

Analysis of expenses on transportation activities



Expenses on transportation activities totalled RUB 1,266.2 bln in 2015, a 6.8% increase compared with 2014.

7.1 %

growth in transportation costs versus the 2014 level despite 15.5% average annual inflation

Expenses on transportation activities, RUB bln

Indicator	2014	2015	Growth	
			+/-	%
Expenses on transportation activities	1185.6	1266.2	80.5	106
Payroll expenses	380.0	395.6	15.6	104
Allocations for social needs	104.8	110.4	5.6	105
Material expenses	393.0	432.7	39.7	110
Materials	55.0	55.9	0.9	101
Fuel	84.3	83.1	-1.2	98
including for train traction	69.6	70.5	0.9	101
Electricity	121.6	128.0	6.4	105
including for train traction	106.4	112.5	6.1	105
Other material expenses	132.2	165.7	33.5	125
Depreciation	188.3	189.8	1.5	100

Other expenses	119.6	137.7	18.1	115
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Structure of Russian Railways expenses on transportation activities in 2014 by cost components, % (RUB bln)

Structure of Russian Railways expenses on transportation activities in 2015 by cost components, % (RUB bln)

Payroll expenses totalled RUB 395.6 bln in 2015, an increase of 4.1%, or RUB 15.6 bln, compared with 2014.

The change in expenses was due to the following factors:

- growth in expenses that depend on transportation volume by RUB 0.3 bln;
- growth in expenses due to the partial indexation of wages at 3.5% starting from 1 March 2015 (5.1% average for 2015 versus 2014) in accordance with local company regulations prepared based on clause 4.1.5 of the Russian Railways collective bargaining agreement for 2014-2016 (RUB +17.5 bln);
- growth in expenses by RUB 0.5 bln due to the maintenance of newly built facilities in the Eastern operating domain and Ust-Luga, among others.
- a decrease in expenses by RUB 2.1 bln (including through the outsourcing of non-core operations and the transition to full after-sales service of the locomotive fleet starting from 1 July 2014).

At the same time, it should be noted that salaries were indexed at 5.1% (in average annual terms) in order to achieve a financial balance in operations given actual average annual consumer price growth of 15.5% (12.9% December vs. December), which led to a decline in the real salaries of the Company's employees.

Allocations for social needs totalled RUB 110.4 bln in 2015, an increase of 5.4%, or RUB 5.6 bln, compared with 2014.

The change in expenses was caused by the following factors:

- increased expenses resulted from amendments to legislation (RUB +2 bln):
 - starting from 1 January 2015, mandatory medical insurance premiums are paid at a tariff of 5.1% of all payments and other remuneration paid to an individual for the corresponding fiscal year with no restriction on the limit value of the premium base;
 - starting from 1 January 2015, the limit value for mandatory pension insurance premiums totalled RUB 711,000, while the limit value for mandatory social insurance premiums in the event of temporary disability and for maternity was RUB 670,000 with respect to each individual;
 - starting from 1 January 2015, exemptions are made for compensation payments for the dismissal of employees prescribed by employment and collective bargaining agreements in an amount not exceeding three times the average monthly salary or six times the average monthly salary for employees dismissed from organisations located in areas of the Far North and equivalent areas.
- increased expenses in accordance with growth in payroll expenses resulting from the partial indexation of salaries and the introduction of new facilities (RUB +3.6 bln).

Fuel expenses amounted to RUB 83.1 bln in 2015, a decrease of 1.4%, or RUB 1.2 bln, from 2014, including:

- fuel expenses on train traction increased 1.3% (RUB +0.9 bln) with the change in expenses occurring due to:
 - a decrease in transportation volume as measured in gross tkm in diesel traction by 2.1% (RUB —1.5 bln);
 - an increase in diesel fuel prices taking into account growth in excise taxes for diesel fuel in accordance with Federal Law No. 306-FZ dated 27 November 2010 'On Amendments to Part One and Part Two of the Tax Code of the Russian Federation' (RUB +3.3 bln);
 - optimisation measures that aim to cut fuel consumption by reducing specific fuel consumption rates for train traction in diesel traction by 2.0%, which made it possible to cut costs by RUB 0.9 bln;
- expenses on other production needs decreased 13.9% (RUB —2.1 bln) with the change taking place due to:
 - an increase in diesel fuel prices taking into account growth in excise taxes for diesel fuel in accordance with Federal Law No. 306-FZ dated 27 November 2010 'On Amendments to Part One and Part Two of the Tax Code of the Russian Federation' (RUB +0.7 bln);
 - a decrease in fuel consumption due to optimisation measures, including through the outsourcing of non-core operations, the transition to full after-sales service of the locomotive fleet starting from 1 July 2014 and other measures (RUB —2.8 bln).

Electricity expenses amounted to RUB 128.0 bln in 2015, an increase of 5.3%, or RUB 6.4 bln, from 2014, including:

- electricity expenses on train traction grew 5.7% (RUB +6.1 bln) with the change in expenses resulting from:
 - a decrease of 0.8% (RUB —0.8 bln) in transportation volume as measured in gross tkm in electric traction;
 - growth of 7.7% (RUB +8.1 bln) in the average electricity tariff for train traction;
 - optimisation measures that aim to cut electricity consumption by reducing specific electricity consumption rates for train traction in electric traction

by 1.2%, which resulted in cost-cutting of RUB 1.2 bln;

- expenses on other needs increased 2.2% (RUB +0.3 bln) with the change in expenses due to:
 - growth in the average electricity tariff by 8.4% (RUB 1.3 bln);
 - a decrease in electricity consumption due to optimisation measures and the transition to full after-sales service of the locomotive fleet transition started from 1 July 2014 and other measures (RUB —1.0 bln).

