MOSCOW EXCHANGE

MOEX Q3 2017 IFRS Results Conference Call

9 November 2017

Speakers:

- Alexander Afanasiev, CEO
- Maxim Lapin, CFO
- Anton Terentiev, Director of IR

Participants asking questions:

- Svetlana Aslanova, VTB Capital
- Sergey Garamita, Raiffeisen Bank
- Andrzej Nowaczek, HSBC
- Olga Veselova, Bank of America Merrill Lynch
- Olga Naydenova, BCS

Investor Relations contacts – Anton Terentiev, Director of Investor Relations

Tel: +7 495 363 3232 – Email:ir@moex.com

Operator

Good afternoon, ladies and gentlemen, and thank you for standing by. Welcome to today's MOEX Q3 2017 IFRS results conference call. At this time, all participants are in a listen-only mode. There will be a presentation followed by a Q&A session, at which time if you wish to ask a question you will need to press "*1" on your telephone and wait for your name to be announced. I must advise you that this conference is being recorded today, Thursday, 9 November 2017. I would now like to hand the conference over to your first speaker today, Mr Anton Terentiev. Please go ahead, sir.

Anton Terentiev – *Director of Investor Relations*

Good afternoon everyone, and welcome to Moscow Exchange Q3 2017 IFRS results conference call. As usual, after the prepared remarks, we will have a Q&A session. On the call today we have Alexander Afanasiev, CEO, and Maxim Lapin, CFO.

Before we start, I would like to remind you that certain statements in this presentation and during the Q&A session may relate to future events and expectations and, as such, constitute forward-looking statements. Actual results may differ materially from those projections. The Company does not intend to update these statements to reflect the events occurring after the date of the call prior to the next conference call. By now, you should have received our press release containing the results of the Q3 2017. Our management presentation is available on the Company's website in the IR section.

I will now hand over the call to Alexander Afanasiev. Alexander, please go ahead.

Alexander Afanasiev – *CEO*

Thank you, Anton. Good afternoon, ladies and gentlemen. I would like to begin by the introduction of the main speaker today, and I hope also, the main speaker for many conference calls in the future, our new CFO Maxim Lapin. I believe that many of you have already met him during our roadshows or at meetings in Moscow. For others, I can tell you that Maxim is a highly professional, dynamic leader with extensive management experience at large corporates across multiple sectors. Prior to joining MOEX, Maxim Lapin served as a member of the Management Board of MMK, one of Russia's largest steel companies. Before that, he was at SIBUR. In the earlier days of his really impressive career, Maxim worked at McKinsey. He graduated from Moscow State University and has an MBA from Columbia Business School. You know, it really took me some time to find a new CFO who could fit our company because we required someone who could equally be capable of maintaining our high level of transparency and our strong dialogue with the investment community, to further drive and develop our business, but at the same time focusing on operational efficiency and on cost control. I am happy to say that the Board and I agreed that Maxim is just the person we need for this role. So, I wish Maxim every success and would like to turn the call over to him.

Maxim Lapin – *CFO*

Thank you, Alexander. Thank you all for joining us today to discuss Moscow Exchange's financial results. I will first cover some events that occurred since the beginning of Q3.

In September, the Company had an EGM, which was the first one where MOEX shareholders could vote using e-voting technology and experience the results of the corporate actions reform. The EGM approved the dividend payments for H1 2017 in the amount of RUB 5.7 bln, or RUB 2.49 per share. The Company completed all dividend payments in early November.

In October, Moscow Exchange held its annual Forum in New York City. As always, it attracted several hundreds of investors and financial professionals, interested in the Russian financial markets.

ACRA, Russia's leading credit rating agency, recently affirmed NCC's credit rating at AAA, which is the highest rating on ACRA's national rating scale. In addition, in September, Fitch changed NCC's rating outlook to positive following the change in Russia's sovereign rating outlook and affirmed NCC's foreign currency credit rating at BBB-, which is the cap for Russian issuers nowadays.

MSCI, a global index provider, changed its closing price policy for securities traded on the Moscow Exchange. Starting the end of October, MSCI uses closing auction prices for calculating investable indices. This change reflects increased liquidity of closing auctions that were introduced in 2013 as well as a number of enhancements made to the mechanism of closing auction price determination.

