



**Management Discussion and Analysis for
six month period ended 30 June 2013**

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1. Executive Summary

Revenue of Georgian Railway JSC (“GR” or “the Company”) for the six month period ended 30 June 2013 comprised GEL 214.9 million. This is 4.5% less than the revenue for the same period in 2012. The major change relates to the decrease in the revenue from freight car rent, which is discussed in details in the later sections.

Revenue from freight transportation (a core business of the Company) in six month period ended 30 June 2013 is GEL 165.7 million and represents 1.0% increase from 2012. In April 2013 the Company purchased Georgian Transit LLC, a company that transports largest portion of oil and oil product through Georgia, and per GR tariff policy receives discounted tariffs. Acquisition of Georgian Transit LLC contributed additional GEL 6.2 million of revenue only in the second quarter of 2013, when the transportation of oil and oil products was at a minimum level.

Salary and staff optimization project that started in 2012 went into full scale in the beginning of 2013. The project implied gradual increase of average salary, with simultaneous decrease in number of employees. Beginning of 2013 was a period when there was a social tension in the country (subsequent to the parliamentary elections in October 2012) and the decision was made to postpone optimization of number of employees until more favourable period. This decision caused increase in overall salary expenses by GEL 15.7 million in the first half of 2013 and had a respective effect on operating expenses of the period.

Adjusted EBITDA for the period comprises GEL 96.6 million, while Adjusted EBITDA margin is 45%. Respective figures for comparative period of the previous year represent GEL 130.7 million and 58%.

2. Profit & Loss Statement

In this section we present comparative consolidated IFRS income statement of the Company for the six month period ended 30 June 2013 and 2012 and discuss significant changes.

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Revenues	214,910	-4.5%	-10,220	225,130
Other income	5,439	-55.9%	-6,894	12,333
Payroll expenses	-65,876	31.3%	-15,690	-50,186
Depreciation and amortization expense	-50,305	-4.5%	2,370	-52,675
Electricity and materials used	-21,099	-14.1%	3,454	-24,553
Other expenses	-36,553	-20.3%	-6,180	-30,373
Result From Operating Activities	46,516	-41.6%	-33,160	79,676
Finance Income	7,374	-34.3%	-3,855	11,229
Finance Cost	-5,442	-12.9%	806	-6,248
Net finance income	1,932	-61.2%	-3,049	4,981
Profit before income tax	48,448	-42.5%	-36,209	84,657
Income tax	-6,592	-51.3%	6,952	-13,544
Net income	41,856	11.9%	4,438	71,113
Adjusted EBITDA	96,592	-26.1%	-34,069	130,661
Adjusted EBITDA margin	44.9%			58.0%

Following paragraphs present the analysis of the profit and loss statement of Georgian Railway JSC for the six-month period ended 30 June 2013.

2.1. Revenues

Following table sets forth revenue breakdown and comparison of 6 month periods ended 30 June 2013 and 2012. Reasoning behind each change could be observed in sections below.

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Freight transportation	165,775	1.0%	1,694	164,081
Freight handling	25,972	1.0%	259	25,713
Freight car rental	14,996	-40.6%	-10,262	25,258
Passenger transportation	7,012	-6.5%	-490	7,502
Other revenue	1,154	-55.2%	-1,422	2,576
Total Revenue	214,910	-4.5%	-10,220	225,130
Other Income	5,439	-55.9%	-6,894	12,333

2.1.1 Freight revenues

Freight transportation revenues:

Freight transportation revenues increased by 1.0 per cent (GEL 1.7 million) in the six-month period ended 30 June 2013 compared to the same period of the previous year.

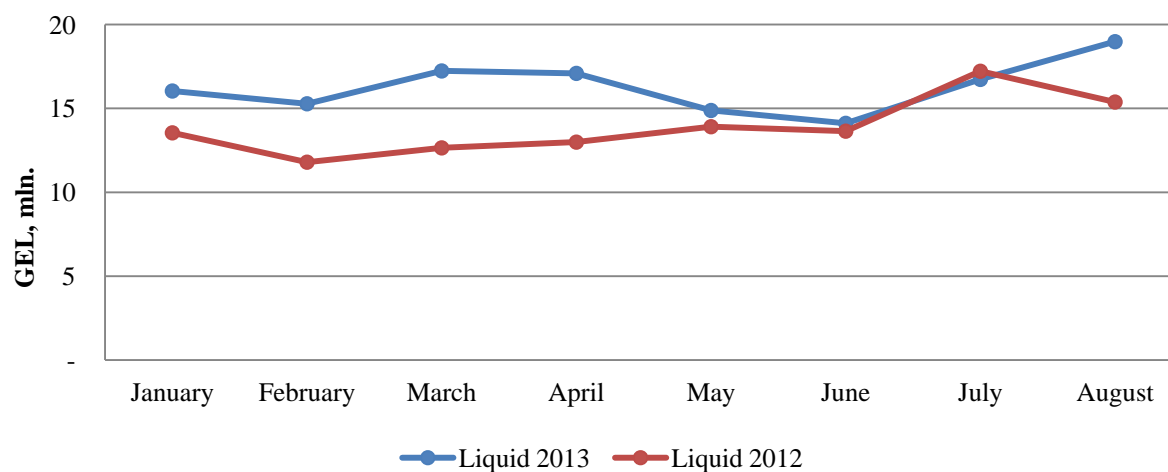
In 2013, liquid cargo contributed to 57.1 per cent of total cargo transportation revenue while dry cargo contributed to 42.9 per cent. In the first 6 month of 2012, liquid cargo contributed to 47.9% of total cargo transportation revenue and dry cargo to 52.1%. The types of freight that positively contributed to the six-month period-over-period change in freight transportation revenue mainly were Crude Oil and Oil products. This was offset by the decrease in revenue from transportation of dry cargo.

The following table sets forth freight transportation revenue by types of freight for the six-month periods ended 30 June 2013 and 2012:

GEL, Millions	Six-month periods ended 30 June			
	2013	% Change	Abs. Change	2012
Liquid Cargoes	94.6	20.4%	16.0	78.6
<i>of which</i>				
Crude Oil	34.5	4.6%	1.5	33.0
Oil Products	60.1	31.9%	14.5	45.6
Dry Cargoes	71.2	-16.9%	-14.3	85.5
<i>of which</i>				
Grain	5.6	-45.2%	-4.6	10.1
Construction Freight	5.7	9.8%	0.5	5.2
Cement	1.5	15.0%	0.2	1.3
Industrial Freight	3.4	-18.7%	-0.8	4.2
Ferrous Metals and Scrap	8.6	-0.6%	-0.1	8.6
Ores	16.2	-22.5%	-4.7	20.9
Sugar	5.8	-25.2%	-1.9	7.7
Chemicals, fertilizers	3.4	-40.0%	-2.3	5.7
Other	21.1	-3.2%	-0.7	21.8
Total	165.8	1.0%	1.7	164.1

Liquid cargo revenues:

The following graph presents distribution of revenue from liquid cargo transportation by months, for the eight month periods ended 31 August 2013 and 2012:

