Georgian Railway
9M18 update

Georgia | Transportation
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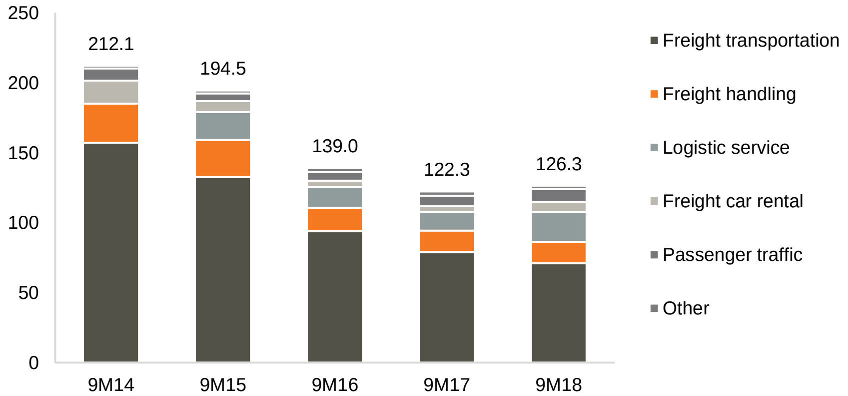
December 12, 2018

GR released 9M18 unaudited results together with Management Discussion and Analysis. Revenue increased 3.3% y/y to US$ 126.3mn, mostly due to increased logistics and freight car rental revenues, up 65.4% y/y to US$ 28.8mn. Passenger traffic also posted a 19.2% y/y growth to US$ 9.0mn in 9M18, enhanced by main line passengers. Meanwhile, operating expenses posted slight growth of 3.7% y/y to US$ 114.2mn. Adjusted EBITDA increased 3.6% y/y to US$ 49.3mn. GEL's depreciation-related non-cash FX loss of US$ 4.2mn in 9M18 compared to US$ 31.6mn gain in the same period last year caused the bottom line to plunge to US$ 7.3mn. Fitch Ratings revised Georgian Railway's outlook to positive from stable and affirmed the rating at "B+" in November 2018.

Freight transportation, the largest revenue category, declined 9.9% y/y to US$ 71.0mn in 9M18 from last year's low base of US$ 78.8mn. This decline was fully offset by logistic service revenue growth of 59.1% y/y to US$ 21.3mn. Freight car rental and passenger traffic revenues, together accounting for 13.0% of total revenue, posted significant growth of 86.4% y/y to US$ 7.4mn and 19.2% y/y to US$ 9.0mn, respectively. Other revenue was down 24.9% to US$ 2.3mn.

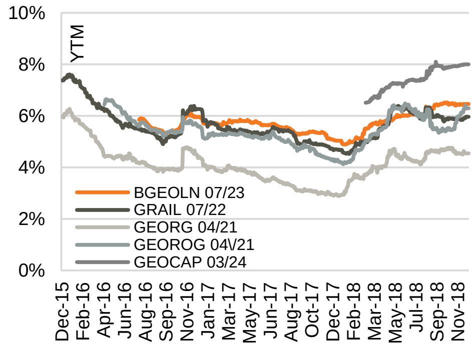
Figure 1: Revenue, US$ mn



Source: Company data

9M18 operating expenses increased 3.7% y/y to US$ 114.2mn. Employee benefits expense, largest expense category, remained flat at US$ 44.3mn. Depreciation and amortization expense rose 7.4% y/y to US$ 35.6mn. Other categories, accounting for just 30.0% of total expenses increased 4.1% y/y; Namely, electricity, consumables, and maintenance expenses were up 3.6% to US$ 13.2mn, increased logistical service and freight car rental revenue-related costs were also up 39.1% to US$ 5.0mn and 54.6% y/y to US$ 1.8mn, respectively. Taxes (exc. Income tax) were down 9.1% y/y to US$ 7.6mn, the only category that posted a decrease both in GEL and USD terms.

