR also published 1Q19 unaudited financials. In US$ terms revenue remained relatively flat (up 0.6% y/y) at US$ 39.1mn, while in GEL terms the top line increased by 8.0% y/y to GEL 104.2mn in 1Q19 due to GEL's 7.3% depreciation vs US$. The upswing in freight transportation had lion's share in total growth.

The share of freight transportation revenue in total increased from 57.1% in 1Q18 to 67.9% in 1Q19. Freight transportation posted a solid 19.6% y/y growth in 1Q19 (+28.4% y/y in GEL terms) one of the highest growth recorded in recent years. Liquid cargo transportation, which made up 39.4% of total freight transportation revenue, was up 5.6% y/y (13.4% in GEL) to US$ 10.5mn. Dry cargo transportation revenue surged 30.9% y/y (40.6% y/y in GEL) to US$ 16.1mn in 1Q19.

Oil products were the only liquid cargo transported by GR, as crude oil transportation volumes were negligible. Oil products transportation was up 9.5% y/y (17.6% y/y) to US$ 9.1mn in 1Q19 fully compensating 10.5% y/y drop in oil products transportation volumes.

Dry cargo transportation revenue surged 30.9% y/y (40.6% y/y in GEL), reaching US$ 16.1mn in 1Q19 as sugar, ores and chemicals transportation increased. Sugar transportation revenue growth was related to increased demand from Azerbaijan generating US$ 1.4mn revenues in 1Q19 vs. US$ 0.7mn in 1Q18. Ores transportation grew 25.4% y/y (34.6% y/y in GEL) to US$ 3.3mn in 1Q19 caused by increased demand from Russia and Jamaica. Chemicals and fertilizers transportation rose 48.0% y/y (58.9% y/y in GEL) to US$ 2.2mn due to increased demand from Turkmenistan. Grain transportation was the only dry cargo that was down almost 3.0x in 1Q19, due to reduced transportation of wheat from Russia.

Passenger traffic remains on upward trajectory, with revenue growing 4.3% y/y (12.0% y/y in GEL) to US$ 1.8mn in 1Q19. On the other hand, freight handling and logistic service revenues declined 38.4% y/y (33.9% y/y in GEL) to US$ 3.1mn and (36.6% y/y in GEL) to US$ 3.7mn, respectively.

Operating expenses, which are mostly GEL denominated decreased 11.2% y/y to US$ 33.5mn (down 4.7% y/y in GEL). Employee benefits, the largest expense category, were down 4.4% y/y to US$ 14.1mn in 1Q19 (in GEL terms it increased 2.7% y/y). Electricity, consumables, and maintenance expenses reached US$ 4.2mn (+11.2% y/y in GEL). Other expense categories decreased also, down 18.9% y/y (-13.0% y/y in GEL) in 1Q19.

The enhancement in both revenues and operating expenses improved adjusted EBITDA, which was up 14.7% y/y to US$ 15.2mn in 1Q19. This translated into improved adjusted EBITDA margin, which came in at 39.0% in 1Q19, compared to 34.2% in 1Q18. Nevertheless net profit came in at US$ 3.0mn in 1Q19, compared to US$ 31.3mn in 1Q18 when the company realized significant FX gain (US$ 31.8mn).