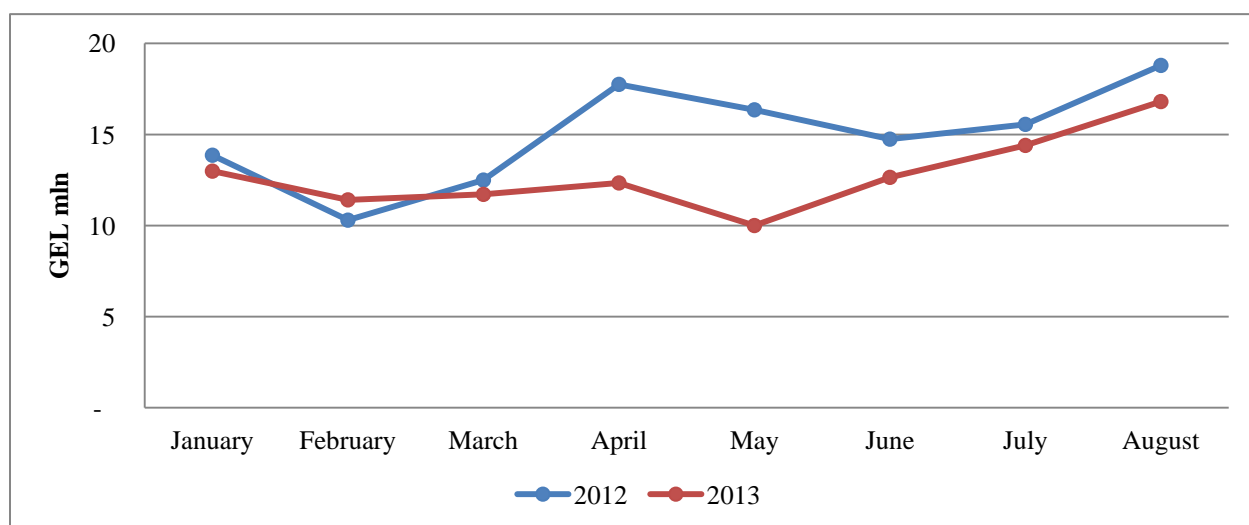


Second quarter decrease is related to maintenance works on oil fields located in Kazakhstan. Starting from Q3, oil production was renewed in full scale, which contributed to the increasing trend of revenues in July and August of 2013.

It should be noted that significant effort was done to attract new liquid cargo on Georgian railway. Mainly, in September, the Company already signed agreement on transportation of Kazakh crude oil from Zhanazhol oil fields and mazut. Transportation of crude oil from Zhanazhol oil fields started in September (additional 150,000 tons per month) and transportation of mazut will start in October 2013 (additional 120,000 tons per month). Moreover, construction of Methanol plant in Azerbaijan is already completed and additional volumes of methanol are expected in the 4th quarter of 2013.

Dry cargo revenues:

The following graph shows monthly revenues from dry cargo transportation for the periods ended 31 August 2013 and 2012:



Dry cargo volumes and revenues in the six month period ended 30 June 2013 decreased by 17.1 per cent and by 16.8 per cent respectively. Reduction mainly relates to the transportation of grain, construction materials and ore products. For reasons behind mentioned decrease please refer to section “Freight traffic data” of this report.

Starting from July, dry transportation increased compared to the previous months. Management believes that dry cargo transportation will show significantly improved performance in H2 2013 compared to the first half of the same year.

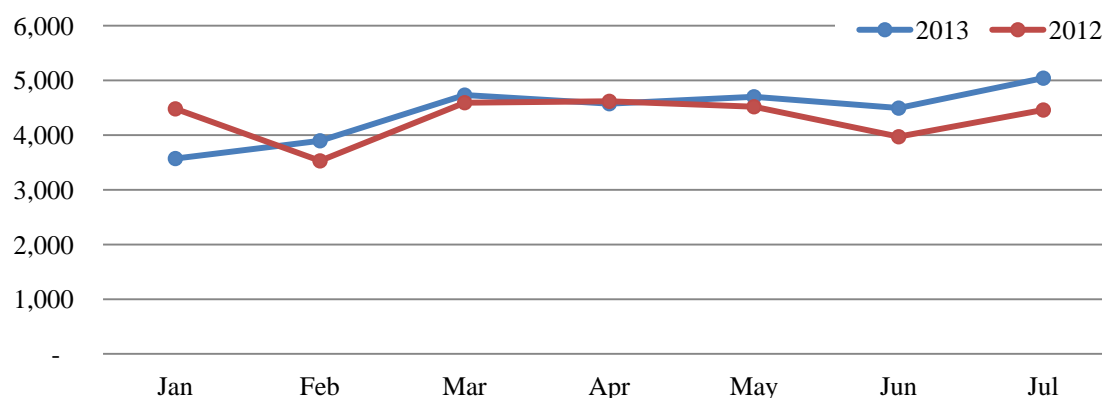
Freight handling revenue:

The following table sets forth the revenues from freight handling for the six-month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			2012
	2013	% Change	Abs. Change	
Freight handling	25,972	1.0%	259	25,713

Revenue from freight handling increased by 1.0 per cent (GEL 0.3 million) in the six-month period ended 30 June 2013 compared to the same period of the previous year. This is mostly attributable to the optimization of station service tariffs. Tariff for station services was increased to USD 1.7 per ton for GR's own diesel locomotives instead of USD 1.6 per ton. For customers' own diesel locomotives, tariffs increased to USD 0.6 per ton instead of USD 0.55 per ton. Delay of customers' own railcars in GR's stations increased to GEL 50 per day instead of GEL 20 per day. Assigning GR's railcars for transportation to Afghanistan destination also increased by USD 100\$ per railcar sent. This was offset by the decrease in transportation volumes.

The following graph shows comparison of freight handling revenue by months for the seven-month period ended 31 July of years 2013 and 2012:



Freight car rental revenue:

The following table sets forth the revenues from freight car rental for the six month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			2012
	2013	% Change	Abs. Change	
Freight car rental revenue	14,996	-40.6%	-10,262	25,258

Revenue from freight car rental decreased by 40.6 per cent (GEL 10.3 million) in the six month period ended 30 June 2013 compared to the same period in 2012. The decrease was primarily due to the additional diesel locomotives acquired by Turkmenistan Railway in order to improve turnover of the

cargo. Previously GR's wagons were delayed in Turkmenistan due to the bottlenecks on Afghanistan border. When railcars are delayed for 30-45 days, freight car rental daily tariff is multiplied by a coefficient of 1.3, while for the delay of more than 45 days the tariff triples. As the bottlenecks were dealt with by Turkmenistan, turnover improved significantly and railcar delays decreased, returning the tariff to normal amounts. In the first six months of 2013 freight car rental revenue from Turkmenistan decreased to GEL 2.5 million from GEL 7.5 million in the same period of 2012. This has a positive effect on the wagon turnover and capacity for Georgian Railway, eliminating the possible need for future investments into the railcars.

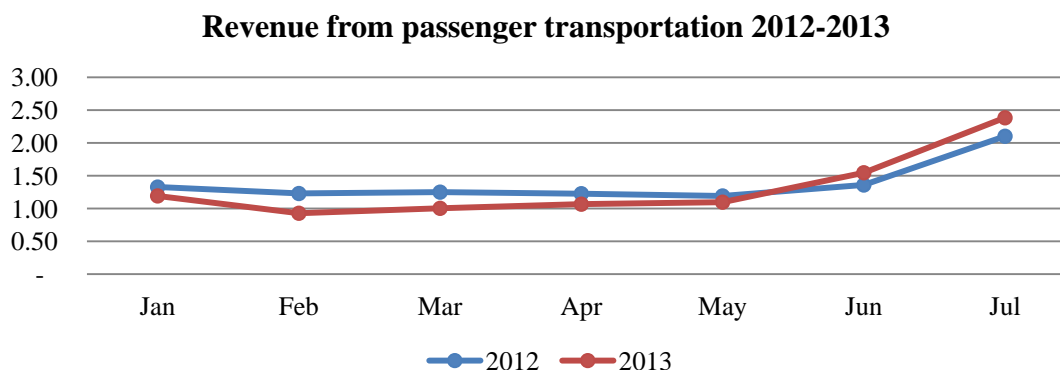
2.1.2. Passenger revenues

The following table sets forth the revenues from passenger transportation for the six-month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Passenger revenues	7,012	-6.5%	-490	7,502

Passenger revenues decreased by 6.5 per cent (GEL 0.5 million) in the six-month period ended 30 June 2013 compared to the same period of the previous year. In the first half of 2013, GR transported 5.9 per cent less passengers than in the same period of 2012, causing respective decrease in revenue. The reason for the decreased transportation was the reduced number of passenger railcars in the first months of 2013, part of which became obsolete. To overcome the deficit of wagons the Company is negotiating a contract for the leasing of additional 38 wagons for passenger transportation. Part of this new fleet is expected to be delivered in Q4 2013. Starting from mid June 2013, revenue from passenger transportation increased and exceeded the level of previous year. This was due to additional new electric trains on main-line route, namely the addition of two trains per day serving this direction.