In H2 2017 to date, eight Russian issuers listed on Moscow Exchange completed public offerings totaling almost RUB 89 bln.

In October, Capital Group Companies, Inc. increased their collectively owned stake in MOEX to just above 5%.

Now let us turn to the product offering. In July, we granted access to the Money Market to Russian corporates. They can place funds with the CCP at the repo market rates. Deposits made by corporates are matched with orders to borrow funds against general collateral certificates (GCC) placed by other market participants. I will talk about the repo with general collateral certificates in greater detail in a moment.

The FX fixing rate deals were introduced on the FX Market. This new instrument allows to enter into FX trades at MOEX FX fixing rate and is designed for hedging risks that arise from the FX and derivative positions. The new instrument is in high demand by international participants.

Options on two currency pairs, GBP/USD and USD/JPY, started trading on the Derivatives Market. We also introduced weekly options on the USD/RUB pair in addition to monthly and quarterly options. Addition of new products and maturities allows market participants greater flexibility in choosing trading strategies and is a major component of developing our Derivatives Market.

Let me provide a short overview of how our long-term projects developed in the beginning of Q3 and share some of our plans. We have been testing the basic functionality of the Unified Collateral Pool (UCP) with the market participants. We expect to implement all features of the Unified Collateral Pool over the next six months. The implementation of trading under the UCP will be performed in stages and followed by changes in fees for the Money, Derivatives, and FX Markets. On the Money Market, the change will affect fees charged for the repo with the CCP, which will initially rise by 3% in July 2018 and later, by the same amount more, in October 2018. The total change will be 6% relative to the current level. On the FX Market, fees for the FX swaps will rise by 10% in July next year, and by another 10% in October next year. The total increase will be around 20% relative to the current fees. Finally, on the Derivatives Market, all fees will rise by 10% in October 2018. All of these changes were adopted by client committees. The first step of the increase in fees applies to the UCP accounts only, while the second step applies to all accounts.

Let us turn to GCC now. During Q3 2017, volumes of repo with general collateral certificates started to grow rapidly, increasing more than seven-fold QoQ. There were several factors behind this increase. First, there was a change in the way the Central Bank treats GCCs for purposes of calculating regulatory ratios. The Bank of Russia's new document specified how exactly GCCs should be accounted for and dispelled some uncertainties for entities that use GCCs. Secondly, in June, we started the marketing period for GCC repo transactions order book and reduced fees by 20% as a way to promote the product. Thirdly, in July corporates were granted access to deposits with the CCP enabling them to place money with the CCP at the repo market rates. Currently, 20 corporates have joined the market and their trading volumes in Q3 exceeded RUB 600 bln and to date they are exceeding RUB 1 trln.

Now let us move to financial results for Q3 2017. Our operating income was RUB 9.7 bln, down by 10.5% YoY due to the decline in total net interest and finance income. The latter comes from the high base effect of Q3 last year when an AFS securities gain of nearly RUB 1 bln was recorded. Apart from the factor of the AFS securities gain, net interest and finance income was down 18.1% YoY and up 1.4% QoQ. I am proud to say that fee and commission income grew by 14.9% YoY to a new record high of RUB 5.5 bln. Its share in total operating income reached 57% vs only 44% in Q3 of last year, up by 12.6 pp YoY. Operating expenses increased by only 10.9% YoY to RUB 3.3 bln. Roughly half of the growth came from increases in D&A and IT expenses. Costs other than D&A and IT increased only by 7.7% YoY. EBITDA stands at RUB 7.1 bln, down 15.5% YoY. EBITDA margin was a solid 73.5%. Net income declined by 18.2% YoY and amounted to RUB 5.1 bln.

In Q3, a number of markets showed double-digit growth in fees, which helped achieve all-time high quarterly fee and commission income. The greatest contributors to growth in absolute terms were the Money Market (up 30.8% YoY), Depository and Settlement Services (up 21.1% YoY), Fixed Income (up 36.2% YoY) and Equities Market (up almost 20% YoY). Overall, products directly related to interest rates such as repo, FX swaps and bonds posted a very convincing performance in Q3 2017. The structure of overall fee income remained well-diversified with relative shares of different markets quite stable. although the share of fees from the Money Market moved closer to 30%.

