On the path to change

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In 2015, more than RUB 200 bln were spent on the construction and modernisation of railway infrastructure performed by the Company's construction units.

Russian Railways met its objectives of developing the Eastern operating domain, the Moscow Hub, approaches to ports in the Northwest and Azov and Black Seas as well as a number of other projects throughout the entire railway network that aim to eliminate bottlenecks, increase carrying capacity and improve traffic safety.

A process and price audit of the Company's investment projects was conducted in 2015 with the results published on the Company's website and discussed with expert organisations.

The Company actively works to optimise project and technological solutions in order to improve the efficient use of investment resources as part of implementing the orders of the Russian Government.

Based on materials from the final meeting of the Russian Railways Management Board

Investment planning approaches

The planning of the investment programme takes place in several stages:

- formation of a master plan for the development of the railway network using an input-output balance and identification of the general areas for the development of railway transportation;
- identification of sources to fund the investment programme as part of the formation of the Company's financial plan;
- prioritisation during the consideration of investment projects at meetings of the Investment Projects Expert Council and Investment Committee based on the available sources of funding.

Formation of a master plan for the development of the railway network

The process of identifying promising areas for the development of railway transportation essentially consists of the following three stages:

- forecasting transportation volume based on the input-output balance;
- forming a master plan for the development of the railway network;
- identifying medium-term objectives for the development of railway transportation based on the master plan.

Building an input-output balance

Today, the interregional input-output balance of freight transportation is the primary tool used to identify the prospective freight base and the main freight routes on the Company's railway network.

The main principle for building the input-output balance is transitioning from the macroeconomic forecasts of the Russian Ministry of Economic Development to forecasts of interregional traffic flows taking into account the industry's programmes and development strategies, Russia's subnational entities as well as requests from individual enterprises.

One important aspect of constructing forecasts is to take into account plans for the development of related modes of transportation (plans of Russian sea ports) as well as the development programmes and strategies of the constituent entities of the Russian Federation.

An interregional input-output balance of freight transportation was used to determine growth in the freight base of the project 'Modernisation of the Railway Infrastructure of the Baikal-Amur and Trans-Siberian Mainlines with the Development of Traffic and Carrying Capacity' (ensuring growth in freight volumes shipped from the main fields of the Eastern operating domain to 66 mln tonnes).

Formation of a master plan for the development of the railway network

The prospective freight base for railway transportation serves as the basis for identifying and substantiating the measures required to develop railway transportation infrastructure and, in turn, forms the basis of the master plan for the development of the railway network for the period until 2020.

The master plan developed based on this approach aims to detect and resolve a number of systemic constraints and bottlenecks that emerge on railway transportation and are critical for the further development of railway infrastructure.

Identifying medium-term objectives for the development of railway transportation based on the master plan

The Company identifies medium-term priorities for implementing development and renovation investment projects based on the long-term railway infrastructure development plans as well as the growth rates in the freight base.

This three-tiered systematic approach enables the Company to construct forecasts for the development of railway infrastructure with a rather high degree of accuracy and form the Long-term Investment Programme of Russian Railways.

Using the Long-term Investment Programme as a basis, the Company can clearly identify projects that should be implemented in the medium term (three-year period).

Identification of sources to fund the Investment Programme as part of the formation of the Company's financial plan

When forming its Investment Programme, Russian Railways adheres to the principle of consistency with respect to sources of funding and the structure of the Investment Programme.

Specifically, the Company seeks to secure investment budget funding for spending on:

- renovations to fixed assets at the level of depreciation charges;
- commercially effective projects at the level of borrowed funds;
- commercially ineffective projects at the level of government support.

Russian Railways has classified the entire package of investment projects based on the criteria of the payback period and commercial effectiveness according to three categories.

The first category includes projects with a payback period of 10-15 years that Russian Railways is prepared to finance using its own cash flow as well as borrowed funds within an accepted level of debt load.

The second category includes projects with a payback period of 15-30 years. Russian Railways cannot borrow to finance these projects since the market does not offer borrowed funds with this kind of term structure. At present, investment projects in this category are financed by issuing infrastructure bonds.