Financial statements

Income statement

US$, '000	2014	2015	2016	2017	2018	2019F	2020F
Revenue	**296,696**	**266,739**	**227,884**	**188,752**	**175,229**	**180,941**	**192,480**
Freight transportation	216,740	173,015	123,636	104,747	95,210	103,482	113,659
Freight handling	39,102	34,877	22,383	20,006	20,379	20,597	20,918
Logistic service	-	24,706	22,217	29,408	27,744	27,567	27,437
Freight car rental	21,412	10,687	5,893	6,689	10,006	9,841	9,956
Passenger traffic	10,373	6,822	7,608	9,106	10,812	10,645	11,190
Other	2,073	3,078	4,140	3,259	3,380	3,519	3,694
Income from the transferred property	-	3,305	33,926	9,335	-	-	-
Other income	6,995	10,249	8,080	6,203	7,698	5,290	5,627
	6,995	13,554	42,006	15,537	7,698	5,290	5,627
Operating expenses							
Impairment loss on PPE	-	-	-	(152,520)	(272,786)	-	-
Employee benefits expense	(82,212)	(65,468)	(61,953)	(59,116)	(60,894)	(59,383)	(61,827)
Electricity, invent. and repair work	(32,415)	(26,838)	(19,981)	(16,538)	(17,245)	(18,081)	(19,234)
Other expenses	(40,478)	(32,246)	(26,901)	(28,649)	(29,101)	(29,506)	(30,830)
Operating expenses excl. depr. and amort.	(155,105)	(124,552)	(108,835)	(256,823)	(380,026)	(106,970)	(111,890)
EBITDA	141,591	142,186	119,049	(68,071)	(204,796)	73,971	80,590
Adjusted EBITDA	142,664	135,596	82,455	72,320	61,883	73,971	80,590
Depreciation and amortization expense	(59,607)	(45,995)	(44,901)	(43,730)	(44,901)	(38,848)	(40,555)
Results from operating activities	81,984	96,192	74,148	(111,801)	(249,698)	35,124	40,035
Finance Income	6,606	9,220	10,091	17,253	5,734	5,350	11,806
Finance Costs	(63,011)	(138,912)	(73,141)	(46,346)	(38,285)	(32,974)	(23,325)
Net finance costs	(56,405)	(129,692)	(63,050)	(29,093)	(32,551)	(27,624)	(11,519)
Profit before income tax	25,579	(33,500)	11,098	(140,894)	(282,248)	7,500	28,516
Income tax expense	(3,332)	4,649	16,419	(258)	(461)	-	-
Profit and total comprehensive income for the year	**22,248**	**(28,850)**	**27,517**	**(141,152)**	**(282,709)**	**7,500**	**28,516**

Note: GR reclassified the revenue generated by its freight forwarding subsidiaries under logistic service, a new revenue line
Source: Company data, Galt & Taggart Research

Statement of changes in equity

US$, '000	2014	2015	2016	2017	2018	2019F	2020F
Share capital, 1 January	604,777	564,607	439,519	397,840	406,323	393,676	386,117
Common capital issued for PPE	-	228	176	113	176	-	-
Net non-cash contr. by and distr. to owners	1,279	-	-	-	-	-	-
Cash contributions by and distributions to owners	-	-	-	-	-	-	-
FX rate translation adjustment	(41,449)	(125,316)	(41,855)	8,370	(12,823)	(7,559)	4,147
Share capital, 31 December	**564,607**	**439,519**	**397,840**	**406,323**	**393,676**	**386,117**	**390,264**
Non-cash owner contribution reserve, 1 Jan.	18,242	18,359	14,286	37,144	37,880	37,452	36,733
Net non-cash contr. by and distr. to owners	1,528	-	28,235	(51)	818	-	-
FX rate translation adjustment	(1,410)	(4,073)	(5,377)	787	(1,246)	(719)	395
Non-cash owner contr. reserve, 31 Dec.	**18,359**	**14,286**	**37,144**	**37,880**	**37,452**	**36,733**	**37,127**
Retained earnings, 1 January	280,700	255,600	160,505	169,246	36,026	(233,409)	(221,499)
Profit and total comprehensive income for the year	22,248	(28,850)	27,517	(141,152)	(282,709)	7,500	28,516
Dividends to equity holders	**(30,257)**	**(14,462)**	**-**	**-**	**-**	**-**	**-**
Net non-cash contr. by and distr. to owners	-	(515)	(686)	(201)	(634)	-	-
Cash contr. by and distr. to owners	-	-	-	-	-	-	-
Total transactions with owners…	(30,257)	(14,977)	(686)	(201)	(634)	-	-
FX rate translation adjustment	(17,091)	(51,268)	(18,090)	8,133	13,908	4,410	(2,379)
Retained earnings, 31 December	**255,600**	**160,505**	**169,246**	**36,026**	**(233,409)**	**(221,499)**	**(195,361)**
Total equity	**838,566**	**614,310**	**604,230**	**480,229**	**197,719**	**201,351**	**232,030**