The average investment portfolio in Q3 2017 was around RUB 700 bln, down 10.6% YoY due to moderation in balances of market participants. However, on a QoQ basis, RUB balances started to recover in Q3 2017, growing by 20.0% QoQ. Total net interest and finance income excluding gain on AFS securities was RUB 4.2 bln, down by 18.1% YoY on the back of lower RUB interest rates. Higher USD interest rates and continued use of FX swaps helped to offset lower RUB rates and change in the size of the portfolio. As a result, the effective yield on the investment portfolio stayed at the level of 2.4%, roughly the same as in Q2 2017. Gain on AFS securities contracted from RUB 0.9 bln in Q3 last year to just RUB 16 mln in the last quarter making a contribution of this line to the total net interest income negligible.

Trading volumes on the Equities Market increased by 14% YoY and fees were up by 20% YoY. Q3 2017 featured the highest trading volume in equities among third quarters since the MOEX IPO year of 2013. Market velocity increased to 27% in Q3 from 24% last year. We continued to see some welcome developments in the Equities Market. One of them is a growing engagement of retail investors. The number of Individual Investment Accounts (IIA) reached 269,000 at the end of the quarter, up by 76% YoY. The number of active retail accounts on the Equities Market was more than 92,000 in September, up 19% YoY. Trading volumes generated by retail investors are also rising, although at a lower rate than the number of active accounts. They were up 5% YoY in Q3. We are also happy to observe a pick-up in IPO/SPO activity, which this time is characterised by participation of medium-sized companies such as Shoes of Russia and Globaltruck. MOEX, in its turn, has started to support such public SMEs, having launched the new market segment for them in July this year. We call it the ‘Growth Sector’. The share of international investors in equities trading volumes is growing as well: in Q3 2017, it increased 1.3 percentage points YoY and reached 46%.

Performance of the Fixed Income Market continues to accelerate throughout 2017. The interest rate environment remains favourable for issuers, while infrastructural upgrades aimed to ease the placement process work as a supporting factor. That being said, total trading volumes on the Fixed Income Market grew by 121% YoY, more than a two-fold expansion. Most of the growth came from primary placements, which expanded five times YoY. This amount includes RUB 2.9 trln of placement volumes in overnight bonds. Primary placements excluding overnight bonds amounted to RUB 1.3 trln, up 51% YoY. Placements of government and CBR bonds grew by a strong 79%. Overall, the total volume of placements in the bond market excluding overnight bonds approached the level of Q4 2016, which is the highest to date. Secondary trading volumes increased by 25% YoY with trading in government and CBR bonds growing the most rapidly up 36% YoY. In terms of fees from the bond market, Q3 was just short of Q2, which is the standing record so far. Fees and commissions amounted to RUB 495 mln, 36% more than in Q3 2016. This is the second highest growth rate over the last two years.

The Derivatives Market. As a result of muted volatility, the Derivatives Market trading volumes declined by 19% YoY led by FX and index futures – a similar picture compared to Q2 2017. However, trading volumes of commodity futures continued to grow by 8% YoY and contributed 22% of total trading volumes from the derivatives market. Option trading volumes also advanced by 27% YoY driven mostly by index options, up 35% YoY. Fees and commissions from the Derivatives Market increased by 5% YoY despite the above-mentioned 19% decrease in trading volumes. The effective fee was supported by changes in the product mix that favoured higher yielding products.

The Money Market trading volumes increased by 26% YoY and by 30% YoY excluding repo with CMS through NSD. Growing trading volumes translated into higher fees, which were up by 31% YoY in line with volumes. Both trading volumes and fees reached a new record high in Q3 rising substantially both on a quarterly and annual basis. In absolute terms, volume growth was rather evenly split between repo with the CCP, including GCC repo and repo with the Bank of Russia. The former continued to be a major driving force as the total CCP volumes increased by 28% YoY and its share in total inter-dealer repo reached 77%. As for the latter, liquidity imbalances in the banking system reinvigorated the demand for repo with the Bank of Russia and volumes surged 2.2x on an annual basis. Our diversified business model, which features an inventory of financial tools for every set of circumstances, helped to mitigate these developments. Volumes of GCC repo through the CCP increased over 14x YoY in Q3 2017 making it the fastest growing segment of the Repo Market. GCC repo still accounts for a small portion of on-exchange repo volumes with 1.4% only, but given the recent changes in the regulation of GCCs as well as the participation of corporates, it is becoming a more meaningful component of the Money Market income.

