MOSCOW EXCHANGE

Q3 2020 IFRS results conference call

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Moscow Exchange Speakers:

- Max Lapin, CFO
- Anton Terentiev, Director of IR

Participants asking questions:

- Mikhail Shlemov, VTB Capital
- Sergey Garamita, Raiffeisen Centrobank
- Shamil Mindubaev
- Samarth Agrawal, Citi
- Elena Tsareva, BCS GM
- Andrey Klapko, Gazprombank
- Andrew Keeley, Sberbank CIB
- Olga Veselova, Bank of America
- Andrey Pavlov-Rusinov, Goldman Sachs
- Robert Bonte-Friedheim, Millennium Capital Partners
- Pawel Wieprzowski, WOOD & Co.

Investor Relations contacts – Anton Terentiev, Director of Investor Relations

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

Anton Terentiev – Director of IR

Good afternoon, everyone. Welcome to Moscow Exchange's 3Q 2020 IFRS Results Conference Call.

As usual, after the prepared remarks we will have a Q&A session.

Today, we have on the call our CFO, Max Lapin. 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 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 for the 3Q 2020. Our management presentation is available on the company's website in the Investor Relations section.

I will now hand the call over to Max Lapin. Max, please go ahead.

Max Lapin – CFO

Thank you, Anton. Thank you all for joining us today to discuss Moscow Exchange financial results.

Slide 2. Delivery on strategic initiatives in the third quarter 2020 and beyond. First, the Exchange continues to add new products. Sovcomflot, Russia's largest shipping company, broke the 3-year long IPO silence on MOEX, raising a total of RUB 43 bln – an equivalent of half a billion USD. Samolet, a residential real estate developer, followed suit, commencing its IPO in late October and raising approximately RUB 3 bln, an equivalent of USD 37 mln. MOEX launched foreign equities trading. A selection of 20 shares from the S&P 500 Index is now available in both main and evening sessions. Next Monday, on November 2nd, we'll double the amount of available foreign stocks. The list includes Chinese names like Alibaba and Baidu. We plan to expand the offering of foreign equities to 50+ names by the end of the year. HeadHunter, a leading online recruitment platform in Russia, and Globaltrans, a freight rail transportation group, did secondary listings on MOEX. This exemplifies the trend for secondary MOEX listings by Russian companies incorporated abroad. There has been a total of five such listings in 2020 YTD. We observe continuous expansion of the local ETF universe. Eight new Russian-law ETFs began trading since the start of the quarter. One of them tracks Sustainability Vector Index. It became the second ETF with an ESG focus in our offering. As a result, 49 ETFs with a total NAV of approximately RUB 100 bln are now available on MOEX. Derivatives Market continues to extend its product range. Deliverable futures on equities of Polymetal, Interrao and Mail.ru were launched as well as split-lot futures on Nornickel stock.

Second, we continue to work on new services. A personal finance platform Finuslugi – also known as the Marketplace project – went live mid-October for all clients following a successful 'friends & family' launch in early September. Currently, six Russian banks are connected to the platform and are offering deposits at competitive rates. Up to ten banks might join before the end of the year. Russian citizens are welcome to try it at www.finuslugi.ru. Derivatives Market introduced several novelties, such as iceberg orders with partial visibility of volumes or synthetic matching of calendar spreads – a feature for seamless rollover of futures. Standardized OTC derivatives' maximum contract terms were extended from five to ten years and several new base rates for interest rate swaps became available. The NSD introduced ruble DVP-2 in Central Bank Money to meet an increased demand from international investors for trading in Rubles. This new service allows Custodians to manage their liquidity more efficiently, eliminate counterparty risk and streamline operations. As a result, more investors will be able to trade in the currency of their choice. On top of that, NSD launched a new service allowing clients to access NSD's aggregate volume & value data on OTC repo transactions and deals in derivatives.

Third, we continue to develop the client base and partnerships. As of the end of October, the number of unique retail clients exceeded 7 mln and amounted to 7.4 mln. This means that more than three million new clients have joined since the beginning of the year. The total number of Individual Investment Accounts has passed the 3 million mark. The number of corporate issuers on the Bond Market continues to grow. In the second quarter, 60 corporates – including 12 newcomers – placed 169 bond issues, raising a total of RUB 448 bln. Transit 2.0, a platform for exchange of financial messages and electronic documents, continues to build the client base. Eleven banks and 20 corporates are already using it. Today and early next week, MOEX is holding its annual investment Forum in a remote format together with Sberbank. Let us move on to the thematic slides now.

Slide 3. Diversification opportunities: foreign securities on MOEX. Some people think that recent launch of foreign equities' trading opens a brand-new opportunity for our clients, which is access to global FX-linked securities. However, this opportunity at MOEX is much more mature. We've long been trading FX-nominated or FX-linked securities. Specifically, Eurobonds have been around for more than 10 years. In the current interest rates environment, the demand for Eurobonds is growing rapidly – see the bottom left chart. We respond by adding new and unbundled issues, featuring lot sizes suitable for retail investors. Today, we have 44 unbundled, split-lot Eurobond issues trading in our regular electronic order books. More than 20 of them have ADTV above RUB 1 mln, which is where meaningful liquidity for retail investors starts. We'll add up to 15 such Eurobonds till the end of the year. On top of that, ETFs on global benchmarks have become substantially more popular as measured by both ADTV and NAV – see the two charts at bottom right. Speaking of standalone foreign equities, we can see convincing increase of value held in custody at NSD and repo transactions. ADTVs can be seen on the two charts at top right. Therefore, we have six charts related to foreign instruments on the slide, and only one of them is sort of flatlining. This is because we've only added 20 foreign stocks thus far. Once we build a universe of 100+ names in the next couple of quarters, we expect trading in foreign stocks to pick up as well. Dynamics of value in custody and repo transactions as well as ETFs might be good precursors, we think.