The following graph shows distribution of revenues from passenger transportation by months in eight month periods ended 31 August 2013 and 2012:



2.1.3. Other revenues

The following table sets forth other revenue for the six month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Other revenue	1,154	-55.2%	-1,422	2,576

Other revenues comprise of items such as: - revenue from rent of space in buildings, sale of scrap, repair services and such. Decrease in six-month period ended 30 June 2013 compared to the same period in 2012 was caused by the delay in scrap sales.

2.1.4. Other income

The following table sets forth other income for the six month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Other Income	5,439	-55.9%	-6,894	12,333
<i>Of which:</i>				
Continuing Operations	5,038	-52.7%	-5,605	10,643
Non-Continuing Operations	401	-76.3%	-1,289	1,690

Other income mostly comprises of items such as penalties accrued on debtors or creditors, gain on inventory revaluation, revenue from communication services, revenue for inflicted loss on company from third parties, revenue from the surplus of inventory, revenue from heavy equipment services and other. In the six-month period ended 30 June 2013 other income decreased by 55.9 per cent (GEL 6.9 million), compared to the same period of the previous year.

In order to better illustrate the operational profitability of the company, GR divides other income into two categories: income which is reoccurring between the periods due to their nature (for example such are penalties on creditors and debtors, different types of non-core revenues and some other items) – this is classified as income from continuing operations. Second type of other income comes from one time sources, such as provisions, gain/loss on inventory revaluation, revenue from gifts and other items, which are not expected to reoccur in the following periods.

The decrease in other income was mainly caused by the decrease in continuing operations by 52.7 per cent (GEL 5.6 million) This was mainly caused by the reduced accrued penalty on creditors (GEL 4.3 million), which was high in H1 2012 due to only one case. This was no longer present in H1 2013, thus causing the decrease.

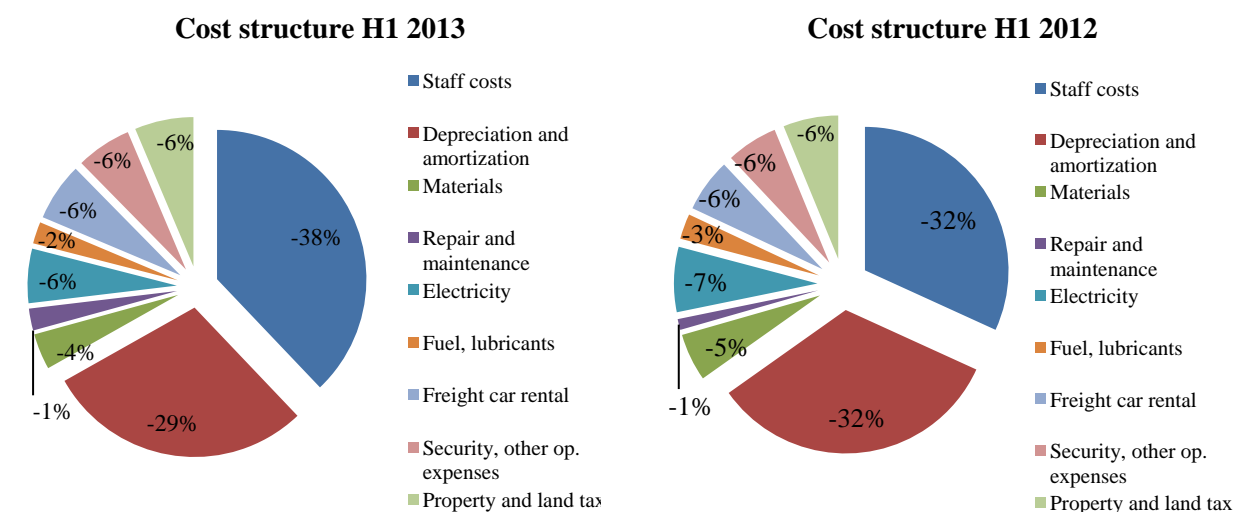
2.2. Operating expenses

The following table sets forth total expenses of Georgian Railway JSC, excluding Finance Costs, Interest Income/Expense and Profit Tax, for the six month periods ended 30 June of years 2013 and 2012:

	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Staff costs	-65,876	31.3%	-15,690	-50,186
Depreciation and amortization	-50,305	-4.5%	2,370	-52,675
Materials	-6,774	-20.1%	1,706	-8,480
Repair and maintenance	-4,130	114.1%	-2,201	-1,929
Electricity	-10,221	-11.7%	1,357	-11,578
Fuel, lubricants	-4,104	-8.7%	391	-4,495
Freight car rental	-10,931	15.1%	-1,434	-9,497
Security, other op. expenses	-10,410	13.9%	-1,273	-9,137
Property and land tax	-11,081	13.0%	-1,271	-9,810
Total	-173,832	10.2%	-16,045	-157,787

Total expenses for six month period ended 30 June 2013 increased by 10.2 per cent (GEL 16.0 million) compared to the six month period ended 30 June 2012, the main reasons of which was the increase in salary expense.

The following charts sets forth the cost structure for the six month period ended 30 June of years 2013 and 2012:



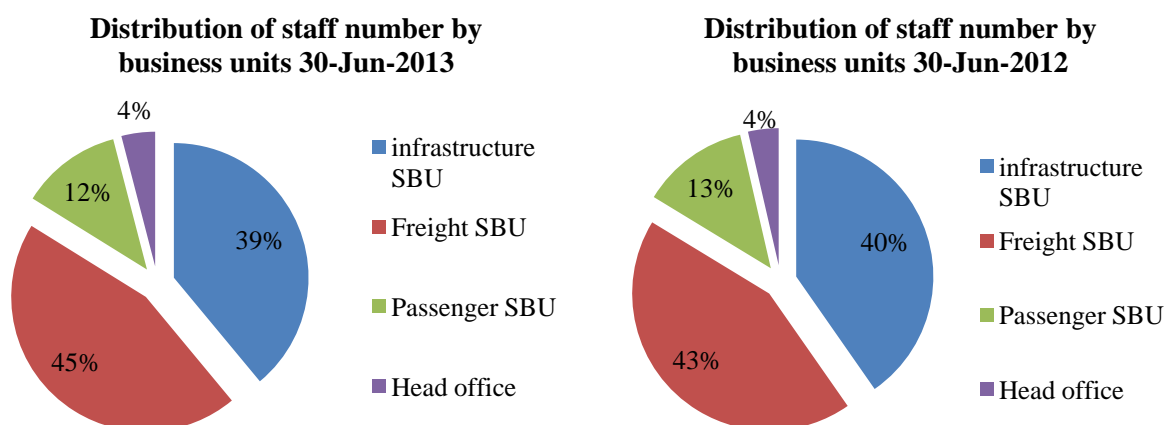
2.2.1. Staff cost

The following table sets forth staff costs for the six month period ended 30 June for years 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Staff cost	-65,876	31.3%	-15,690	-50,186

Main reason for the increase in staff costs by 31.3% (GEL 15.7 million) was increase in salary expenses at the end of 2012 and in the first months of 2013. The reason behind this was the faster pace of our ranking program. According to the initial plan, number of employees was being reduced, while the average salary was being gradually increased. The increase was applied in a manner that the total salary would stay mostly flat. However, after the elections there were social tensions in the country. As a result, by the end of 2012 GR shareholder has made a decision to complete salary ranking process all at once without staff lay-offs. Respectively, the decision was followed by an increase in salary expense. Management believes that there is a possibility to decrease the salary expense when the political situation becomes more stable. Employee number at the end of the first six months of 2013 was equal to 12,622 and accordingly at the end of first six month of 2012 the number of employees was 12,572. Average salary at the end of first six month of the year 2013 was GEL 870 compared to GEL 665 in the same period of 2012.