Source: Company data, Galt & Taggart Research

Statement of financial position

US$, '000	2014	2015	2016	2017	2018	2019F	2020F
Assets							
Property, plant and equipment	1,276,147	1,036,951	991,232	913,656	682,430	682,584	694,176
Investment property	-	-	-	-	-	-	-
Deferred tax assets	835	457	-	-	-	-	-
Loan receivable	-	-	13,494	6,988	7,651	3,752	-
Other non-current assets	91,323	61,797	55,752	47,667	36,436	39,957	42,913
Non-current assets	1,368,306	1,099,205	1,060,479	968,311	726,517	726,294	737,090
Inventories	18,249	14,518	11,241	12,656	12,285	15,072	16,187
Loan receivable current	-	16,009	1,501	-	-	-	-
Current tax assets	5,862	4,590	2,693	910	1,457	1,598	1,716
Trade and other receivables	28,946	29,498	37,649	28,398	15,285	17,774	14,228
Prepayments and other current assets	9,952	4,969	132	148	155	152	154
Term deposits	-	-	-	-	-	-	-
Cash and cash equivalents	161,506	123,088	105,015	93,750	90,155	106,572	137,338
Current assets	224,515	192,673	158,231	135,862	119,336	141,167	169,622
Total assets	**1,592,821**	**1,291,877**	**1,218,711**	**1,104,173**	**845,854**	**867,461**	**906,712**
Equity and liabilities							
Share capital	564,607	439,519	397,840	406,323	393,676	386,117	390,264
Non-cash owner contribution reserve	18,359	14,286	37,144	37,880	37,452	36,733	37,127
Retained earnings	255,600	160,505	169,246	36,026	(233,409)	(221,499)	(195,361)
Total equity	**838,566**	**614,310**	**604,230**	**480,229**	**197,719**	**201,351**	**232,030**
Loans and borrowings	498,698	498,268	514,433	530,192	499,389	499,389	499,389
Advance received from the government	123,083	92,608	27,886	17,974	17,408	27,046	27,337
Trade and other payables	28	22	-	-	-	-	-
Deferred tax liabilities	32,195	18,342	-	-	-	-	-
Non-current liabilities	654,003	609,240	542,319	548,166	516,797	526,435	526,726
Loans and borrowings current	46,861	18,729	21,600	22,687	50,136	49,719	50,197
Trade and other payables current	42,112	37,270	41,423	43,292	71,587	78,509	84,319
Liabilities to the government	4,543	3,344	3,173	2,929	1,986	2,179	2,340
Provisions	3,459	3,476	3,229	3,068	4,243	5,556	7,113
Dividend payable	-	1,153	-	-	-	-	-
Other taxes payable	-	-	-	-	-	-	-
Current tax liabilities	-	-	-	-	-	-	-
Other current liabilities	3,276	4,355	2,735	3,802	3,385	3,712	3,987
Current liabilities	100,252	68,328	72,161	75,778	131,337	139,674	147,956
Total liabilities	**754,255**	**677,568**	**614,481**	**623,944**	**648,134**	**666,109**	**674,682**
Total equity and liabilities	**1,592,821**	**1,291,878**	**1,218,711**	**1,104,173**	**845,853**	**867,461**	**906,712**

Source: Company data, Galt & Taggart Research

Statement of cash flows

US$, '000	2014	2015	2016	2017	2018	2019F	2020F
Cash flows from operating activities							
Cash receipts from customers	298,361	248,813	192,986	178,388	179,771	178,131	196,218
Cash paid to suppliers and employees	-138,081	-114,631	-111,590	-107,067	-109,025	-106,970	-111,890
VAT refund from the State	-	-	`-	-	-	-	-
Cash flows from operations before income taxes and interest paid	160,279	134,182	81,395	71,321	70,746	71,162	84,327
Income tax paid	-1,657	-2,256	-2,209	-1,070	-107	-170	-101
Net cash from (used in) operating activities	**158,623**	**131,926**	**79,186**	**70,251**	**70,640**	**70,991**	**84,226**
Cash flows from investing activities							
Acquisition of property, plant and equipment	-49,184	-69,154	-84,621	-65,878	-41,307	-46,193	-47,205
Proceeds from sale of property, plant and equipment	43	-	1,415	2,046	6,848	-	-
Finance income	6,525	9,247	9,479	5,902	4,678	5,350	6,442
Issuance/repayment of the loan	-	-16,962	-13,759	-	-	3,788	3,793
Repayment of loans given	-	-	15,988	-	-	-	-
Other investing	-	-	454	-	-	-	-
Net cash from (used in) investing activities	**-42,616**	**-76,870**	**-71,043**	**-57,931**	**-29,781**	**-37,055**	**-36,970**
Cash flows from financing activities							
Proceeds from borrowings	-	-	17,894	20,030	-	551	-56
Repayment of borrowings	-	-27,537	-	-4,383	-4,469	-	-
Interest paid	-41,241	-37,764	-38,850	-41,109	-39,858	-23,293	-23,325
Dividends to equity holders	-28,502	-9,626	-679	-	-	-	-
Net cash from (used in) financing activities	**-69,743**	**-74,927**	**-21,636**	**-25,462**	**-44,327**	**-22,742**	**-23,381**
Net increase in cash and cash equivalents	46,264	-19,870	-13,493	-13,142	-3,468	11,195	23,875
Cash and cash equivalents, 1 January	120,368	161,506	123,088	105,014	93,749	90,154	106,572
Effect of exchange rate fluctuations on cash and cash equivalents	5,828	17,140	6,381	-784	3,012	-	-
FX rate translation adjustment	-10,954	-35,687	-10,962	2,661	-3,139	5,223	6,891
Cash and cash equivalents, 31 December	**161,506**	**123,088**	**105,014**	**93,749**	**90,154**	**106,572**	**137,338**