Slide 4. MOEX listings of Russian companies incorporated abroad. We're now observing how the growing number of Russian companies with secondary listing on MOEX feeds into trading volumes. During the quarter, their share in total Equity Market volumes approached 20%. The increase was driven by the inclusion of Yandex into MSCI Russia index and the activity stemming from it. Today, we have Mail.ru as a candidate for inclusion into MSCI Russia, according to recently published research pieces. It will be interesting to see if such event an provides further support to trading volumes.

Slide 5. 3Q 2020 summary of financials. Operating income grew 6.0% YoY. Fee income surged by 30% YoY, mitigating a 30% YoY decline in net interest income. The share of F&C income surpassed 70%, the strategic benchmark, and reached the record-high of 74%. Operating expenses amounted to 4.2 bln rubles, adding 12% YoY. The recurring cost-to-income ratio increased by 1.9 pp YoY. The increase in OPEX was mainly caused by the expansion of personnel expenses by 22% YoY. I'll talk about that later. Adjusted EBITDA was virtually flat, increasing by 2.6% YoY for a margin of 70.2%. Adjusted net income added 1.8% YoY.

Slide 6. Diversified fee and commission income. Overall F&C income growth of 30% YoY rests on double-digit performance by every single business line. The top-3 leading contributors in absolute terms were the Equities Market, the Money Market and Depository & Settlement services. The latter two hit record highs. The Equity Market's share in the overall F&C structure gained 2pp YoY as it became the fourth-largest business line. It's a significant improvement from dead-last just a few quarters ago. Overall, we delivered an all-time high F&C income for the fourth quarter in a row.

Slide 7. Money Market. Fee income from the Money Market gained 38% YoY, while trading volumes increased 28%. The effective fee dynamics is explained by three factors. First, it's higher shares of CCP-based repos in total volumes. Second, an extension of average repo terms. And third, greater open interest. The overall share of higher value-added CCP-based repos, both single-security and GCC, in total interdealer repo now stands at 90%. Also, in October we launched market-makers' programs for foreign equities' repo, and the activity surged as you can see on slide number 3. It's one of the previous slides.

Slide 8. Money Market: recent trends in details. The average on-exchange repo term increased by 20% YoY, mainly due to the increase of GCC repo terms by 26% YoY. The aggregate position, a.k.a. open interest, continued to expand during the third quarter, surpassing the RUB 4.5 trln mark. The need to manage assets and liabilities amid changing economic conditions, shrinking liquidity surplus in the banking system and substantial offerings of OFZs by the Ministry of Finance may have all contributed to the higher aggregate position in the Money Market.

Slide 9. Depository. Fees and commissions from Depository and Settlement improved by 26% YoY. The main factor behind this growth was the 12% expansion of average assets on deposit at NSD. The growth was registered across all asset classes but was most pronounced in government bonds. The gap between growth rates of fee income and assets on deposit is the result of business lines beyond safekeeping. Clearing and collateral management services did particularly well in 3Q'20 amid higher demand for repo deals.

FX Market, Slide 10. FX Market fees increased by 13% YoY. Spot trading volumes added 22% YoY, while swap volumes contracted by 3.3% YoY. The higher share of spot trading remains the primary explanation of effective fee dynamics. USD/RUB pair was the main contributor to spot market dynamics among FX pairs. The number of active clients surpassed 462,000 at the end of the third quarter – up 5-fold YoY, with retail clients driving the growth. The spot market now has a higher retail volumes' share of 13%, up 6 p.p. YoY. Corporates' volumes added 17% YoY. MOEX's 3Q'20 market share vs onshore OTC reached 47% vs 42% in 3Q'19 as the demand for CCP services remains strong. The speed bump trading mode volumes exceeded USD 2.7 bln in the quarter.

Let's turn to the Equities Market, slide 11. Fee income from the Equities Market rose 58% YoY, following a nearly equivalent increase in trading volumes of 63%. The insignificant discrepancy between fees and volume dynamics was due to the tariff structure that provides incentives for higher volumes traded. It is the same effect as in first and second quarters. In other words, a few clients generated sufficient volume to get into lower tariff brackets. The fee income as well as volumes were supported by MOEX Index level that averaged a quarterly historic high of 2917 points. Velocity of trading volumes remains elevated. MOEX's market share vs the LSE in trading of dual listed stocks improved 10 pp YoY to 78% for 9M'20, reaching an all-time high. All IMOEX constituents as well as foreign stocks are now admitted to after-hours trading, bringing the number of available instruments to 62 vs 25 at launch. More foreign stocks will be added next week, including some Chinese names. ETFs will follow suit in November.

The Derivatives Market on Slide 12. Fee income from the Derivatives Market increased by 18% YoY. Trading volumes of on-exchange contracts were up 32% YoY. FX futures were the main volume driver, doubling YoY. The discrepancy between volumes and fees is due to the shift in the mix towards less profitable FX and index derivatives and a lower share of options. A few commodity derivatives saw recent surge in trading volumes despite the negative performance of the category amid lower oil prices. These include Henry Hub Natural Gas futures, precious metals contracts – such as silver and gold futures – and recently launched weekly options on Brent oil.

Slide 13. IT Services, Listing and Other Fee Income – ITSLOFI. The line showed a strong performance with fee income rising by 42% YoY. Listing fees grew 34% YoY as clients paid extra fees for accelerated placements. Information services fees increased by 39% YoY, mainly due to the ruble weakening and proceeds from information audit. Sales of software and technical services were up 21% YoY, supported by software commissioning at KASE. As in the last two quarters, other fee and commission income was largely driven by additional fees for recording individual clearing collateral in euro and Swiss franc client balances. These fees were introduced at the beginning of the year.

Fixed Income Market, slide 14. Fee income from the Bond Market improved by 18% YoY, whereas trading volumes added 23% YoY. We observed a nearly twofold increase in primary market activity due to the low base effect and a record high OFZ/OBR placement volume. The share of government bond placements in total primary market activity amounted to 84%. The discrepancy between fees and volumes dynamics stems from 3 factors. First, a lower fraction of corporate placements. Second, a higher share of short-term OBRs in the primary market. Third, a higher share of less profitable negotiated trades versus electronic order book in the secondary market. To sum it up, the declined interest rate environment supported primary market.