The FX Market trading volumes increased by 6% YoY due to growing swap volumes, which were up by 16% YoY on the back of continued demand for liquidity management instruments. Spot FX trading volumes declined by 17% as volatility was quite muted. Spot FX trading volumes were hovering around the same level as in the two preceding quarters of the year. The number of corporates with access to the FX Market increased from 9 to 16 throughout the quarter and stands at 16 at the start of November. MOEX's market share of the onshore FX Market was 51%, roughly the same as in Q3 2017.

Depository and Settlement. The segment continues to be a steady performer getting to second place among business lines by revenue generated in Q3 2017. Average assets under custody increased by 13% YoY to RUB 37.3 trln. The growth was primarily due to the growing value of bond issues under custody. Fee and commission income grew by a staggering 21.1% YoY mostly driven by safekeeping fees on the back of a general increase in assets under custody. NSD has continuously worked on developing new services and in October, it used, for the first time ever, a blockchain-based settlement platform to complete an inaugural placement of RUB 500 mln bond issue.

IT services and listings. Listing and other fees related to the Securities Market declined by 14% YoY. Sales of software and technical services were down by 1% YoY and sales of market data and information services subsided by the same percent YoY, due to continued RUB appreciation which stood at around 9% YoY and somewhat eroded the FX –denominated portion of fees for the market data services.

Total operating expenses grew just short of 11% in Q3, below the previously given guidance of 15–17%. This resulted in the 9M total OPEX rising by 10% YoY. Most of the growth was attributable to the expenses related to implementation of the CAPEX programme for 2016. In Q3, depreciation, amortisation and IT maintenance expenses increased by 19% YoY. There also was a single one-off expense related to the disposal of a building in Nizhny Novgorod. The remaining administrative expenses – administrative expenses less D&A and IT-related costs and one-offs – actually advanced only by 8.8% YoY. Personnel expenses grew by 3.0% YoY due to less active hiring compared to the initial plan. Based on the results for 9M 2017, we are updating our end-of-year expense growth guidance to 11–13%. This represents a downward revision of six percentage points compared to the original guidance given at the beginning of this year. The difference can be decomposed into two factors of a similar magnitude – the stronger rouble and the deferred accrual of stock-based compensation, also helped by a better rollout of IT programmes, which showed results in stability and reliability of our platform sooner than planned.

That concludes our opening comments, and I now would like to open up the call for any questions. Thank you very much for your attention, we are ready to take questions.

Operator

Thank you. Ladies and gentlemen, we will now begin the Q&A session. As a reminder, if you wish to ask a question, please press "*1" on your telephone and wait for your name to be announced.

The first question is coming from the line of Svetlana Aslanova. Please go ahead.

Svetlana Aslanova – *VTB Capital*

Hello and thank you very much for the presentation. You mentioned that fee and commission income reached a historic high. Given that we are already in the middle of Q4, what do you see as a possible guidance for fee and commission income for the coming quarters? Shall we see the Q3 as a peak, or probably we'll see a further growth in fees and commissions, albeit at a slower pace? Thank you.

Maxim Lapin – *CFO*

Thank you, Svetlana. We have a strong outlook for this year, but we are not providing guidance on fees and commissions.

Operator

Thank you, your next question is coming from the line of Sergey Garamita. Please go ahead.

Sergey Garamita – *Raiffeisenbank*

Hello. Thank you for the presentation. I have a couple of questions. The first question is a quick follow-up on your OPEX guidance. You have revised the guidance down to 11–13%, and one of the rationales for that was the stronger rouble. I was just wondering if you could give us a RUB/USD breakdown of the total OPEX? Or something like that.

My second question relates to the Unified Collateral Pool (UCP). Could you provide some specific date in December when the first stage kicks in and also if you could give us a vague idea about the difference between the two stages. So, are we supposed to see already the full-fledged differences in market participants, balances and trading activity by the end of December, or not?