The third category consists entirely of ineffective (stranded) investment projects for Russian Railways that may only be funded by budget sources since the state budget can recoup the invested funds via a multiplier budget effect. This category includes the following projects:

- modernisation of the railway infrastructure of the Baikal-Amur and Trans-Siberian Mainlines with the development of traffic and carrying capacity;
- comprehensive development of the Mezhdurechensk-Tayshet section of Krasnoyarsk Railway;
- development and renovation of railway infrastructure at approaches to ports in the Azov and Black Seas;
- construction of the Prokhorovka-Zhuravka-Chertkovo-Bataysk railway line (a new line on the Zhuravka-Millerovo route);
- development of the Moscow Transport Hub;
- construction of secondary tracks and the electrification of the Vyborg-Primorsk-Yermilovo section;
- construction of the Moscow-Kazan High-Speed Railway.

Prioritisation of investment projects

After the objectives for railway transportation development are identified at meetings of the Russian Railways Investment Projects Expert Council and Russian Railways Investment Committee taking into account the transition projects that have already been implemented and also based on the available sources of funding for the Investment Programme in the medium term, the parameters of the investment projects for renovating and developing railway infrastructure are optimised.

The Investment Projects Expert Council's primary objective is to conduct an in-depth technological study of the proposed projects prior to their consideration by the Investment Committee.

The Investment Projects Expert Council considers the details of the medium-term investment projects on an itemised basis each year at meetings in August and September and selects the most optimal measures from a technological standpoint.

The primary objectives of the Investment Committee are:

- to conduct an economic expert evaluation of the projects;
- to identify possible funding targets for the Company's Investment Programme;
- to rank and prioritise the investment projects based on the performance indicators and overall strategic objectives of the Company's investment policy;
- to consider and approve the projects in the Company's Investment Programme;
- to monitor the implementation of the Company's Investment Programme;
- to consider matters concerning the optimisation of the management of the Company's investment activities.

Based on the decisions regarding the priority of investment projects adopted at the meeting of the Company's Investment Committee, a three-year Investment Programme is prepared and subsequently considered by the Russian Railways Board of Directors and the Russian Government.

Audit of investment projects

Design documentation underwent a process and price audit at 30 railway infrastructure facilities in the reporting year.

The Company continued work initiated by the Russian Government in 2015 to conduct an independent process and price audit (PPA) of its investment projects.

The introduction of the PPA procedure was an important step towards improving the openness and transparency of the Company's investment programmes that are funded in full or in part by federal budget funds and generate increased interest from the public.

Taking into account the decisions of the Russian Government as well as the procedure specified in the Corporate Standard 'Mandatory Process and Price Audit of the Investment Projects of Russian Railways and Its Subsidiaries and Affiliates', the biggest investment projects included in the Russian Railways Investment Programme underwent an audit during their pre-project stages:

- reconstruction and modernisation of the Baikal-Amur and Trans-Siberian Mainlines;
- development of railway infrastructure at approaches to ports in the Azov and Black Seas, including the bypass of the Krasnodar Railway Hub;
- development of railway infrastructure at approaches to ports in northwest Russia until 2020.

In accordance with the Corporate Standard, the results of the audit were published on the officialwebsite of Russian Railways and discussed with expert communities.

Overall, the experts noted that the projects have been sufficiently studied given the current implementation stage.

In December 2014, the Government Transportation Commission ordered audits of the design documentation for 72 railway infrastructure facilities in the Eastern operating domain with a final decision to be made on 12 of the facilities at meetings of the Interdepartmental Working Group on Railway Transportation Development Affairs.

Since the start of 2015, design documentation audits have already been conducted for 30 railway infrastructure facilities in the Eastern operating domain. Seven of the audit reports were sent to the Interdepartmental Group for consideration and two of them have already been reviewed by the Interdepartmental Group.

In 2016, design documentation audits are to be conducted at 38 facilities taking into account the expiration of deadlines for the