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RESEARCH

Georgian Railway
1H17 update

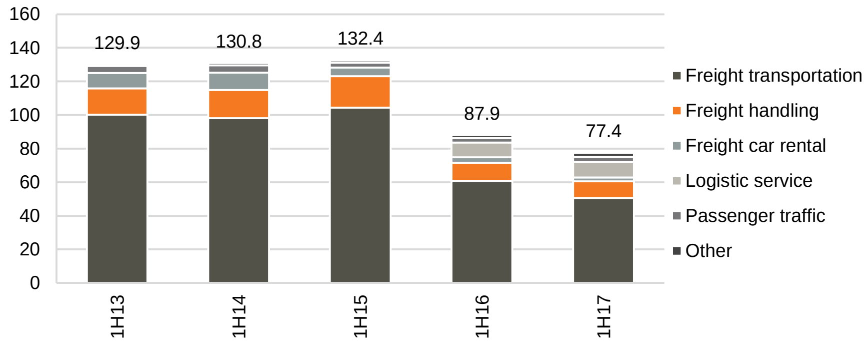
Georgia | Transportation
Georgian Railway
September 15, 2017

S&P / B+ / Outlook Stable
Fitch / B+/ Outlook Stable

GR released 1H17 unaudited results and Management Discussion and Analysis. Revenue decreased 12.0% y/y to US$ 77.4mn due to lower freight traffic volumes. Operating expenses, which are mostly fixed in GEL, decreased 10.0% y/y to US$ 71.5mn. As a result, adjusted EBITDA declined 16.1% y/y, from an already low base, to US$ 28.4mn, with the adjusted EBTDA margin down to 36.7%. Strengthening of GEL vs. US$ in 1H17 led to a non-cash FX gain of US$ 44.0mn, which propped up net income at US$ 46.2mn. The modernization project is proceeding as planned, expected to be completed by late 2019. The bypass project remains under review.

Freight transportation revenue declined 16.9% y/y to US$ 50.6mn in 1H17 from the low base of 1H16 (-41.8% y/y). Freight handling declined 7.8% y/y to US$ 9.9mn, while logistic service posted a 3.2% y/y increase to US$ 9.1mn. These three categories together accounted for 89.9% of 1H17 revenue. Freight car rental revenue decreased 27.4% y/y to US$ 2.3mn, while passenger traffic increased 14.8% y/y to US$ 3.2mn. Other revenue was up 48.4% y/y to US$ 2.3mn due to the increase in the sale of scrap.

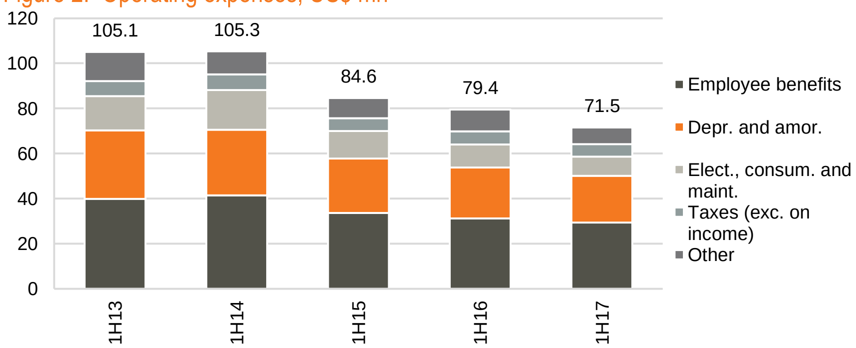
Figure 1: Revenue, US$ mn



Source: Company data

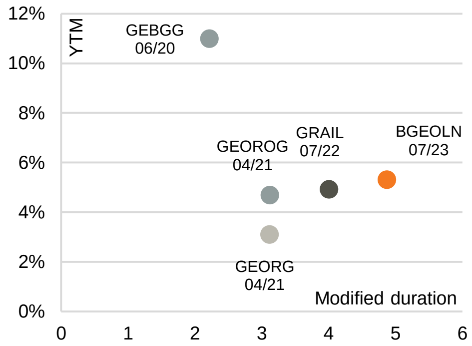
1H17 operating expenses, which are mostly GEL-denominated, declined 10.0% y/y to US$ 71.5mn, helped by the 7.4% higher average USDGEL rate in 1H17 vs 1H16. There were declines across all major expenses, but the largest contributor to the overall decline in costs was the 'Other' category, down 23.4% y/y to US$ 7.3mn, largely due to reduced logistic costs.