Following charts show the distribution of staff number by strategic business units and head office of the Company (excluding subsidiaries):



The following table sets forth average salaries for the six-month period ended 30 June 2013 and twelve-month period ended 30 June 2012:

'GEL	6 month period ended 30 June 2013	% Change	Abs. Change	6 month period ended 30 June 2012
Average Salary	870	30.8%	205	665

2.2.2. Materials, Repair and Maintenance Expenses

The following table sets forth materials and repair and maintenance expenses for the six month period ended 30 June for years 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Materials	-6,774	-20.1%	1,706	-8,480
Repair and maintenance	-4,130	114.1%	-2,201	-1,929
TOTAL	-10,904	4.8%	-495	-10,409

Total expense for materials and repair and maintenance services for the six month period ended 30 June 2013 increased by 4.8 per cent (GEL 0.5 million) compared to the six-month period ended 30 June 2012. Materials expenses decreased by 20.1 per cent (GEL 1.7 million). Material expenses are not evenly distributed during the year and this variance for the first six months is not unusual. Repair and maintenance expense increased by 114.1 per cent in the first six months of 2013 compared to the same period in 2012. High expense in 2013 was partly caused by the new types of repairs, namely the replacement of Twin-Heads on freight and passenger railcars. Such repairs were not present in H1 2012.

2.2.3. Electricity and Fuel Expenses

The following table sets forth electricity expense for the six month period ended 30 June for years 2013 and 2012:

Electricity Expense:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Electricity	-10,221	-11.7%	1,357	-11,578

Electricity expense for the six-month period ended 30 June 2013 decreased by 11.7 per cent (GEL 1.4 million) compared to the six-month period ended 30 June 2012. Change in electricity expense is a function of two major variables: price per purchased KWh and consumed electricity, which in the six month period ended 30 June 2013 decreased by 11.4 per cent (15.3 GWh), to ca. 119.0 GWh compared to the consumption in the six-month period ended 30 June 2012. The decrease was mainly caused by the increase of the number of railcars in one train composition and other optimizations in the Company operations.

The following table shows purchased electricity and weighted average tariff paid by Georgian Railway JSC:

	2013			2012		
	GWh	Amount paid (GEL m.)	WA.tariff (Tetri per KWh)	GWh	Amount paid (GEL m.)	WA tariff (Tetri per KWh)
January	23.6	2.09	8.85	24.9	2.18	8.76
February	20.6	1.82	8.85	21.3	1.89	8.87
March	21.9	1.92	8.76	23.3	2.05	8.80
April	19.5	1.68	8.58	21.7	1.9	8.76
May	16.7	1.36	8.12	22.0	1.81	8.23
June	16.7	1.36	8.15	21.1	1.77	8.39
Total	119.0	10.22	8.59	134.3	11.58	8.62

The following graph shows comparison of purchased volumes by months for the six-month period ended 30 June of years 2013 and 2012:

Fuel expenses:

The following table sets forth fuel expense for the six-month period ended 30 June for years 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Fuel and Lubricants	-4,104	-8.7%	391	-4,495

Fuel (and lubricants) expense in the six-month period ended 30 June 2013 decreased by 8.7 per cent compared to the six-month period ended 30 June 2012. The main reason for the decrease was the fact that customers began usage of their own diesel locomotives rather than GR's. As diesel locomotives are mainly used for freight handling operations, fuel expense is closely tied to the level of their operations.

2.2.4. Freight car rental expense

The following table sets forth freight car rental expense for the six-month period ended 30 June for years 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Freight car rental	-10,931	15.1%	-1,434	-9,497

Freight car rental expenses for the six-month period ended 30 June 2013 increased by 15.1 per cent compared to the six-month period ended 30 June 2012. The increase was mainly due to the rental of

additional 425 tank cars by Georgian Railway in mid 2012 to decrease the deficit of tank cars in the transportation corridor. The 425 tank car rental expense in first six month of 2012 was GEL 1.1 million which increased to GEL 5.3 million in the same period of 2013. This increase was partly offset by privatization of Ukrainian, Russian and Kazakh wagon fleet, causing the decrease of freight car rental fees that GR has to pay when using other railway's wagons for transportation on its territory.

2.2.5. Security and other expenses

The following table sets forth security and other operating expenses for the six month period ended 30 June for years 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Security	-3,601	-1.0%	35	-3,636
Other op. expenses	-6,809	23.8%	-1,308	-5,501
Total	-10,410	13.9%	-1,273	-9,137

Total security and other operating expenses for the six-month period ended 30 June 2013 increased by 13.9 per cent (GEL 1.3 million) compared to the six month period ended 30 June 2012. Other operating expenses mainly consist of such items as: municipal, communication, legal costs, consultancy, membership fees, administrative expenses and etc. The increase in other operating expenses was mainly caused by the purchase of new subsidiary (Georgia Transit LLC, starting from April 2013), whose freight handling services in Batumi were served by third party companies.

2.2.6. Property and land taxes

The following table sets forth the breakdown of Property and Land taxes for the six month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% change	Abs. change	2012
Property tax	-5,841	22.7%	-1,079	-4,762
Land Tax	-4,604	-0.8%	36	-4,640
Other taxes	-636	55.9%	-228	-408
Total	-11,081	13.0%	-1,271	-9,810

Property tax increased due to the increase in Construction in Progress due the Modernization and Bypass projects. Other taxes consists additional expenses for tax purposes.

2.3. Finance costs and income

The following table sets forth the breakdown of financial costs and income for the six-month periods ended 30 June 2013 and 2012:

'000 GEL	6 month period ended 30 June			2012
	2013	% Change	Abs. Change	
Interest income	6488	10.4%	611	5,877
FX gain	886	-83.4%	-4,466	5,352
Provisions	-68	100.0%	-68	0
Impairment loss on trade receivables	-1,235	-80.1%	4,978	-6,213
Interest expense	-4,208	11849.3%	-4172	-35
Net finance income	1,863	-62.6%	-3117	4,981

Finance income in the six-month period ended 30 June 2013 decreased by GEL 3.1 million compared to the six-month period ended 30 June 2012. Main reason was FX gain, which has decreased significantly. This was caused by the revaluation of Eurobonds on the Company's balance sheet, which are denominated in USD. In the first six month in 2012 the appreciation of GEL against USD was 1.5 per cent, while in the same period of 2013, such appreciation was only 0.4%. Subsequently, this had a lower impact on liability revaluation.

Another reason for the decrease of net finance income was interest expense. Interest expense of Georgian Railway is mostly being capitalized according to the IFRS. During the construction phase of the projects for which the proceeds of interest bearing loan has been used, interest expense is being capitalized, thus not having an effect on P&L. Before the USD 500 million July 2012 issue, 100% of interest expense was capitalized. Currently capitalization rate is lower, which is calculated periodically according to IFRS guidelines.

2.4. Income Tax Expense

The following table shows the Income Tax Expense for the six-month period ended 30 June of years 2013 and 2012:

'000 GEL	6 month period ended 30 June			2012
	2013	% change	Abs. change	
Income Tax Expense	-6,592	-51.3%	6,952	-13,544

Decrease in income tax expense is in line with the decreased income before taxes in the six month period ended 30 June, 2013.