Slide 15. Interest and finance income in 3Q'20. Net interest and finance income decreased by 30% YoY, Core NII was down 17% YoY. The negative factor of declining interest rates coupled with a normalized level of client balances largely explains the corresponding decrease. The effective yield narrowed by 0.6pp as the investment portfolio's value stood virtually unchanged, decreasing by a mere 2.2% YoY. The client funds' currency mix expectedly changed in favor of USD due to the additional fee on EUR balances. The share of euro balances almost halved, but that of dollars more than doubled YoY. As for the composition of the investment portfolio, FX deposits and current accounts remain its largest constituents, whereas smaller shares of RUB deposits and securities remain major income generators.

Slide 16. Operating expenses excluding provisions. Operating expenses in 3Q'20 increased by 12% YoY. This brought 9M'20 OPEX growth to 5.7% YoY, below the FY'20 guidance range of 7.0-8.5%. Personnel expenses added 22% YoY and became the main driver behind OPEX dynamics. This deserves an explanation. Personnel expenses growth decomposes into 4 components: [1] 11.9 pp come from bonus accruals for 9M'20 stemming from outperformance on KPIs. For 9M'20, our KPIs were above the targeted levels. Therefore, we have provisioned for an extra bonus for the year. [2] 4.5 pp are due to Marketplace-related hires. [3] 4.4 pp net effect stems from the new LTIP program, and [4] the remaining 1.6 pp are other factors. Total D&A costs barely changed, ticking up by 0.6% due to the offsetting effects of an increase in amortization of intangibles and a decrease in depreciation of PP&E. Together with equipment and intangibles' maintenance, the line added 4.6%. Remaining admin expenses were virtually flat, falling only 0.8% YoY.

On to the OPEX outlook. First, as the development of Marketplace progresses, we expect an acceleration of spending during the 4Q. We will continue hiring personnel for the project. Second, office migration to flexible/sharable layout is also underway while the bulk of our personnel are still working from home. We still expect that OPEX returns to normalized run-rate as we enter 2021. The revised FY'20 OPEX guidance range now stands at 7.5-8.5%, 50bps narrower from 7.0-8.5% previously. CAPEX for the quarter amounted to RUB 800 mln. We also update FY'20 CAPEX guidance to RUB 2.6-2.8 bln from RUB 2.3-2.7 bln.

In conclusion, let me address the Marketplace project, now known under the name Finuslugi – Financial Services. It was launched as planned in early September in 'friends & family' mode. On October 15th, Finuslugi launched commercially, becoming available to all clients. Currently, there is a limited selection of deposit types. We are on track to make all deposit types covered by applicable legislation available by the end of the year. Obligatory car drivers' liability insurance will be added in November as planned. As for the fees, we charge 0.25% (25bps) of the deposit size plus 400 rubles for courier services required for onboarding. The ultimate fee level is negotiable depending on the degree of a bank's involvement in the project. We intend to keep client acquisition costs lower compared to banks' own sales channels.

This concludes my overview of yet another solid quarter for Moscow Exchange. We are now ready to take questions. You're welcome.

Operator

Thank you, ladies and gentlemen, we will now begin the Q&A session.

The first question comes from the line of Mikhail Shlemov from VTB Capital.

Mikhail Shlemov – VTB Capital

Good evening, Anton and Max, thank you for the presentation. I have two questions, actually. The first one is regarding the NII. Previously, I think you've been guiding that the average run rate on the NII part should have been in the range from RUB 3.0-3.5 bln. Given that you're obviously at the lower end of a range and that we are in the low interest rate environment pretty much across the currencies, is this guidance on the NII sustainable or are you wishing to revise it?

The second question is actually about the revenue mix. Obviously, the low interest rate environment has helped you to reach your revenue mix target in terms of the fees. Would you want to refresh a strategic target of 70%, which you have in the strategy? Thank you.

Max Lapin – CFO

Those are good questions. Let's turn to NII range estimate. Previously, when we have been talking about, let's say, RUB 3.0-3.5 bln range, we've been anchoring the lower range of the guidance, which is more sustainable. So, RUB 3.5 bln refers to a potential fly up if it happens. The CBR rate remains unchanged for a couple of CBR announcements already. Our expectation that we are probably a little bit short of RUB 3 billion run rate of the core NII for the quarter. If we realize some gains, we will have potential on top of that.

So, Core NII is a little bit short of RUB 3 bln a quarter. With additional trading activities' realized gains, it might be slightly above. That's the best estimate. Another driver to keep in mind is the amount of client balances. We came back to the original volume that we had for the quarter before the pandemic situation. So, we think that client balances are relatively stable. We have a little bit more rubles and a little bit more dollars, which helps. If you would chip in the fees that we are generating from euro custody – euro clearing fees – the effective sum would be RUB 3+ bln. But those fees are accounted for in the F&C income.

As for the revenue mix, I think that's kind of a good question. Yes, we hit and surpassed the strategic benchmark of having 30% NII and 70% in F&C income. Now we have like ¼ NII and ¾ F&C income. We look at this as the strategic target achieved earlier than we expected due to [1] sustainable expansion in the Equities Market this year thanks to retail investors; [2] the Money Market and [3] the Fixed Income Market due to healthy interest rate environment for the liquidity management and the bond placements.

We think that we surpassed the strategic benchmark. We don't have another benchmark in mind yet, but the direction is moving in the right way. It makes us more predictable as well. We've heard from many investors and many analysts that higher share of F&C versus NII is supportive for the multiple of the company. I hope this answers your question.

Anton Terentiev – Director of IR

I'll just add a quick word that we were talking about the run rate for core NII, not the total NII because the total contains the revaluation that we can't foresee. But the realistic run rate range of the core NII is something like RUB 2.8-3.0 bln now. That's where we are sitting at the moment.

Mikhail Shlemov – VTB Capital

Thank you. That's very helpful.

Operator

The next question comes from the line of Sergey Garamita from Raiffeisen Bank.