Figure 2: Georgian Eurobonds



Source: Bloomberg

Georgian Railway credit ratings

S&P Global Ratings	Fitch Ratings
B+ Stable Affirmed Sep-18	**B+** Positive Affirmed Nov-18

Source: Rating agencies

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

	9M17	9M18	Change, y/y
Revenue	122,292	126,338	3.31%
EBITDA	50,739	54,781	7.97%
EBITDA margin	*41.50%*	*43.36%*	*186bps*
Adjusted EBITDA	47,598	49,298	3.57%
Adjusted EBITDA margin	*38.90%*	*39.02%*	*10bps*
EBIT	17,566	19,149	9.01%
EBIT margin	*14.40%*	*15.16%*	*76bps*
Net income	37,781	7,336	-80.59%
Net profit margin	*30.90%*	*5.81%*	*-2509bps*
Assets	1,310,504	1,103,368	-15.81%
Liabilities	626,694	619,416	-1.16%
Equity	683,810	483,952	-29.23%

Source: Company data

US$-GEL	9M14	9M15	9M16	9M17	9M18
Period-end	1.75	2.38	2.33	2.48	2.62
Average	1.75	2.23	2.32	2.48	2.49

Source: NBG

Note: Georgian Railway financial statements published in GEL and converted into USD by Galt & Taggart

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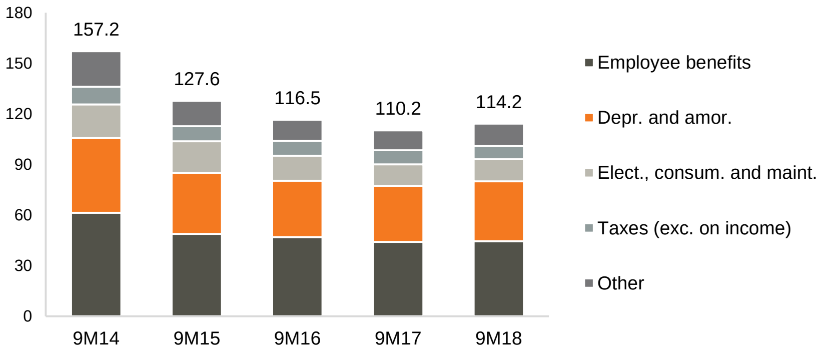
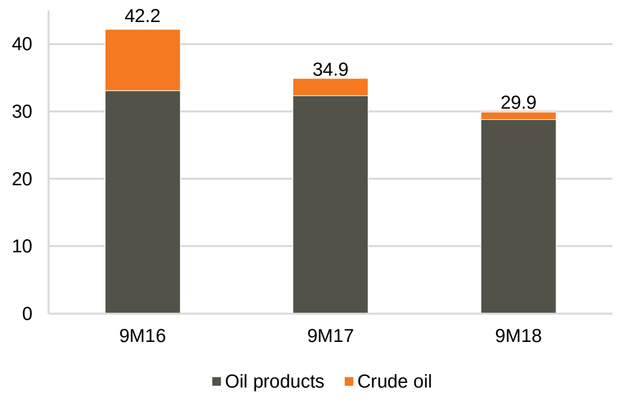
Figure 3: Operating expenses, US$ mn



Source: Company data

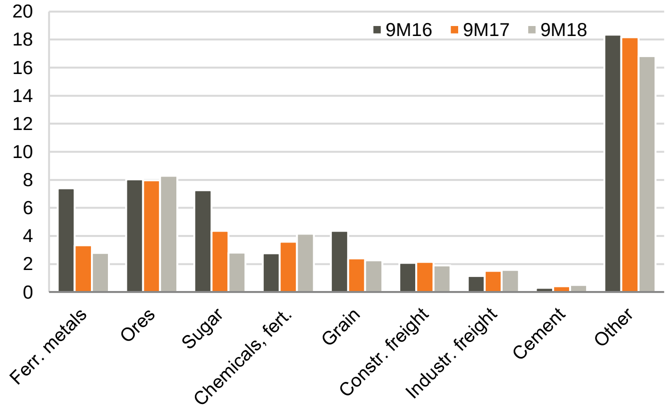
The decline in freight transportation revenue was mainly attributable to decrease in liquid cargo transportation. Oil products transportation revenue, which makes up 96.3% of liquid cargo, was down 10.9% y/y to US$ 28.8mn, while crude oil transportation more than halved (-56.9% y/y) to US$ 1.1mn in 9M18. The drop in oil products transportation (635,000 tons lower) was driven by the reduced transportation volumes from Kazakhstan, while 61.2% y/y drop in crude oil transportation volumes by rail is explained by re-direction of crude oil from Azerbaijan into the pipelines going through Georgia.