2.5. Profitability

The following Table show the calculation of Adjusted EBITDA and Adjusted EBITDA margin for the six-month periods ended 30 June, 2013 and 2012:

'000 GEL	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Revenues	214,910	-4.5%	-10,220	225,130
Other income	5,439	-55.9%	-6,894	12,333
Expenses	-173,833	10.2%	-16,046	-157,787
Result from Operating Activities	46,516	-41.6%	-33,160	45,981
Depreciation add-back	50,305	-4.5%	-2,370	52,675
Non-continuing operations from other income	-401	-76.3%	1,289	-1,690
Write-offs	172	100.0%	172	0
Adjusted EBITDA	96,592	-26.1%	-34,069	130,661
Adjusted EBITDA Margin	44.9%			58.0%

Adjusted EBITDA for the six-month period ended 30 June 2013 amounted to GEL 96.6 million, representing a decrease of 26.1 per cent (GEL 34.1 million) compared to the same period of previous year. Adjusted EBITDA margin reached 44.9 per cent, compared to the 58.0 per cent for the six-month period ended 30 June 2012.

2.6. Company's Leverage

Maintaining the maximum rating is one of the main priorities for the company and the shareholder. The company believes that it is able to maintain leverage at a healthy level, in order to support company's rating and the interests of our investor. GR expects that 2013 will be a peak for its leverage, with stable decrease in the following year. However, management is confident that it will be able to maintain healthy headroom under its covenants for the Eurobonds. There are multiple reasons to support management's confidence:

- 1) Flexibility in CAPEX – Significant CAPEX which was planned to be paid for Bypass project is expected to be delayed and the negotiations for this are already taking place. The payments are expected to be delayed by up to 3 years from 2013. As the project is without operational benefits for the Georgian Railway, this delay is positive for the company, producing additional free cash on its bank accounts to support the leverage.
- 2) Additional cargo – Company has signed a contract for transportation of Mazut from Kazakhstan significantly increasing expectations for liquid cargo transportation. Additional 150 thousand tons per month of crude oil from Zhanazhol oil field. Additional liquid volumes from transportation of Azerbaijan Methanol.
- 3) Support from shareholders – There is support from the shareholder in form of strictly performance based dividend policy, giving the company additional resources of cash on its balances, decreasing the expected leverage at the end of the year.

2.7. Future plans and projects

Management believes that the vertical integration of the Company will enhance competitiveness of Georgia transportation corridor and will attract new cargo currently transported through other corridors and modes of transport. In this respect, the Company is currently involved in planning and construction of new projects:

Intermodal stations in Batumi, Poti and Vale are being planned to be built with the GR as the 100% investor and owner. This is expected to add additional dry cargo volumes to Company's transportation from early 2014. Construction works in Batumi are already started. Each point of construction is expected to take approximately 6 month to build with an investment cost of USD 5 million each. Total additional cargo expected to flow from the projects is about 400-500 thousand per year.

GR intends to enter in a ferry business on the Black Sea. The idea is to offer competitive prices to cargo owners from overseas. The announcement on Expression of Interest for the GR to participate in the business has just been released. The ferry will operate on the Poti-Kavkaz (Russia) direction to serve newly opened Russian market for Georgia. Operations are expected to start from 2014 with additional transported volumes of 100-150 thousand tons per year.

3. Cash flows

'000GEL	<u>Six-month period ended 30 June 2013</u>	<u>Six-month period ended 30 June 2012</u>
Cash flows from operating activities		
Cash receipts from customers	209,737	237,040
Cash paid to suppliers and employees	(104,722)	(107,930)
Cash flows from operations before income taxes and interest paid	105,015	129,110
Income tax paid	(15,324)	-
Interest paid	-	-
Net cash from operating activities	89,691	129,110
Cash flows from investing activities		
Acquisition of property, plant and equipment	(106,133)	(161,432)
Proceeds from sale of property, plant and equipment	-	-
Purchase of a company share	(48)	-
Decrease/Increase in term deposits	40,781	67,723
Increase in restricted cash	-	(219)
Interest received	6,753	6,385
Net cash used in investing activities	(58,647)	(87,543)
Cash flows from financing activities		
Proceeds from borrowings	-	190
Repayment of borrowings	(17)	(489)
Interest paid	(35,444)	(20,660)
Dividends paid	(12,000)	(28,000)
Contribution of cash by owners	-	-
Distribution of cash to owners	-	(3,101)
Net cash from /(used in) financing activities	(47,461)	(52,060)
Net increase/(decrease) in cash and cash equivalents	(16,417)	(10,493)
Cash and cash equivalents at 1 January	115,076	61,553
Effect of exchange rate fluctuations on cash and cash equivalents	(720)	238
Cash and cash equivalents at 31 December	97,939	51,298
Bank deposits	58,780	8,725
Restricted Cash	-	(3,181)
Total Cash and cash equivalents	156,719	63,204

The Company's cash flow management policies focus on maintaining a flexible capital expenditure programs and maximizing cash flow generation, in line with potential future changes in passenger numbers and freight volumes transported. Through these policies, management aims to permit both the maintenance of infrastructure and the pursuit of selective growth opportunities. Management seeks to rely on operating cash flows to finance capital expenditures, but also seeks to maintain a diversified funding structure for strategic initiatives.

3.1. Net cash from operating activities

Following table shows cash from operating activities for the six-month periods ended 30 June 2013 and 2012:

'000GEL	Six-month period ended 30 June 2013	Abs. Change	% change	Six-month period ended 30 June 2012
Cash flows from operating activities				
Cash receipts from customers	209,737	(27,303)	-12%	237,040
Cash paid to suppliers and employees	(105,722)	2,208	-2%	(107,930)
Cash flows from operations before income taxes and interest paid	105,015	(24,095)	-19%	129,110
Income tax paid	(15,324)	(15,324)	-	-
Interest paid	-	-	-	-
Net cash from operating activities	89,691	(39,419)	-31%	129,110

Net cash from operating activities in six-month period ended 30 June 2013 has decreased by 31 per cent (GEL 39.4 million) compared to the same period in 2012. This was mainly caused by the decrease in cash receipts from customers by 12 per cent (GEL 27 million) and by increase in income tax paid by GEL 15.0 million.

Decrease in cash receipts from customers was mainly caused by reimbursement of VAT surplus in 2012 of a total GEL 23 million to compensate the accumulated VAT from implementation of capital projects. In 2013 such reimbursements have not taken place, however management expects to receive such reimbursement by the end of the year, in total amount of GEL 16 million (GEL 7.5 million will be reimbursed by the end of September 2013).

Increase in income tax was caused by the following: Payments for income tax are made through the year in advance and based on previous years' results. These advance payments can cause both deficit and surplus of income tax paid, which is apparent after the total advance payments are compared to the actual performance of the company at the end of the year. In 2012, the Company had a significant surplus due to which the payment of income tax was only GEL 8 million. In 2013, surplus of income tax decreased

compared to 2012, causing a payment of GEL 15 million. No further payments of income tax are expected to take place in 2013.

3.2. Net cash used in investing activities

Following table shows cash from investing activities for the six-month periods ended 30 June 2013 and 2012:

Cash flows from investing activities	Six-month period ended 31 March 2013	Abs. change	% change	Six-month period ended 31 March 2012
Acquisition of property, plant and equipment	(106,133)	55,299	-34%	(161,432)
Proceeds from sale of property, plant and equipment	-	-	-	-
Purchase of a company share	(48)	(48)	-	-
Decrease/Increase in term deposits	40,781	(26,942)	-40%	67,723
Increase in restricted cash	-	219	-	(219)
Interest received	6,753	368	6%	6,385
Net cash used in investing activities	(58,647)	29,896	-34%	(87,543)

Net cash used in investing activities has decreased by 34 per cent (GEL 29.7 million), which was mainly caused by decrease in acquisition of property, plant and equipment by 34 per cent (GEL 55 million).