Sergey Garamita – Raiffeisen Bank

Thank you. Actually, I have a question regarding OPEX guidance. This range, 7.5-8.5% growth in OPEX. Does the 1 percent range in 7.5-8.5% guidance range reflect passthrough costs for Marketplace? This is the first question.

The second question regards your capital position. Could you give an update regarding your required capital? It was around RUB 80-81 bln. And now as we see, we already have more than RUB 97 bln in cash position. So, you are already up to the level of cash available for dividend distribution next time, comparable to the 2019 level. And you still have like 2-3 quarters before the next dividend payment.

Could you give an update on the required capital level? Is it still RUB 81 bln? Thank you.

And my final question regarding your CAPEX. Does the one-off increase in CAPEX guidance reflect any additional CAPEX for Marketplace or something else? Because you mentioned in the press release that you lowered your planned investments in KASE for this year. What's the reason for the CAPEX increase then?

Max Lapin – CFO

Sergey, let me start with the OPEX guidance. The guidance at the beginning of the year was wider because the lower end of the range was pretty much conservative about the speed of the Marketplace development and the risk of potential weakening of the ruble. The higher end of the guidance range was slated for somewhat weaker ruble and full speed Marketplace development.

That's why we are moving up the lower end of the guidance range because it becomes irrelevant, because Marketplace went live and there's some weakening of ruble, but we are not moving the higher range of the guidance, not at all. That's the logic behind it.

The logic behind CAPEX guidance is virtually the same. We have some impact from devaluation because CAPEX has hardware and licenses components, which are billable in dollars or pegged to dollars, on one hand. On the other hand, CAPEX includes full speed Marketplace development, which is happening.

Therefore, we are drifting to the higher end of the CAPEX guidance range that we had, because we are moving in accordance with the aggressive plans for the Marketplace. It's moving as we planned. You might also consider yet one more additional factor. We are looking at the change of regulation in Russia that some software might be VAT – value-added taxation – chargeable as of 1st of January next year. Therefore, we are considering to buy some of that software in December, and therefore, under this year's VAT taxation, which is absent for some particular parts of software.

So, that's what we are looking into. It's quite an effective solution because it will be like 20% cheaper if acquisition of the software is done by the end of the year. And since a lot of software is amortizable as an intangible asset, it might also fall into the slightly increased CAPEX guidance.

This answers two of your questions. Let's move to the capital level question. Yes, we do announce in our investor presentation on Slide 5. If you download the investor presentation from the website, you will see the capital position that we have. It's roughly around RUB 80 bln, all in all, like regulatory requirements, and we are moving slightly above that.

I have to remind you that our regulatory capital for NCC is quite proportional to the volume of trading and the volume of collateral. Collateral remains roughly unchanged. NCC is well capitalized, and we are pretty decently capitalized for the dividend, that's another angle that you touched upon.

We will be talking about some refinement of those RUB 80 bln capital requirement benchmark. We will be talking about it in the coming quarters. As for the dividend calculation, there is CAPEX, there are potential M&As, there are changes in regulatory capital, which are somewhat proportional to the volume of trading. So, we have some proportionality in the capital level akin to working capital type of proportionality for other companies, but it's quite limited.

As for the dividend calculation, we are really looking at the capital adequacy for the first quarter of the year, that's when the dividend calculation is taking place. Therefore, I would say that for the dividend calculation we might have a quarter to go, but not much more – then the dividend cut off date happens. It's not like you can incorporate half a year into calculations because the dividend recommendation is due in March.

I hope this helps. I think we have a strong capital position for the company, adequate capital levels, pretty much confined OPEX and CAPEX growth for this year and might expect healthy free cash flow to equity available for 2020.

Sergey Garamita – Raiffeisen Bank

Thank you. And the final question regarding CAPEX. Where do you see the sustainable level in view of the ruble depreciation and other factors?

Max Lapin – CFO

Very roughly speaking, CAPEX is 50% nominated in USD or pegged directly to USD. So, we have some devaluation impact on that – let's say, half of CAPEX. Then for the next year we will have some further development of Marketplace because we will be developing the commercial loans functionality. We will be CAPEX'ing those lines of code development. And we will have some additional CAPEX for the data center update, because we moved into the new data center several years back. It's time to update some of the service, because of the technical policy.

I will be talking about the CAPEX guidance for 2021 in March. So far, we are going through the budgeting cycle. But I would think of MOEX that we are striving to make our business with a predictable level of costs and we succeeded in that. The only flexible thing that we have is the speed of the Marketplace scaling up. We are looking, so far, into the user experience of the Marketplace project. It went live for everyone in the country just a couple of weeks ago. So, it's too early to tell, but we have several scenarios for the Marketplace development. We are looking at them by the end of the year. And by March, we'll have a good guidance for 2021.

Anton Terentiev – Director of IR

Since we are discussing capital and Marketplace, I will just read out loud a couple of questions that we have in the webcasting interface. The first one comes from Shamil Mindubaev. What trend in ruble balances will be in the future? From what does it depend mainly? So, Max has just touched on the level of client balances, but regarding rubles, mainly it will depend on the amount of trading volumes. And at the same time, where we stand right now in the historical context is quite a sustainable level.

And the second question is from Samarth Agrawal from Citi. Congratulations on launch of the Marketplace project and thanks for the additional details. Just one query. I understand it is in early stages, but could you comment on the initial customer feedback that you have received? And one more, if I may, could you comment on progress on operational efficiency program at NCC announced in Q2?

Max Lapin – CFO

Yes, good. As for the Marketplace feedback, we went through September to hammer out all technical potential bugs and glitches and it went fine. So, we are satisfied with the 'friends & family' mode. 'Friends & family' mode so far is over. The marketplace project is out for the customers. So far, we have observed the conversion funnel, we are observing the conversion ratios and collecting focused feedback on the technical components.

The good feedback will come when we expand the selection of banks by the end of this year. We have 6 banks at the moment. When we expand to 10+ banks and have a wider range of products, it will be the proper time for customer feedback. And as for the second question, Anton, would you please remind me the second question?