Figure 2: Operating expenses, US$ mn



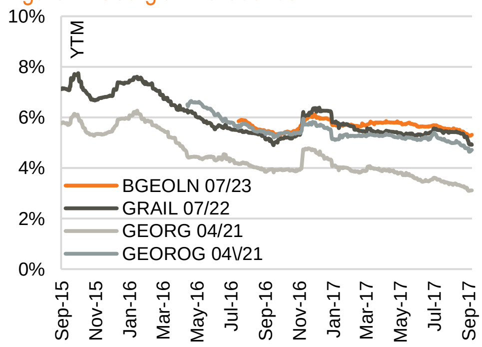
Source: Company data

Figure 3: Georgian Eurobond universe



Source: Bloomberg

Figure 4: Georgian Eurobonds



Source: Bloomberg

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

	1H16	1H17	Change, y/y
Revenue	87,928.0	77,413.5	-12.0%
EBITDA	35,032.4	30,591.5	-12.7%
EBITDA margin	*39.8%*	*39.5%*	*-32bps*
Adjusted EBITDA	33,861.3	28,423.1	-16.1%
Adjusted EBITDA margin	*38.5%*	*36.7%*	*-179bps*
EBIT	12,384.9	9,886.5	-20.2%
EBIT margin	*14.1%*	*12.8%*	*-131bps*
Net income	21,330.3	46,216.1	116.7%
Net profit margin	*24.3%*	*59.7%*	*354bps*
Assets	1,323,957.6	1,346,159.5	-1.7%
Equity	649,344.7	712,659.3	-9.8%
Liabilities	674,613.0	633,500.2	-6.1%

Source: Company data

US$-GEL	1H13	1H14	1H15	1H16	1H17
Period-end	1.65	1.77	2.25	2.34	2.41
Average	1.65	1.76	2.18	2.32	2.51

Source: NBG

Georgian Railway prepares and publishes financial statements in GEL; translations into US$ are made by Galt & Taggart.

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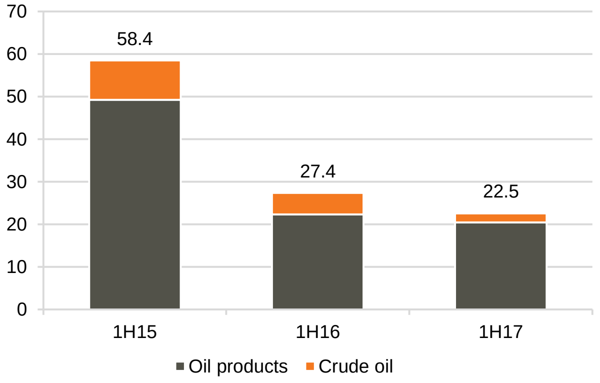
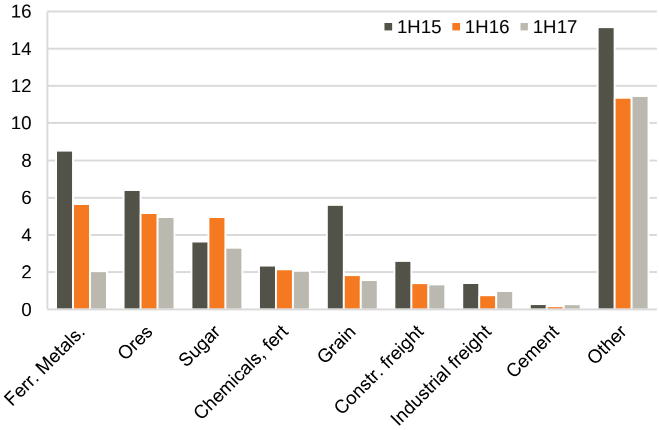
In freight transportation, the downward trend persisted in both liquid and dry cargoes. Revenue from liquid cargo transportation decreased 17.6% y/y to US$ 22.5mn, while dry cargo revenue was down 16.3% y/y to US$ 28.0mn. Crude oil transportation dropped off 57.3% y/y to US$ 2.2mn, with its share in liquid cargo revenues down to a mere 9.6%. A sharp decline (-90.0% y/y) in crude oil transportation from Turkmenistan was the main culprit. Despite higher oil products transportation volume in 1H17, oil products transportation revenue also decreased 8.5% y/y to US$ 20.4mn, as GR lowered tariffs and freight origin shifted from Azerbaijan to Kazakhstan. In dry cargo, precipitous declines in ferrous metals and scrap and sugar transportation were the leading drivers. Ferrous metals and scrap dropped 64.0% y/y to US$ 2.0mn due to an unfavorable shift in the freight destination mix, while sugar transportation shrank 32.8% y/y to US$ 3.3mn due to lower volumes to Azerbaijan.