Total effect was partly offset by the decrease in cash from term deposits by 40 per cent (GEL 26.9 million), which represents just a reclassification of term deposits to cash and cash equivalents and does not have an impact on company's total cash.

Cash paid for Bypass project was GEL 21.7 million in the six-month period ended 30 June 2013 and GEL 28.7 million in the six-month period ended 30 June 2012. Cash paid for Modernization Project was GEL 28.3 million in the six-month period ended 30 June 2013 and GEL 53.5 million in the six-month period ended 30 June 2012.

3.3. Net cash used in financing activities

Following table shows cash from financing activities for the six-month periods ended 30 June 2012 and 2011:

Cash flows from financing activities	Six-month period ended 30		% change	Six-month
	June 2013	Abs. change		period ended 30
				June 2012
Proceeds from borrowings	-	(190)	-	190
Repayment of borrowings	(17)	472	-97%	(489)
Interest paid	(35,444)	(14,784)	72%	(20,660)
Dividends paid	(12,000)	16,000	-57%	(28,000)
Contribution of cash by owners	-	-	-	-
Distribution of cash to owners	-	3,101	-	(3,101)
Net cash used in financing activities	(47,461)	4,599	-9%	(52,060)

The Company's total net cash used in financing activities decreased by 9 per cent or GEL 4.6 million. This was mainly caused by decrease in dividends paid by 57 per cent (GEL 16 million) and by decrease in distribution of cash to owners (GEL 3 million), which was attributable to the disposal of Batumi Tower project in 2012. Total decrease of net cash used for financing was partly offset by the increase in interest paid by 72 per cent (GEL 14.8 million). The reason behind this is the increased amount of debt due to the new issue of Eurobonds (USD 500 million), which was offset by the tender of old Eurobond issue: 88.9 per cent of USD 250 million was bought back by the Company alongside with the new bond issue.

Company's dividend payments are restricted by its covenants for the bonds, according to which 50% of previous year's consolidated net income is the maximum amount that can be paid in any given year. In 2013, up to the release date of this report, the Company has made a dividend distribution of GEL 18 million. Shareholder supports the company's financial stability and the future dividends are subject to operational performance.

4. Balance Sheet

'000GEL	30 June 2013	Abs. change	% change	31 Dec 2012
ASSETS				
Non-current assets				
Property, plant and equipment	2,268,056	70,821	3%	2,197,235
Deferred tax assets	1,557	0	0%	1,557
Other non-current assets	270,357	(10,573)	-4%	280,884
Total non-current assets	2,539,970	60,351	2%	2,479,676
Current assets				
Inventories	47,624	12,053	34%	35,571
Current tax assets	9,724	-	-	-
Trade and other receivables	45,577	6,324	16%	39,253
Prepayments and other current assets	44,520	(17,128)	-28%	61,648
Term deposits	58,780	(41,541)	-41%	100,321
Cash and cash equivalents	97,939	(17,137)	-15%	115,076
Total current assets	304,164	(47,705)	-14%	351,869
Total assets	2,844,134	(12,589)	0.4%	2,831,545
EQUITY AND LIABILITIES				
Equity				
Share capital	1,049,789	38	0%	1,049,751
Non-cash owner contribution reserve	31,673	0	0%	31,673
Retained earnings	471,222	21,846	5%	449,376
Total equity	1,552,684	21,884	-1%	1,530,800
Non-current liabilities				
Loans and borrowings	868,080	-2,854	0%	870,934
Advance received from the Government	231,592	0	0%	231,592
Trade and other payables	52	0	0%	52
Deferred tax liabilities	59,861	2,559	4%	57,302
Total non-current liabilities	1,159,585	(295)	0%	1,159,880
Current liabilities				
Loans and borrowings	31,880	(1,540)	-5%	33,420
Trade and other payables	69,496	(12,149)	-15%	81,645
Liabilities to Government	11,926	(1,030)	-8%	12,956
Provisions	4,201	69	2%	4,132
Current tax liabilities	-	(1,542)	-100%	1,542
Dividends payable	6,449	-	-	-
Other current liabilities	7,913	743	10%	7,170
Total current liabilities	131,865	(9,000)	-6%	140,865
Total liabilities	1,291,450	(9,295)	-1%	1,300,745
Total equity and liabilities	2,844,134	12,589	0.4%	2,831,545

4.1 Non-current Assets

The following table sets forth breakdown of non-current assets as of 30 June 2013 and 31 December 2012:

'000GEL	30 June 2013	Abs. change	% change	31 Dec 2012
ASSETS				
Goodwill	46	-	-	-
Property, plant and equipment	2,268,056	70,821	3%	2,197,235
Deferred tax assets	1,557	0	0%	1,557
Other non-current assets	270,311	(10,573)	-4%	280,884
Total non-current assets	2,512,331	60,294	2%	2,479,676

Total non-current assets increased by 2 per cent (GEL 60.3 million) as at the 30 June 2013, comparing to the 31 December 2012. The increase was mainly caused by increase in property, plant and equipment by 3 per cent (GEL 70.8 million). This increase was due increase in construction in progress within the framework of Modernization and Tbilisi Bypass project. Acquisition of other railway assets also contributed to the increase in PPE. Total increase of non-current assets was partly offset by decrease in other non-current assets by 4 per cent (GEL 10.6 million) caused by the decrease in prepayments for wagon repairs, due to completed works.

4.2 Current Assets

The following table sets forth breakdown of current assets as of 30 June 2013 and 31 December 2012:

'000GEL	30 June 2013	Abs. change	% change	31 Dec 2012
Inventories	47,624	12,053	34%	35,571
Current tax assets	9,724	9,724	-	-
Trade and other receivables	45,577	6,324	16%	39,253
Prepayments and other current assets	44,520	(17,128)	-28%	61,648
Term deposits	58,780	(41,541)	-41%	100,321
Cash and cash equivalents	97,939	(17,137)	-15%	115,076
Total current assets	304,164	(47,705)	-14%	351,869

Total current assets decreased by 14 per cent (GEL 47.7 million) as at the 30 June 2013 comparing to the 31 December 2012. The decrease was mainly caused by the decrease in cash and cash equivalents and term deposits. The decrease was mainly caused by implementation of capital projects such as Bypass and Modernisation and other capital expenditure needs. The decrease was partially offset by the increase in

inventories, trade and other receivables and by increase in current tax asset due to the advance payment of income tax.

4.3 Equity

The following table sets forth breakdown of equity as of 30 June 2013 and 31 December 2012:

'000GEL	30 June 2013	Abs. change	% change	31 Dec 2012
Share capital	1,049,789	38	0%	1,049,751
Non-cash owner contribution reserve	31,673	0	0%	31,673
Retained earnings	471,222	21,846	5%	449,376
Total equity	1,552,684	21,884	1%	1,530,800

Total equity increased by 1 per cent (GEL 21.9 million) as at the 30 June 2013, comparing to the 31 December 2012. The increase was caused by an increase in retained earnings by 5 per cent (GEL 21.9 million) due to net income in the six-month period, partly offset by dividend payments.

4.4 Non-current liabilities

The following table sets forth breakdown of non-current liabilities as of 30 June 2013 and 31 December 2012:

'000GEL	30 June 2013	Abs. change	% change	31 Dec 2012
Loans and borrowings	868,080	-2,854	0%	870,934
Advance received from the Government	231,592	0	0%	231,592
Trade and other payables	52	0	0%	52
Deferred tax liabilities	59,861	2,559	4%	57,302
Total non-current liabilities	1,159,585	(295)	0%	1,159,880

Total decrease in non-current liabilities was 0.03 per cent as of 30 June 2013, comparing to the 31 December 2012. Increase in deferred tax a liability which originates from temporary differences between tax asset base and IFRS asset base was offset by decrease in loans and borrowings which was caused by the difference in USD/GEL exchange rate between 31 Dec 2012 and 30 June 2013, as the liabilities are mostly in USD.