Anton Terentiev – Director of IR

Yes, sure. It's about the progress on operational efficiency program at NCC that we announced the previous quarter.

Max Lapin – CFO

The operational program at NCC is aimed at the risk management at NCC. Basically, this program focuses on two things: fully automatic mode for all of the clearing regimes' risk control and cybersecurity. So, this operational program is aimed at preventing risk from occurring. We have a selection of risks that happened with the NCC in the past. Therefore, this program aims at risk prevention per se. We think that it is rolling out just fine, it's one of the KPIs for the company. We will be looking at it through the cost efficiency, through cost-benefit analysis, the amount of costs that are required to support diminished risk profile. So, we will be talking about those cost profiles for the operational risk management in the year to come.

So far, whatever costs that happened throughout this year, they went into this year's OPEX numbers, and they are within the guidance that we have.

Let me remind just one more time. It's not the pure cost cutting program per se. It's a risk management program to prevent operational risk from happening and repeating at NCC, where roughly 4 trillion ruble worth of transactions occur on a daily basis. That's a lot. So, there we shouldn't have any revisions and reserves.

Anton Terentiev – Director of IR

Thank you, Max. We are ready to take further questions over the phone.

Operator

The next question comes from the line of Elena Tsareva from BCS GM.

Elena Tsareva – BCS Global Markets

Good afternoon. Thank you very much for the call. I have several follow-ups on the questions asked earlier. One question, a follow-up on NII. Given we had a very strong trading volume update in third quarter, we had balances actually contracting QoQ. What could be the explanation for such decline in client balances despite volumes growth? This is my first question.

Max Lapin – CFO

Well, client balances just went back to normal. Elena, let's look at Slide 15. The client balances in the third quarter are virtually the same to what we had in the first quarter and similar to the quarters of last year. We are having less euros and more dollars. But all in all, it's the same amount. What I would look into, given that a vast majority of net interest income is generated in rubles, is the higher share of rubles. The share of rubles is higher because rubles serve as a collateral currency and as a settlement currency. Settlement, it's a single account for collateral and settlement purposes. Since settlements are being done in rubles and settlement is proportionate to the volume of trading, the amount of ruble collateral is increasing. 2/3 of the euro and dollar collateral are being driven by the FX market. These currencies serve as a collateral and settlement funds for the FX market. They will be volatile, but the impact on NII is relatively limited. So, we are back to a normal level of collateral, nothing special is happening this year. We are not observing unusual things.

Elena Tsareva – BCS Global Markets

Understood. Thank you very much. My second question for you is about OPEX. You're saying that in 4Q you may see OPEX going to normalized run rate. So, what is the normalized run rate you see for OPEX for the next year? Can you provide some kind of a range?

Max Lapin – CFO

Yes. Good question, Elena. We are working out the budget for next year. In fact, in our company, we are switching from one-year budgeting to three-year business planning to keep it aligned with the strategy. In the strategy, our goal for the costs was very much simple. The F&C go above 10%, costs definitely should be growing at CAGR below 10%.

So, for next year, we are not yet issuing guidance. We'd like to repeat the suit that we have already developed: we should have positive operating jaws for F&C income and operating costs. It might be tougher next year because we have a huge F&C run-up for 2020. But let me assure you, our internal aim that business, excluding Marketplace, should behave as before. The Marketplace project is sensitive to the amount of advertising rubles being spent to acquire clients. We are planning like 3 scenarios for Marketplace ramp-up, and that's the only unpredictable or relatively less predictable amount of spending for the next year. The range is not that big. I'd rather not talk about it before March when we see how the first wave of marketing and customer acquisition went. So, before March, I'd rather not outline a specific guidance. But other cost disciplines should remain the same.

Elena Tsareva – BCS Global Markets

I assume that a normalized run rate for the costs, excluding marketplace, could be like around 7% growth a year? Or this is not what you are going for?

Max Lapin – CFO

Normalized means excluding Marketplace, because Marketplace is an advertising gorilla in the room. For Marketplace, I cannot talk numbers, but for the business as the fees without Marketplace, we'd like to repeat what happened this year, the year before and what's in our strategy. We are still nailing down the range that we are planning for next year.

Elena Tsareva – BCS Global Markets

Understood, thank you. And just a minor question on the provision increase. So, what is the rationale? It's not a major amount, but for nine months it's already like RUB 300 mln something. So, what is the rationale of pickup of the provision? And also, if you could just remind the main calculations behind this provision.

Max Lapin – CFO

It's purely a CDS expansion that affects the calculated provision on the bond portfolio that we hold. The way it happened through the year, let's say, in the first quarter, when volatility hit, we had that IFRS 9 expansion on the bond portfolio to the tune of RUB 850 mln. Then we wound down this provision of approximately RUB 600 mln in the second quarter because volatility went down. Now we are, let's say, because volatility is somewhat up in 3Q, we restored some of that provision because of the CDS adjustments. So, I would say that this provision fluctuations are proportional to whatever is happening in the CDS universe – CDS range on the Russian debt universe. That's it. We didn't have any defaults, we didn’t have any cash losses. So, it's a pure calculatable provision.

Elena Tsareva – BCS Global Markets

Got it. Thank you very much for the answer.

Operator

The next question comes to the line of Andrey Klapko from Gazprombank.

Andrey Klapko - Gazprombank

Hi Max, Anton. Thanks for the call. In your presentation in Equities section, you voiced about the tariff structure changes to stimulate the bigger volumes. What are your plans to fine-tune tariff lines across the segments? If you could share about the upcoming decisions, it would be very helpful.

Max Lapin – CFO

Well, good question. One refinement and one projection. We did not change the tariff structure for the Equities Market. The very simple thing happened: some of the traders hit up the certain level of volume when they get the fee discount based on the volume of trading.

So, the tariff structure remains the same as it is disclosed on our website. Roughly speaking, the basic flat tariff is 1.8 basis points for the Equities Market on both parties. If you trade more, you might have some discount, but they are limited. So, it’s not like if you trade more, the tariff goes to null, no.