Source: Company data, Galt & Taggart Research
Note: Financial statements have been prepared by translating company-reported audited GEL numbers into US$ (using year-end and average annual FX rates, whichever more appropriate)

Financial ratios

	2014	2015	2016	2017	2018	2019F	2020F
Profitability							
EBITDA margin	48.9%	56.2%	64.0%	48.8%	40.6%	42.1%	43.1%
Adjusted EBITDA margin	49.2%	53.6%	44.4%	41.8%	36.9%	42.1%	43.1%
EBIT margin	28.3%	38.0%	39.9%	-64.5%	-149.0%	20.0%	21.4%
EBT margin	8.8%	-13.2%	6.0%	-81.3%	-168.5%	4.3%	15.3%
Net profit margin	7.7%	-11.4%	14.8%	-81.5%	-168.8%	4.3%	15.3%
Return on Investment							
Operating ROA / Basic earning power	4.9%	7.1%	5.4%	-9.8%	-28.0%	4.0%	4.4%
Return on average assets (ROAA)	1.3%	-2.2%	2.1%	-11.6%	-28.0%	0.9%	3.2%
Return on average equity (ROAE)	2.5%	-4.3%	4.2%	-24.9%	-80.8%	3.8%	13.1%
Return on capital employed (ROCE)	5.2%	7.6%	5.9%	-9.8%	-27.6%	4.9%	5.4%
Solvency							
Component percentage / debt ratios							
Liabilities to assets	47.35%	52.45%	50.42%	56.51%	76.62%	76.79%	74.41%
Liabilities to equity	89.95%	110.30%	101.70%	129.93%	327.81%	330.82%	290.77%
Liabilities to EBITDA	5.4x	4.7x	5.8x	7.7x	9.7x	8.9x	8.4x
Debt-to-assets	34.25%	40.02%	43.98%	50.07%	64.97%	63.30%	60.61%
Debt-to-invested capital	39.42%	45.70%	47.01%	53.52%	73.54%	73.17%	70.31%
Debt-to-equity	65.06%	84.16%	88.71%	115.13%	277.93%	272.71%	236.86%
Debt-to-EBITDA	3.9x	3.5x	4.7x	6.7x	8.4x	7.4x	6.9x
Net debt-to-EBITDA	2.7x	2.8x	3.5x	4.9x	6.2x	5.2x	4.4x
Net debt-to-adjusted EBITDA	**2.7x**	**2.9x**	**5.0x**	**5.7x**	**6.8x**	**5.2x**	**4.4x**
Long-term debt-to-assets	31.31%	38.57%	42.21%	48.02%	59.04%	57.57%	55.08%
Long-term debt-to-equity	59.47%	81.11%	85.14%	110.40%	252.57%	248.02%	215.23%
Financial leverage (equity multiplier)	1.9x	2.1x	2.0x	2.3x	4.3x	4.3x	3.9x
EBITDA coverage	3.4x	3.8x	3.1x	2.1x	1.7x	3.2x	3.5x
Liquidity							
Current ratio	2.2x	2.8x	2.2x	1.8x	0.9x	1.0x	1.1x
Quick ratio (acid test)	2.1x	2.6x	2.0x	1.6x	0.8x	0.9x	1.0x
Cash ratio	1.6x	1.8x	1.5x	1.2x	0.7x	0.8x	0.9x

Source: Company data, Galt & Taggart Research

Disclaimer

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