Also, during the previous conference call, you were talking about – apart from the fees that you are increasing – you were also talking about an increased fee for clearing – introducing a special fee. Are we to expect any of that or are the fees that you've already announced, to be increased next year, all that we are to expect?

My third question is a bit technical and a small one. If we, just take a look at the cash flow statement, we can see that in Q3 there was some kind of an income tax refund. I assume it is a one-off, but could you just elaborate what it is related to and – are we to expect something like that in the future? Thank you very much.

Maxim Lapin – ***CFO***

Thank you, Sergey. As for the first question, approximately 30% of our expenses could be linked to US dollars, and the rest is denominated in the local currency.

As for the Unified Collateral Pool (UCP), there are several stages. The full effect of the UCP will be at the end of next year, let's say December. What happens in December this year? We are opening the trial platform for market participants. It means that, internally, we will be fully prepared, and our IT systems will be fully operational, and the market participants will have half a year to adjust their platforms to participate in the UCP. That is why the first hike in prices will take place in Q3 for those who are participating in the UCP programme. But then in Q4, there will be a universal rollout, of the platform, of the UCP solution, for all market participants in the relevant markets.

Getting back to the final question, when taxes are paid by the NCC, they are paid as a portion attributable to the previous quarter. So, that was a tax reimbursement of that quarter, compared to the previous one. I think the next question is coming.

Operator

Thank you, your next question is coming from the line of Andrzej Nowaczek. Please go ahead.

Andrzej Nowaczek – ***HSBC***

Thank you. I need to ask a follow-up question on costs. What drives their growth besides assumingly the exchange rates? You mentioned share scheme and it being deferred. Does it mean that there will be, perhaps, more expenses coming through in the following quarters, in 2018? And in any case, what is your preliminary thinking about 2018 cost growth outlook? Thank you.

Maxim Lapin – ***CFO***

That is a very good question. Let me draw your attention to the growth in D&A and IT maintenance first. What happened in 2016? We were investing heavily into the new data centre and into the stability programme designed to avoid blips and downtime in the market. For example, Q2 and Q3 were the quarters with 100% uptime during the market hours, which is a pretty nice feat achieved and sustained. The "tail" of these CAPEX expenditures is why we have a boost in our IT and D&A expenses, compared to what we've had before. It's a legacy and the majority of it, is non-cash depreciation legacy. Going forward, if you look into the next year, I am currently going through the budget process with my team and the cost centres. We will release the guidance once we have a budget available and approved by the Supervisory Board. We will keep you up-to-date.

In regards to options – the stock-based compensation has been deferred. The size can be calculated. There are relevant notes in our IFRS statement, with the balances and the assumptions behind this stock-based compensation. Thank you.

Operator

Thank you, the next question is coming from the line of Olga Veselova. Please go ahead.

Olga Veselova – ***Bank of America Merrill Lynch***

Thank you. Could I just double-check your answer to the previous question? I understand that the cost guidance will be provided later for the next year. But – the revision of these costs. Were costs partly moved to next year or not?

Maxim Lapin – ***CFO***

That's a great question. We had some internal debate here. Honestly, we see this saving as "non-rollable" going forward. One of the factors behind this is that 2016 was a record year in terms of CAPEX – a lot of programmes just came together in that specific time frame. In this year going forward, we will have approximately the same CAPEX schedule, so we are stabilising, which will not be boosting a change in our depreciation schedule and we will not have any additional spikes in capital spending. As for the FX part of the factor, FX is purely external. If the rouble sustains its appreciation we will see some savings on 30% of our OPEX. If it does not, then it will be changed accordingly. When we budget similar FX-denominated expenditures, we link them to US dollars and we are able to adjust our budget in accordance with FX rates. Thank you.

Olga Veselova – ***Bank of America Merrill Lynch***

Thank you. So the first question is – do you mind quantifying the potential impact on client balances from the launch of the UCP and cross margining? Maybe you could give us a range? And do you think that this will primarily impact client balances in foreign currency or in roubles? So this is my first question.

The second question is – do you mind sharing with us your estimates for the impact of the Central Bank beginning gold trading through the Moscow Exchange?

And the third is, do you know if the Moscow Exchange stake is in the list of the VEB's updated non-core assets, which it plans to sell? Thank you.

