Financial risk management

The Company lays a strong emphasis on managing financial risks and insuring its property and liability. In 2020, key objectives in the realm of financial risk management included framework adjustment to potential adverse geopolitical and macroeconomic factors, and further efforts to ensure implementation of uniform financial risk management principles across the Group.

The key internal regulation governing financial risk management at Russian Railways is the Company's Financial Risk Management Policy. All related decisions are made by the Financial Risk Management Commission, a collective body headed by the First Deputy CEO of the Company. The financial risk management proved the Commission's efficiency as a management decision-making centre due to the involvement of all respective units in discussing and making well-informed decisions taking into account all related risks. The Financial Risk Management Commission holds regular meetings. In 2020, over ten meetings were held to discuss numerous issues, including management of the Company's foreign currency exposure, approaches to hedging, financial risk management as part of implementation of the first priority investment projects.

Russian Railways approaches to financial risk management are based on best practices in financial risk management, principles of diversification through the use of various risk management tools and reliable counterparties. The risk management policy excludes speculative risk management tools, as well as operations with unreliable counterparties.

Credit risks

To manage its credit risks, Russian Railways has put in place procedures to calculate credit limits and regulatory documents governing operations with bank guarantees and sureties, including the unified corporate standard of the Russian Railways Group for dealing with collateral instruments. The Company assesses financial institutions and calculates relevant credit limits so as to manage bank transactions involving deposits and bank guarantees based on the financial standing of the financial institution. The assessment of financial institutions is based on the analysis of their qualitative and quantitative performance indicators in accordance with the internal methodology developed with input from leading risk management experts. The Company lays a strong emphasis on improving and developing the approaches to assess financial institutions taking into account the latest changes in the Russian banking sector. Credit limits are calculated using an automated system.

In its dealings with the real sector companies, Russian Railways relies on a system of management standards that include standard terms of settlement with counterparties, provisional remedies, treasury control, limitation of receivables and payables, bank guarantees underpinning the parties' commitment to competitive bidding, proper performance and repayment of advances. These tools help to protect Russian Railways against the risk of counterparty default. Financial institutions that issue bank guarantees and sureties are selected based on their credit record and existing credit limits.

Liquidity risk

The Company manages its liquidity based on the balance of payments, payment schedule and payment position as per the approved budgets. Depending on the current liquidity situation, the Company promptly raises or deposits funds under the best market conditions. The Company manages its liquidity based on Reuters and Bloomberg systems. The Company is also promoting the use of cash pooling for intercompany liquidity management purposes.

Currency and interest risks

To assess this category of risks, the Company builds models and evaluates budget parameters factoring in potential volatility of the relevant market indicators. Assessment of Russian Railways' currency risks and selection of a currency risk management tool are based on the analysis of the Company's foreign currency exposure, the Company's operations are broken down into and analysed by investment, operating and financial activities.

The amount and structure of the estimated foreign currency exposure have further implications for the Company's borrowing policy and hedging approach. Russian Railways regularly revises its foreign currency exposure and adjusts its approach to managing currency risk and FX-denominated loan portfolio.

The Company minimises its foreign currency risks by reducing its foreign currency exposure, which includes the use of financial derivatives, and seeks to keep it close to neutral with cash inflows and outflows in foreign currencies offsetting each other. The assessment of interest risk is based on the analysis of the floating interest rate volatility and its impact on Russian Railways' loan portfolio. The Company also develops and reviews the foreign currency exposure of the Russian Railways Group in order to assess its risk profile and coordinate solutions across the Group.

Taking into account the heightened risk of changes in the Russian rouble exchange rate, starting from 15 July 2015, Russian Railways has been applying hedge accounting model to liabilities denominated in foreign currencies in line with its approved foreign currency risk management policy. The Company hedges revenue from transit shipments through the Russian Federation denominated in Swiss francs, as well as euro-denominated investments in GEFCO. The hedging tools include loans and borrowings in Swiss francs and US dollars (after conversion into Swiss francs) and a portion of the euro-denominated loan corresponding to the net investment in GEFCO.

Hedge accounting allows the Company to recognise the effect of the currency risk management policy and reduce volatility of its financial results caused by movements in the currency exchange rates. As a result, translation differences on hedged loans are recognised in equity and later reclassified to profit or loss when FX revenue is received and/or FX asset is disposed of.

Each case of foreign currency exposure is analysed for applicability of hedge accounting under the Russian and international financial reporting standards. As at 31 December 2020, over 90% of the Company's borrowings denominated in foreign currencies were subject to hedge accounting.

Insurance

The Company insures its real estate, rolling stock, employees, liability of a railway infrastructure owner, carrier liability, and liability of directors and officers working for the Company or its 99 subsidiaries and affiliates.

Over 1,380 insurance claims were settled in the reporting year, with total insurance compensation exceeding RUB 794.6 m.