Figure 5: Liquid cargo transportation, US$ mn



Source: Company data

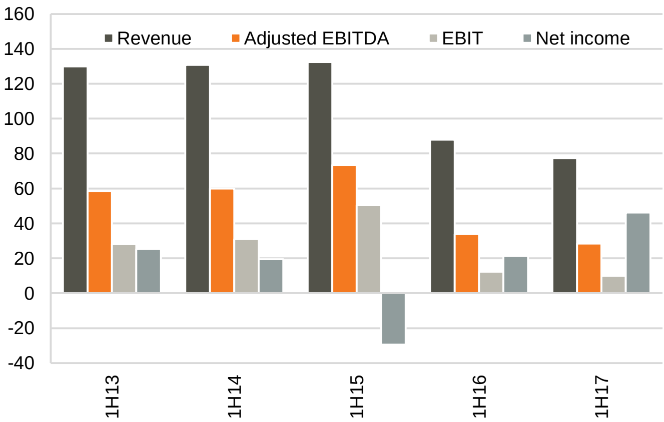
Figure 6: Dry cargo transportation, US$ mn



Source: Company data

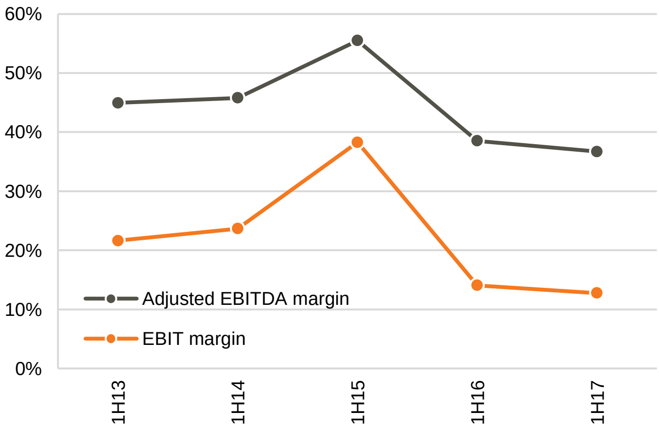
1H17 adjusted EBITDA declined 16.1% y/y to US$ 28.4mn. As a result, the adjusted EBITDA margin contracted from 38.5% in 1H16 to 36.7%. Strengthening of GEL against US$ in 1H17 led to a non-cash FX gain of US$ 44.0mn, accounted for as finance income, which propped up net income at US$ 46.2mn.

Figure 7: Income statement highlights, US$ mn



Source: Company data

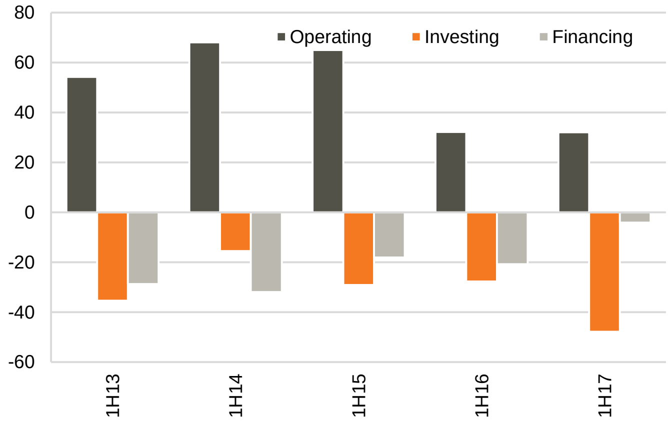
Figure 8: Profitability margins



Source: Company data

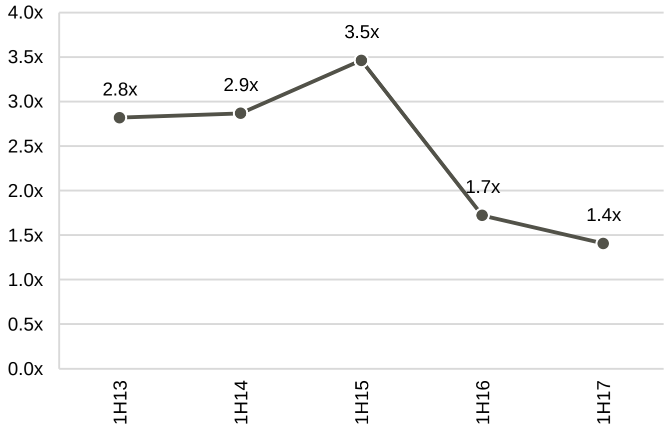
Operating cash remained relatively flat at US$ 32.0mn in 1H17. Investment in new passenger trains and significant modernization project expenses drove the 41.5% y/y increase in capital spending to US$ 50.9mn. The purchase of trains was financed by new debt, which contributed to a deterioration of the adjusted EBITDA coverage ratio from 1.7x in 1H16 to 1.4x in 1H17.

Figure 9: Cash flows, US$ mn



Source: Company data

Figure 10: Adjusted EBITDA coverage ratio



Source: Company data

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