Figure 4: Liquid cargo transportation, US$ mn



Source: Company data

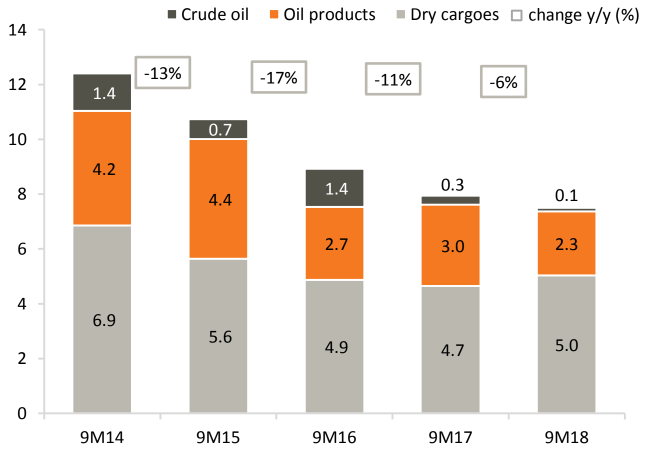
Figure 5: Dry cargo transportation, US$ mn



Source: Company data

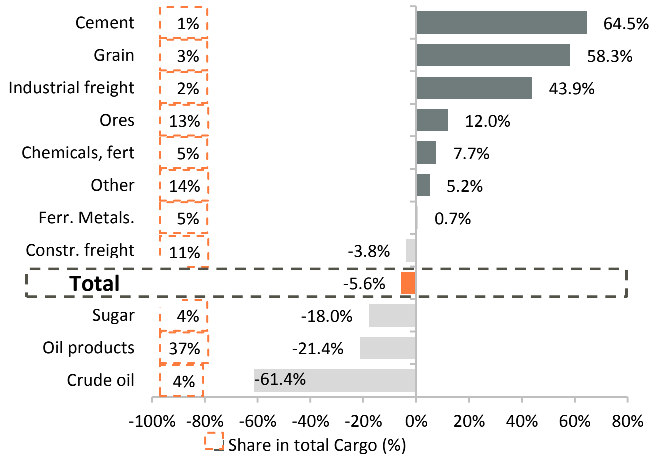
Dry cargo transportation, accounting for 57.9% of total revenue, **decreased 6.4% y/y to US$ 41.1mn in 9M18** explained by reduced transportation of sugar and ferrous metals. Sugar transportation fell 35.6% y/y to US$ 2.8mn and accounted for more than half of the total decline in dry cargo revenue. Reduced transportation volumes from Brazil, coupled with decreased share of cane sugar (relatively more profitable product) in product mix are to be blamed for the decline. Ferrous metals and scrap revenue shrank 16.7% y/y 9M18 to US$ 2.8mn due to decrease in transportation to profitable routes. Construction freight and grain transportation were also down 11.6% y/y to US$ 1.9mn and 5.9% y/y to US$ 2.2mn, respectively. Other dry cargo categories rose, with chemicals and fertilizers category posting the largest positive contribution to the revenue, increasing 15.7% y/y to US$ 4.2mn, while ores transportation, which contributed 20.1% of total dry cargo transportation, posted a low single-digit growth of 3.8% y/y to US$ 8.3mn.

Figure 6: Cargo transportation volume, mn tons



Source: Company data

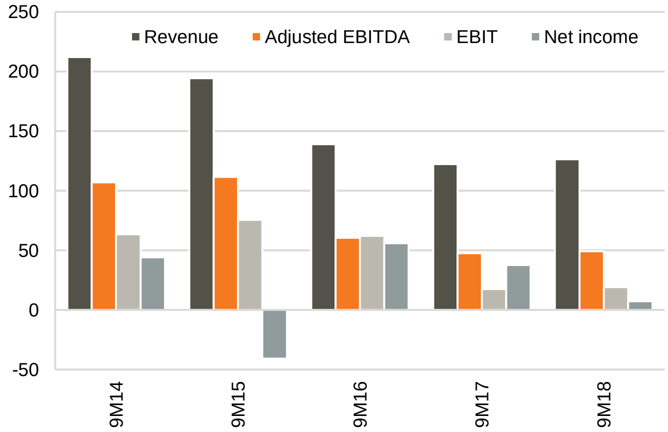
Figure 7: Cargo transportation volume, y/y change in 9M18