We've been benchmarking our tariffs many times to other markets. We are not changing the basic tariff structure for Equities, no.

Andrey Klapko - Gazprombank

Ok, thanks. It’s very helpful.

Operator

The next question comes from the line of Andrew Keeley from Sberbank.

Andrew Keeley - Sberbank

Good afternoon. Thank you for the call. A couple of questions. One is on your depository and settlement services. It seemed like that was the line that really beat my expectation and it seems like consensus as well in 3Q. It was a super strong quarter. And I'm just wondering if you can help us, in any way, understand how we can perhaps better forecast this line. I see from the presentation, the growth in the F&C income at this line is quite a lot higher than the assets on deposits, and you mentioned some other factors. But if you can maybe just give us a bit of color about what kind of the marginal revenue drivers are in this area, that would be very helpful. And then I'll ask another question after.

Anton Terentiev – Director of IR

OK, Andrew, I'll just start answering your question. You rightfully noticed that depository and settlement services are generally driven by the value of assets held in custody. And that's what was exactly the case in this quarter, but also the outperformance came from business lines beyond safekeeping. And we mentioned them on the slide about this business line. These are specifically clearing and collateral management service charges. These are the two income streams related to repo transactions. As you know, we have the big Money Market on exchange. And another kind of smaller money market at NSD. That's OTC repo transactions that people do through NSD.

And as you look into the Money Market, you see that position in the Money Market increased and, basically, the demand for repo transactions increased for the reasons that Max has mentioned during his speech. But same factors work for NSD. At NSD we also saw an increased demand for repo transactions, and that's what helped these other business lines beyond safekeeping. And what's going to happen next is anyone's guess, but from my discussions with colleagues, these are not one-off transactions. These are not one-off business events. And this elevated demand for repo might persist.

Max Lapin – CFO

Andrew, yes, that's a good question, and Anton pretty much covered it. I will add some color onto it. On page 9, we see that safekeeping charges come to be like 2/3 of the revenues of NSD. Those are very reliably proportionate to the assets in custody. So, that proportionality stands.

The red pie that you have here on the slide, like 1/5 of the existing revenue structure, is proportionate to the repo market to a large extent. Those repos at NSD could be roughly proportional to the repo market that we have in the Money Market on the Exchange itself.

Yes, they might be quite unpredictable for the outsider, but they resemble the overall logic of the Money Market.

Andrew Keeley - Sberbank

OK. That's very helpful. Thank you. And a couple of other questions. Can you just outline what your kind of strategy is towards admitting foreign stocks or trading foreign stocks? Because, at first, I thought it was just the U.S., and now I hear you're looking at China as well. Is it just Alibaba and Baidu? Or will there be others? And just any kind of color of how you think about that?

And then – sorry, and then my final question, I'll ask quickly. I see your headcount went up by 100 in the quarter. Was that pretty much all driven by the Marketplace? And are you largely done now with the headcount increases, which have been quite high?

Max Lapin – CFO

Yes, good questions. On the equities' addition strategy. We are onboarding probably up to 50 additional stocks a quarter, through that speed, that's our target for the next year to add 30-50ish stocks a quarter. All of those stocks got to be admitted to custody at NSD. So, we now have a fully-fledged localized solution, when the stock your acquired is custodied at NSD.

Therefore, this structure is more robust than other solutions present in the market and it's more safe. This admission takes a little bit slower pace than just cross trading.

Therefore, that's what limits the speed of the stock offering. But all plans for the next year, let's say, probably 30-ish to 50-ish a quarter addition. The way we approach those stocks, we're looking at, I would say, high-quality type of stocks, which are included into indices for regions and the countries, let's say, we're looking at the top names of S&P500 and similarly from China.

That's the logic. We'd like to expand our universe and it will be expandable at such a rate as I mentioned. I hope that answers your question for the equities. Does it, Andrew?

Andrew Keeley - Sberbank

Yes, it's good, it does. Thank you.

Max Lapin – CFO

The one on the headcount. The headcount we observe here in the presentation on the cost structure slide has a relatively simple explanation. We are ramping up the Marketplace development project and Marketplace requires its staff.

At first, we were doing some outsourcing solution for the Marketplace and then, when we saw that developing code internally is cheaper, we hired some personnel. So that expansion in personnel is mostly attributable to the Marketplace project. And some of that expansion is attributable to the risk management at NCC as we are going through this operational risk management excellence project at NCC.

We are looking at the headcount numbers very thoroughly. We do know that you, as investors, care about those numbers. And we're projecting our business plan with a tight attention to those numbers as well.

Andrew Keeley - Sberbank

Thank you. Can you add any color on whether you feel like we are at a point where we'll revert back to the kind of 10-20 a quarter that was the run rate pre-Marketplace or there's still going to be quite a bit of growth related to the Marketplace to come?

Max Lapin – CFO

Well, I would say that Marketplace drives a large chunk of that. It's visible from the right-hand details on the slide 16. And if you compare YoY, the growth is like 10% and 4.5% in terms of money is driven by the Marketplace. So, the larger part of that impact is the Marketplace. The rest comes to the improved risk management headcount at the NCC, but that's basically it.

Going forward, we will be talking about Marketplace in more details. We will be disclosing somewhat more numbers when we will try to explain the performance of the business as is and the variable part of the Marketplace going forward. So, we will be disclosing that, but please let me do it in March rather than now.

Andrew Keeley - Sberbank

Ok, that sounds good. Thank you.

Operator

The next question comes from the line of Olga Veselova from BofA.

Olga Veselova – Bank of America

Thank you. It's Olga Veselova from Bank of America. I have several questions. Do you think, Max, that the Marketplace can start to generate any visible EPS in the next two to three years? And do you think that the client acquisition cost can be shared with someone, possibly with product providers or maybe with the regulator, given that they are interested in the evolution of this marketplace? So, this is my first question. I will ask my second question after.