All other material expenses (materials and other material expenses) amounted to RUB 221.6 bln in 2015, an increase of 18.4%, or RUB 34.4 bln, from the 2014 level. The change in expenses was caused by the following factors:

- growth in expenses of RUB 27.3 bln due to price increases on consumed products. At the same time, the work being carried out to restrict price growth on the consumed products made it possible to reduce these expenses by RUB 10.5 bln;
- growth in expenses of RUB 17.6 bln due to the outsourcing of non-core operations as well as the transition to full after-sales service of the locomotive fleet starting from 1 July 2014 through the redistribution of expenses among cost components within the limits of total expenditures.

Depreciation amounted to RUB 189.8 bln in 2015, or 0.8% (RUB +1.5 bln) more than in 2014. The change in expenses is due to both the commissioning of new fixed assets as part of the Russian Railways Investment Programme as well as the retirement of a number of facilities and ongoing work to preserve fixed assets not involved in the transportation process.

Other expenses amounted to RUB 137.7 bln, an increase of 15.1%, or RUB 18.1 bln, compared with 2014. The main factors affecting the changes in other expenses were:

- growth in property tax expenses by RUB 9.0 bln, including due to an increase in the tax rate (from 0.7% to 1%) for public railways as well as structures that constitute an integral part of such facilities and amendments made to the Tax Code of the Russian Federation after 1 January 2015;
- growth in expenses by RUB 5.2 bln to fund a programme to lease advanced track maintenance equipment for a wide range of track repair work in order to ensure the efficient operation of railway infrastructure;
- growth in expenses by RUB 1.3 bln due to amendments to the Labour Code of the Russian Federation as of 1 January 2015 as regards employees retaining the average salary at their main place of work when being sent for professional training or additional professional education (stipend previously paid);
- growth in expenses for facility security services, fire safety, etc. (RUB +3.1 bln);
- a decrease in expenses by RUB 0.5 bln due to the outsourcing of non-core operations, the transition to full after-sales service of the locomotive fleet starting from 1 July 2014 and other measures.

Major repairs of fixed assets

Russian Railways spent RUB 57.9 bln on major repairs to its fixed assets in 2015 as part of expenses on transportation activities, including RUB 29.9 bln in subsidies from the federal budget.

Subsidies were used to repair 2,147 km of tracks, 129 engineering structures, 27 km of roadbed, 846 automatic blocking devices and 1,223 interlocking switches, 2,402 km of contact network, 1,435 km of overhead and cable electricity transmission lines and 73 traction substations in 2015.

Cost optimisation

The macroeconomic situation within Russia continued to deteriorate in 2015, and the forecast parameters for the nation's socioeconomic development predicted even more negative trends. In particular, the GDP growth rate has been lowered from +1.2% to —3.7%, which directly impacted the dynamics of our Company's volume indicators and led to losses in revenue receipts.

In order to minimise risks from decreased income as well as increased negative exchange rate differences and interest payments, Russian Railways has taken timely measures to optimise the cost of transportation activities.

Total cost optimisation for transportation activities in 2015 versus the initial plan approved by the Russian Railways Board of Directors and the Russian Government 27 November 2014 (RUB 1,305.9 bln) amounted to RUB 39.7 bln.

This effect was above all achieved through improving energy efficiency, introducing resource-saving technologies, containing price growth as well as implementing organisational and technical measures. The main optimisation measures included:

- a 1.3% downsizing of personnel, restricting salary indexation to 5.1% in average annual terms despite actual consumer price growth of 15.5% (12.9% December vs. December) as well as the use of part-time work schedules;
- continued work to further enhance internal efficiency, including through the consistent improvement of the pricing policy and the sustainable use of materials;
- stricter specific fuel and energy consumption rates for train traction and a decrease in the consumption of fuel and energy resources for other production needs (through the increased efficiency of regenerative braking and the use of regenerative power return, the introduction of resource-saving technologies, the use of energy efficient bulbs and lighting systems, process equipment, the optimisation of heating and air conditioning, and more);
- the preservation of fixed assets due to reduced transportation volumes (primarily locomotives), the revision of Russian fixed asset classification (OKOF codes, updates to the commissioning dates of fixed assets and the revision of the useful life period will lead to a reduction in depreciation charges;
- other measures — enhancing operating technologies, including by improving locomotive performance indicators, modifying the operating mode

on sections with low intensity traffic, merging professions and expanding the service area, among other things.

The Company continues work to optimise material expenses while observing the required product quality levels and supply deadlines as well as guaranteeing the sustainability of their production volume.

Based on a continuous analysis of current prices, the Company monitors the situation on industry-related markets, arranges negotiations with existing and potential product suppliers concerning the ability to lower prices, searches for alternative supply sources and studies the feasibility of obtaining additional discounts for products delivered as part of long-term contracts under which Russian Railways provides counterparties guaranteed supply volumes for a long period.

Timely amendments to regulatory documents of a technological nature that describe the use of labour resources reduce the labour intensity of technological processes and significantly decrease the estimated (required) number of employees.

As a result of the measures adopted by the Company and despite significant price pressure, the cost of transportation activities only increased by 7.1% versus 2014, which is significantly lower than the industry price growth (12.4%) and average annual inflation (15.5%).