Advance received from the Government represents a payment for the land that will be freed up once the Bypass project is completed. As already stated, Bypass project is negotiated to be postponed for about 3

years. Per agreement with the government, in case the project is cancelled, the liability indicated in the balance sheet will be moved to the retained earnings of the Company, without any monetary effect.

4.5 Current liabilities

The following table sets forth breakdown of current liabilities as of June 30 2013 and FY 2012:

'000GEL	30 June 2013	Abs. change	% change	31-Dec 2012
Loans and borrowings	31,880	(1,540)	-5%	33,420
Trade and other payables	69,496	(12,149)	-15%	81,645
Liabilities to Government	11,926	(1,030)	-8%	12,956
Provisions	4,201	69	2%	4,132
Current tax liabilities	-	(1,542)	-100%	1,542
Dividends payable	6,449	6,449	-	-
Other current liabilities	7,913	743	10%	7,170
Total current liabilities	131,865	(9,000)	-6%	140,865

Total current liabilities decreased by 6 per cent (GEL 9 million) as at the 30 June 2013, comparing to 31 December 2012, which was mainly caused by the decrease in trade and other payables by GEL 12.1 million. Increase was partly offset by increase in dividends payable. Main contributor of the decrease in trade and other payables was the payment to the contractor for the works conducted in connection with Modernization project. Current loans and borrowings decreased due to difference in USD/GEL exchange rate between 31 Dec 2012 and 30 June 2013, as the interest accrued on Eurobonds is in USD.

5. Operational Performance Report

5.1. Traffic report

5.1.1. Freight traffic data

The following table sets forth breakdown of the freight transportation volumes, by type of freight transported, for the six-month periods ended 30 June 2013 and 2012:

Ton, Millions	6 month period ended 30 June			
	2013	% Change	Abs. Change	2012
Liquid Cargoes	4.47	-2.9%	-0.13	4.61
<i>of which:</i>				
Crude Oil	1.97	-15.1%	-0.35	2.32
Oil Products	2.50	9.5%	0.22	2.29
Dry Cargoes	4.29	-17.1%	-0.88	5.19
<i>of which:</i>				
Grain	0.23	-63.8%	-0.41	0.64
Construction Freight	0.75	-11.6%	-0.10	0.85
Cement	0.34	21.2%	0.06	0.28
Industrial Freight	0.27	5.6%	0.01	0.26
Ferrous Metals and Scrap	0.50	-10.5%	-0.06	0.56
Ores	0.96	-17.2%	-0.20	1.16
Sugar	0.24	-18.1%	-0.05	0.30
Chemicals, fertilizers	0.20	-22.3%	-0.06	0.25
Other	0.80	-9.4%	-0.08	0.89
Total	8.76	-10.4%	-1.02	9.78

In the six-months of 2013 total freight transportation volumes decreased by 10.4 per cent, compared to the same period of the previous year. The decrease was mainly caused by the decrease in dry cargo transportation by 17.1 per cent (0.88 million tons) which in its turn was due to the decrease in Grain, Construction freight and Ore transportation.

High existing stocks of grain in Armenia at the end of 2012 temporarily eliminated the need for additional grain transportation to this direction. In July and August of 2013, grain transportation increased significantly compared to H1 2013.

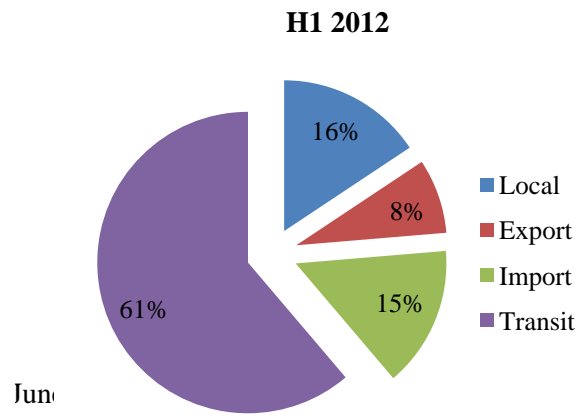
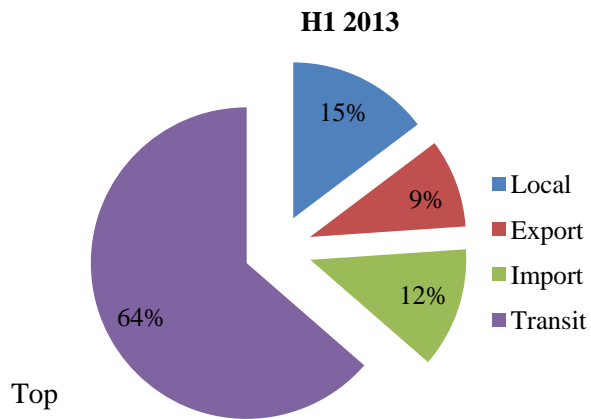
Construction freight transportation decreased due to temporary slow-down of construction projects in the country following parliamentary elections. Ore transportation decreased by 17.2% (0.2 million tons), which was caused by the stopping operations of aluminium plant in Azerbaijan.

The following table sets forth the breakdown of freight transportation volumes by types of freight transported for months of 8 months 2013:

Tons, Millions	2013								8 month Total
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	
Liquid Cargoes	0.84	0.78	0.88	0.77	0.62	0.59	0.70	0.78	5.95
<i>of which</i>									
Crude Oil	0.50	0.41	0.40	0.28	0.19	0.19	0.29	0.28	2.53
Oil Products	0.34	0.37	0.48	0.49	0.43	0.40	0.42	0.50	3.42
Dry Cargoes	0.68	0.65	0.72	0.79	0.67	0.78	0.80	0.87	5.97
<i>of which</i>									
Grain	0.03	0.05	0.04	0.03	0.04	0.05	0.09	0.12	0.45
Construction Freight	0.08	0.10	0.13	0.14	0.15	0.14	0.13	0.10	0.98
Cement	0.03	0.04	0.05	0.08	0.07	0.06	0.06	0.05	0.45
Industrial Freight	0.03	0.04	0.05	0.05	0.04	0.06	0.05	0.06	0.38
Ferrous Metals and Scrap	0.11	0.07	0.08	0.08	0.07	0.08	0.07	0.08	0.65
Ores	0.16	0.14	0.18	0.18	0.14	0.16	0.17	0.18	1.31
Sugar	0.03	0.05	0.02	0.06	0.00	0.08	0.07	0.07	0.38
Chemicals, fertilizers	0.05	0.02	0.03	0.03	0.03	0.02	0.03	0.09	0.31
Other	0.15	0.13	0.13	0.14	0.12	0.13	0.12	0.12	1.05
Total	1.52	1.44	1.60	1.56	1.29	1.36	1.51	1.65	11.92