Max Lapin – CFO

Yes, for the marketplace, we want to show visible revenues from Marketplace project the very next year. That's our aim because we have like one product already available and the other products hitting the shelves shortly, I'm talking about the car drivers' liability issuance in November. With those 2 products, we'll have like a decent business line to show some revenue. We will be able to launch commercial loans a little bit further into 2021 – there's no specific date yet. Then we will have visible revenues.

We will be talking about the Marketplace revenues specifically starting at full year's disclosure. So far, we've had a month and a half of 'friends & family' mode for limited range of customers, and we opened to public around two weeks ago. Let us see. It's not yet that predictable.

In terms of customer acquisition costs, I would say that the project is functioning under the premise that the customer acquisition cost for us and for the bank participating in the platform should be lower than the customer acquisition cost for the banks using their retail network, retail footprint and their marketing expense. That's the benchmark.

We will be also disclosing the cost of customer acquisitions as part of the next cycles of disclosure, and we will be commenting on that. So far, it is too early to tell. We have like only 2 weeks into the full commercial launch. We have a figure in mind. We have a cap on that figure, and we are sure that we can live under that cap.

Olga Veselova – Bank of America

OK, thank you. I have two more questions. Given the high positive impact on trading volumes from the market volatility during the first nine months of this year, do you think that there is a risk that in any up segment, trading volumes can be down or flat next year? And I'm most interested in derivatives and equities. How do you see that? Or you still expect that there will be some growth despite this factor?

Max Lapin – CFO

Well, wonderful question, because it's right into the eye of the business model. Let me refer to Page 6. What's been happening in 3Q was not driven by volatility. We have healthy expansion in all of the markets, not because of volatility, no. Volatility was gone by May. May was in 2Q and in 2Q I was cautiously mentioning that it's fundamental. It's not momentum. Those are fundamental factors explaining sustained increased volumes. By 3Q, I may be more confident about this because it's on the page here. Let me deep dive. Volatility hits or supports FX, Equities and Derivatives Markets first. What happened in March and April, we had a fly-up in the FX, Equities and Derivatives volumes beyond imagination. It was happening because of the volatility. Volatility was gone by May, but volumes did not go down. Why is that? Because there are several strategic factors. First, increased retail interest. Retail is the fundamental driver. Volatility is gone, but retail is here, so the numbers are helping. Then we had the expanded need for liquidity and the soft monetary policy by the Central Bank.

In a nutshell, it means that should we have gone down in May to the original numbers without strategic support, we would be able to show healthy 3Q numbers. We have three markets driven by volatility: FX, Equities and Derivatives market. But now volatility is gone, they are strategically supported by the fundamental factors. Money Market, Depository, IT service, listing and other fee income are position-driven markets, they are not volatility-driven.

So, I would say, a lot of people think that exchange is driven by volatility. No, only three business lines are actually driven by volatility, but the 3Q numbers are strategically driven. I hope it helps.

Olga Veselova – Bank of America

Yes. It does. Thank you. And my last question is about competition. I wanted to ask how did the competition with Saint-Petersburg Exchange evolve? And here I have two sub-questions. What is your differentiating factor versus the competitor other than the currency in which retail clients trade - ruble and dollars? So, what is really different for the customers? And second, if you have that, can you give us the market shares in trading volumes by households between Moscow Exchange and Saint-Petersburg Exchange?

Max Lapin – CFO

We believe that competition is good, it helps to create better services for the customer. In our case, in order to compete, we have to build a more reliable international stocks offering at Moscow Exchange, which I explained earlier that in our way the ownership of the stock in question is direct instead of through the chains of the brokerage houses. So, we think it's a more reliable, more robust product offering for the customer.

The other thing, we offer trading in rubles, which avoids one step of currency conversion in the offering. You don't have to convert currency before starting trading. It's more direct.

As for the market shares, Anton, would you please help me on that?

Anton Terentiev – Director of IR

OK. Olga, what market shares specifically are you talking about, how do you measure them?

Olga Veselova – Bank of America

Yes, trading volumes, the market shares in trading volumes in household segment.

Anton Terentiev – Director of IR

Well, you can only compare their volumes in equities trading versus our volumes in equities trading. And recently, in equity trading, their volumes have been increasing quite substantially. And at times, on some select days, they were getting comparable with our volumes. But, on average, they are still a bit lower than us. So, their share could be 40% if you put all equities together. But if you don't do that and you look at Russian equities stand-alone and foreign equities stand-alone, then you will not see much of an intersection. You will still have 100% Russian names with us. And a vast majority of foreign names still with Saint-Petersburg Exchange, if that answers your question.

Olga Veselova – Bank of America

Yes, thank you.

Operator

The next question comes from the line of Andrey Pavlov-Rusinov from Goldman Sachs.

Andrey Pavlov-Rusinov – Goldman Sachs

Hello, Max, Anton. Thanks a lot for the call. Most of my questions have already been asked. So, I just have one follow-up on the net interest income dynamics. So, if we could go a little bit deeper into the FX portion of your interest income. And if you could discuss, basically, whether the decline in dollar yields that we have seen in the global markets has already been largely reflected in your 3Q numbers. Essentially, should we expect any further decline in your dollar yields if the global rates stay where they are?

And also, it would be also helpful if you could share the amount of the FX interest income that you made during the quarter? Maybe just in broad terms, whether it was like RUB 0.5 bln or RUB 1 bln, portion of your RUB 3 bln core NII?

Anton Terentiev – Director of IR

Yes. I'll just start answering that. First, on dollar instruments yield, yes, you can actually see a decline because of one simple thing. Still, instruments in our portfolio get redeemed. They reach the maturity and they get redeemed, and we have to replenish the portfolio. We have to buy something new. And when we buy these new instruments, the coupon that they generate, the income that they generate is already based on the new rate, it's a lower rate. So, that's what happened in Q3 when we had a substantial cushion in our FX exposure get redeemed, and we had to replace it. So, that's point number one.