Maxim Lapin – ***CFO***

Ok, in regards to the UCP. UCP is a professional product, a professional solution aimed specifically at banks, who know how to manage their collateral. The rouble portion of collateral is usually held by brokers, which are not sensitive to the UCP, because their clients mostly trade in one market only. While banks, mostly, hold euro-denominated collateral, which does not bring us potential interest income. Therefore, if you look at the balances, how they would be affected by the UCP, they will be affected primarily through the professional participants whose are holding mostly euro-denominated collateral.

As for VEB, as we have mentioned before, the shareholders of the Moscow Exchange make decisions on their own, in regards to holding their stakes. Since our corporate governance is pretty robust and is in line with the best worldwide practices, we can work with any set of shareholders. So, if VEB decides to move in or move out, that would be their decision, not ours.

Olga Veselova – *Bank of America Merrill Lynch*

That's clear. And on the impact from gold trading?

Maxim Lapin – *CFO*

You mean precious metal trading?

Olga Veselova – *Bank of America Merrill Lynch*

Yes, the fact that the central bank has started trading gold through Moscow Exchange.

Maxim Lapin – *CFO*

Indeed. That is good news for us because we are developing our platform in the commodities market. It used to be about grain, now it is becoming about precious metals. We expect it to show growing volumes.

Olga Veselova – *Bank of America Merrill Lynch*

Do you have an estimate?

Maxim Lapin – *CFO*

I do not have an estimate at the moment.

Olga Veselova – *Bank of America Merrill Lynch*

No estimate, ok. On the UCP, thank you for the clarification about the euro-part of collateral. But also, do you mind sharing with us how substantial the drop in euro collateral could be – is it 20%, 10%, 5%, 50%? It doesn't have to be exact.

Maxim Lapin – *CFO*

We think that it is going to be about 10-20%. Let's say mid-range 15% would be the best guess at the moment.

Olga Veselova – *Bank of America Merrill Lynch*

Thank you so much.

Operator

Thank you, your next question is coming from the line of Olga Naydenova. Please go ahead.

Olga Naydenova – *BCS*

Hello. I have just one follow-up question regarding the Money Market and its very strong performance. It clearly saw a meaningful spike this quarter, which was partially related to an increased demand for CBR repos. Could you please estimate, for us, the impact of this event on this quarter's results – what was the proportion of CBR repos in this segment's results?

Maxim Lapin – *CFO*

In the Money Market there is a liquidity excess, so the Money Market overall is booming, not only the CBR repos, but also the GCC and CCP repos as well. The overall share of the CCP repos is also growing. As for the CBR volumes, it's a result of the CBR participation in the market and its fluctuations.

Olga Naydenova – *BCS*

Sorry I was asking about your fee base.

Maxim Lapin – *CFO*

We do not expect the fees from CBR repos to continue to grow .

Olga Naydenova – *BCS*

That's understandable, but did you give any estimates, or was I just disconnected for a minute?

Maxim Lapin – *CFO*

No. No estimates are given.

Operator

Thank you, we seem to have no further questions at this time. Actually, sorry another one coming from the line of Svetlana Aslanova. Please go ahead.

Svetlana Aslanova – *VTB Capital*

Ah yes, thank you. Just a very quick follow-up. If we are talking about commissions for GCC, CCP and CBR repos, could you please rank them – where is the highest commission and where is the lowest? I know that it is difficult to give numbers, but probably just for general understanding, what provides more effect?

Maxim Lapin – *CFO*

Of course. The ranking is as follows: the GCC repos are the most expensive product, next comes repos with the CCP, and the repos with the CBR come last.

Svetlana Aslanova – *VTB Capital*

Thank you very much.

Operator

Thank you. There are no further questions at this time. Please continue.

Anton Terentiev – *Director of IR*

Right, ladies and gentlemen, we can wait for one more minute. There may be some questions arising, and if there are none then we will just wrap it up.

Operator

As a reminder, it is "*1" on your telephone if you wish to ask a question.

Operator

There are no questions coming through. Please continue.

Anton Terentiev – *Director of IR*

Alright then, ladies and gentlemen, I think we can conclude our call, so thank you very much everyone for your participation, and I hope to hear you at our full-year 2017 conference call. Goodbye.

Operator

That does conclude our conference for today. Thank you for participating, you may all disconnect.