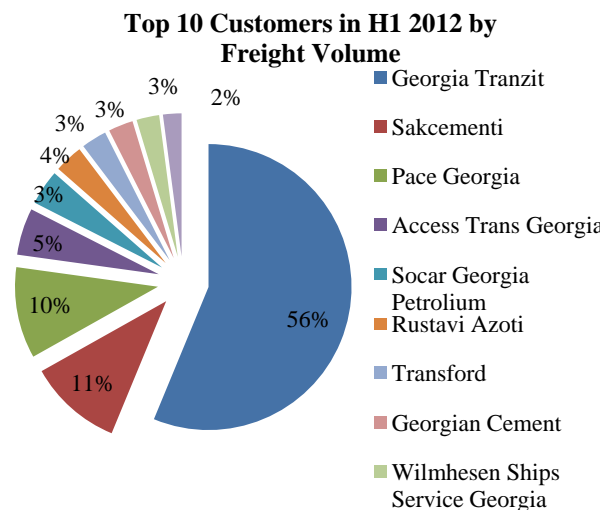
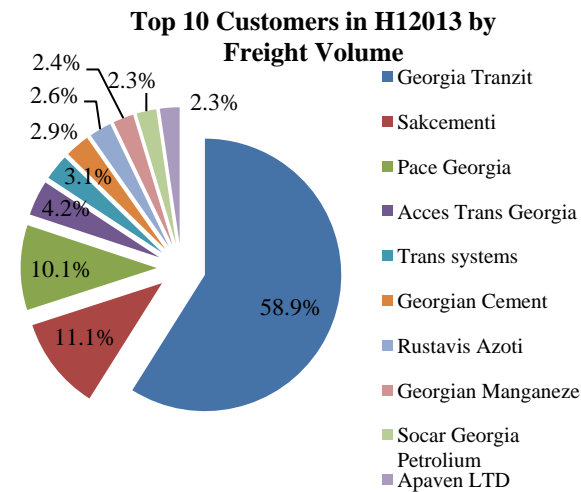
As mentioned above decrease mainly was caused by decrease in Dry Cargo volumes. The main contributor of decrease in dry cargo volumes is Grain, Construction freight and Ore. Main origin country in grain transportation is Kazakhstan. Decrease of grain from Kazakhstan was the main cause, explained in the paragraph above. From May grain transportation increased by 25%. It must be noted that in July and August this increase was preserved and somewhat higher. Management expects additional flows of cargo, namely black oil, from Kazakhstan and other liquid products which will amount to additional liquid volumes in Q4 2013 and thereon (Crude oil from Zhanazhol field and Mazut). Methanol volumes from Azerbaijan are also expected to add to the transportation growth in H2 2013.

The following graphs show the freight transportation volumes by type of destination:

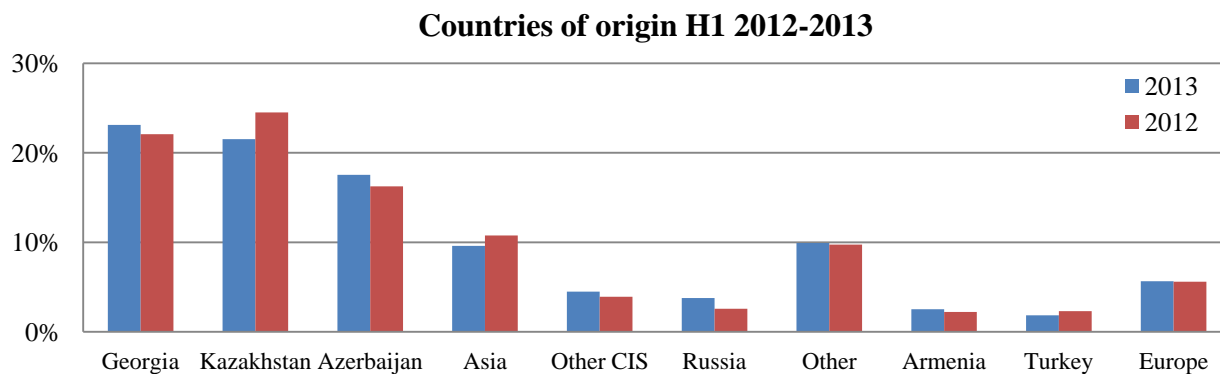


In H1 2013 top ten freight customers transported 72.4% (6.34 million ton) of total freight volume – 8.76 million ton:

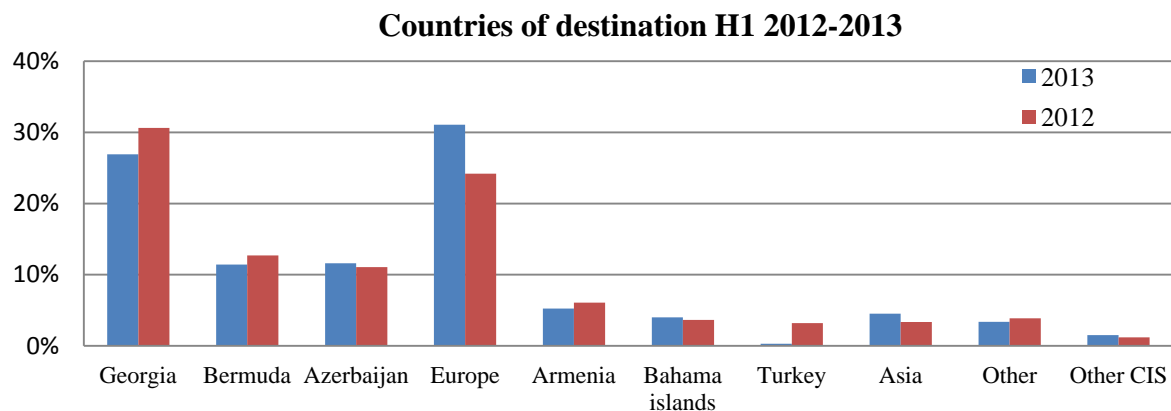
In H1 2012 top ten freight customers transported 68.7% (6.72 million ton) of total freight volume – 9.98 million ton:



The following graphs show the breakdown of countries of origin of freight transported:



The following graphs show the breakdown of countries of destination of freight transported:



5.1.2. Passenger transportation data

The following table sets forth the passenger transportation volumes by months of H1 2013 and H1 2012:

Number of Passengers ('000)	2013	% Change	Abs. Change	2012
January	224	-7.26%	-17.5	242
February	199	-11.07%	-24.8	224
March	222	-9.67%	-23.8	246
April	228	-8.82%	-22.1	250
May	244	0.59%	1.4	242
June	259	0.13%	0.3	258
July	315	-7.00%	-23.7	339
Total	1,690	-6.11%	-110.1	1,801

5.1.3. Freight transportation tariffs

The following table sets forth average revenue per thousand ton-kilometers by quarters 2013-2012:

<u>'USD per 1,000 ton-km</u>	Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013
Crude oil	22.2	22.5	26.1	26.3	26.4	27.7
Oil products	38.4	38.7	41.0	40.2	38.9	45.1
Dry	38.8	41.2	40.8	40.7	40.0	39.4

Starting from February, 2013, Georgian Railway has increased all of its base tariffs for transportation by 3 per cent. This does not have its effect on discounted transportation of liquid cargo as the tariffs set there remained the same. Also must be noted, that liquid cargo revenue consists revenue of GR's subsidiary company Georgia Transit (starting from April 2013) from liquid cargo transportation.

Average revenue per 1,000 ton-km of crude oil increased Q2 2013 and Q4 2012, which was a result of acquiring Georgia Transit LLC and thus adding its share of the tariff to the Group's.

Average revenue on oil products increased to USD 45.1 comparing to Q4 2012, which was again a result of acquisition of Georgia Transit LLC by the Company from April 2013.

Average revenue per 1,000 ton-km of dry cargo in the first six months of 2013 decreased by 3.2 per cent compared to Q4 2012. The reason is the change in dry cargo mix.

It must be noted that when calculating average revenue per 1,000 ton-km in the above table, company has subtracted revenue from transportation of empty wagons owned by private companies, which generally is classified as transportation of dry cargo however does not count as transported tons and has no impact on ton-kilometres. Such revenue has increased by 28.3 per cent (GEL 0.7 million) if comparing H1 of 2013 is compared to the same period in 2012, which is a result of privatisation of Russian, Kazakh and Ukrainian wagon fleet.