And then point number two, on the FX component, just reminding that it's all fixed income or cost in nature. Because if you're a treasurer and you manage your ruble exposure, you can either put it into overnights with banks or some short-term securities or invest, let's say, in euro-ruble swaps, where you change rubles for euros and then change them back and you know your entry-level and exit level upfront and the interest rate differential is your interest income. Or you can do the reverse. If you're experiencing, let's say, an outflow of US dollar funds, you can either sell your portfolio and lose income, or you can actually swap euros for dollars, which are mostly laying idle because of the lack of investment opportunities. So, we can swap these idle euros into dollars, cover the outflow and still retain the investment that we have. And if there is a positive gap, that's the thing you would do as a treasurer.

Andrey Pavlov-Rusinov – Goldman Sachs

Thanks, Anton, that's helpful. And still, some number would be helpful. I understand that the management could be quite complex, but essentially, what you earn on the core part of your FX portfolio, potentially on FX security, what would be the average yield you generate in the 3Q? That would be helpful to know.

Anton Terentiev – Director of IR

OK. We can think about it, but that's not the figure we have at the moment.

Andrey Pavlov-Rusinov – Goldman Sachs

Sure-sure. Thank you.

Operator

The next question comes from the line of Robert Bonte-Friedheim from MLP.

Robert Bonte-Friedheim, Millennium Capital Partners

Hi, it’s Robert Bonte-Friedheim from Millennium, thanks for taking the question. Again, I think a lot of people have asked around the question, so let me just approach my understanding a little bit differently. I think a lot of your products and especially on the derivatives side, I think it feels like people use it to counteract volatility. It’s a good hedge against the volatility that we've seen rising over this year and next year. And again, and I'm wondering if you see it that way? I mean, if you look at the derivative volumes, they were very, very high in September, much higher than in July and August. Can you give us, one sense of how we should think about the ranges of derivatives volumes for 4Q into next year? What kind of a range? And two, maybe just give us some color on how October is doing so far on the derivatives side?

Max Lapin – CFO

Well, the numbers for October are due early next week. I think you will find them satisfactory. The daily volumes are also available on our website. You might look into daily volumes statistics, let's say, it's positive.

The derivatives, yes, indeed, the derivatives volumes are sensitive to volatility. But once we have that expansion in the base assets being tradable and some devaluation in dollar – we’ll have an expansion in derivatives volumes. So, derivatives volumes are not only driven by volatility. They are volatility-sensitive, but derivatives expansion that we are observing now is a fundamental. More base assets being traded and currency rate fluctuation is helping.

But as for the guidance for specific derivatives numbers, we are not issuing guidance line-by-line. I would look into our strategy, where we attribute a substantial chunk of featured growth to macro factors. And then we have our initiatives on top. On a quarterly basis, we cannot forecast whatever revenue is going to be coming because macro factors are really impacting volumes or not. So, we dare not predicting derivatives volumes for the quarter, we dare not.

Robert Bonte-Friedheim, Millennium Capital Partners

Ok, understood. Thanks for taking the question.

Operator

There are no further questions at this time. I would like to hand over the call back to Max Lapin for closing remarks. Thank you.

Anton Terentiev – Director of IR

Sorry, I'll just read out loud one more question from the webcasting interface. I'm not sure we can answer it. I think Max has touched upon it a few times, and we cannot provide any more details, but I will just read out loud once again.

It comes from Pawel Wieprzowski of WOOD & Company. The question goes as follows. Could you please share with us your considerations over the costs of running Marketplace project after the ramp-up onboarding stage? As far as I remember, you mentioned during the previous call, it might be up to two years. If I correctly understand, after this period, you will strive to keep the OPEX cost growth, including Marketplace below F&C growth, yet in 2021 and 2022, it may not necessarily be the case given the project. Is that correct understanding of your approach to the cost management?

Max Lapin – CFO

Wonderful. It refers very much to the point that Andrew Keeley made probably a year ago, when we were talking at one of the MOEX Forums.

We might be fronting or front-loading some costs for the Marketplace development in 2021-2022. In 2020, we managed to go within the guidance, which is good. For 2021 we are entering active marketing expenditure space, therefore, we might have more dynamics in Marketplace costs YoY that are beyond the growth in F&C. Therefore, I'd like to draw your attention one more time. We'd like to start talking about business as is on Marketplace as a separate revenue line starting next year because Marketplace will start ramping up. With Marketplace it will be hard to keep the total rate of cost growth below F&C because we are fronting some advertising costs, but for the original business - that's one of our key strategic themes.

So, Marketplace is akin to a new business line created from scratch, which will require marketing expenditures. Let’s see how we fare with the Marketplace project until December and January. That will give us ample of data to look into and talk about customer acquisition cost and the revenues and the potential efficiency of Marketplace. Because on one hand, we already disclosed the number. Any customer deal has a fixed flat fee of RUB 400 for customer onboarding and 0.25% - it's flexible - 25 basis points for the transaction payable by the bank. That is the preliminary revenue structure that we have.

And once we hammer out the customer acquisition costs, we’ll have two points of data sufficient to model the Marketplace. You'll see the customer acquisition cost, and you will see the revenues. Hence, you'll see the efficiency, and you will be able to model Marketplace like a stand-alone business line. I don't have customer acquisition cost in stone or range yet. I only know the cap for customer acquisition cost that it should not be higher than what the banks are using now. So, we are aiming that Marketplace will be more effective. I hope this helps.

OK. Then moving on. Anton, we have no further questions, right?

Anton Terentiev – Director of IR

Yes, we don't have any more questions in the queue. So, since we have closing remarks at our hands, I think we can just say thank you, everybody, for great insightful questions and staying in touch to reconnect next time with our full year results.

Max Lapin – CFO

Please, appreciate the fact that we moved our IFRS disclosure one week earlier. We intend to replicate that experience for 2021. One week earlier is better. Next week, we'll have potentially good news. Expect the volumes disclosure for October. We have a great 3Q. We're having robust start of the 4Q. Let's look forward to the year-end. The Exchange is doing fine.

Thank you, and see you at our next call in the first week of March.