Source: Company data

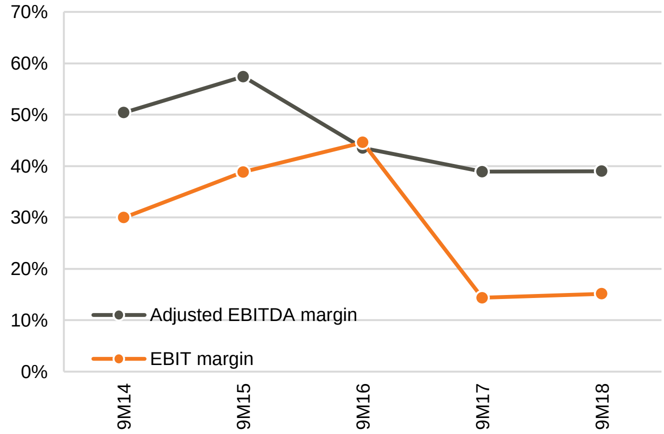
9M18 adjusted EBITDA increased 3.6% y/y to US$ 49.3mn. As a result, the adjusted EBITDA margin rose from 38.9% in 9M17 to 39.0% in 9M18. The growth in other income to US$ 5.8mn (+74.5% y/y) was stemming from the sale of fixed assets in the reporting period. GEL's 5.6% depreciation against US$ in Sep-18 vs Sep-17 led to a non-cash FX loss of US$ 4.2mn compared to US$ 31.6mn gain in the same period last year. This caused net income to drop to US$ 7.3mn in 9M18 from US$ 37.8mn in 9M17.

Figure 8: Income statement highlights, US$ mn



Source: Company data

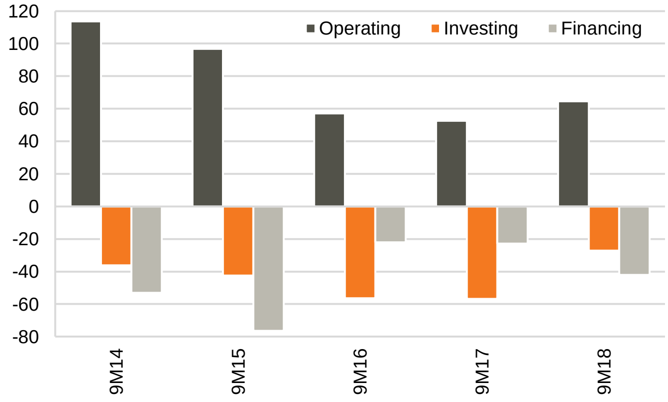
Figure 9: Profitability margins



Source: Company data

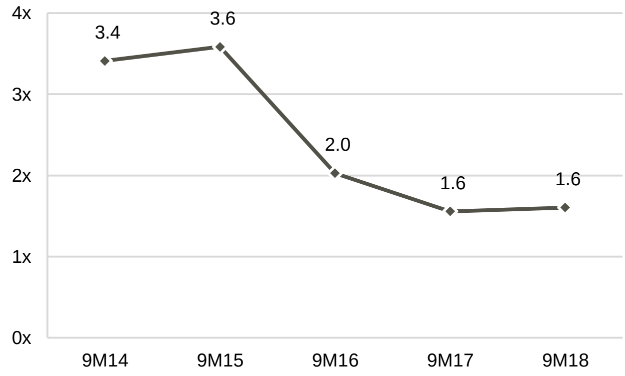
Operating cash increased 22.8% y/y to US$ 64.6mn in 9M18. Cash flow for investing activities came in at US$ 27.0 compared to US$ 56.8 last year, while cash flow from financing activities stood at US$ 42.0mn vs US$ 22.9mn in 9M17. This is explained by acquisition of two new Stadler trains from the proceeds of the new loan by GR in 2017.

Figure 10: Cash flows, US$ mn



Source: Company data

Figure 11: Adjusted EBITDA coverage ratio



Source: Company data

Fitch Ratings revised Georgian Railway's outlook to positive from stable and affirmed the rating at "B+", in November 2018. The upgrade in outlook reflected the change in the Georgian Sovereign rating (BB-/Positive) in March 2018.

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