



CONFERENCE CALL DEDICATED TO VK FINANCIAL RESULTS 3Q 2021

Company: VK

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Participants:

- Boris Dobrodeev, Chief Executive Officer (Russia)
- Matthew Hammond, Managing Director, Chief Financial Officer
- Fedor Rubtsov, Chief Financial Officer (Russia)
- Vladimir Gabrielyan, First Deputy Chief Executive Officer (Russia)
- Vladimir Nikolsky, Chief Operating Officer (Russia)
- Tatiana Volochkovich, Director of Investor Relations

Tatiana Volochkovich:

Thank you all. And welcome to VK's Third Quarter Unaudited Financial Results Conference Call. I'm joined by Boris Dobrodeev, Matthew Hammond, Fedor Rubtsov, Vladimir Gabrielyan, and Vladimir Nikolsky.

In light of the elevated number of COVID cases in Russia, we continue to work remotely and still at least the end the year. As a result, we are in multiple different locations and hence coordination during Q&A might cause some minor delays in our responses. We also kindly ask you pose one question at a time to keep things manageable on our end. We will take time to answer all of your follow-up questions and thank you in advance for your understanding and cooperation.

Before I pass it onto to Matthew, I will read the Safe Harbor statement. Please note that our results press release contain statements of expectations and other forward-looking statements regarding future events or future financial performance of the group. The forward-looking statements in the release are based upon various assumptions that are inherently subject to significant uncertainties and contingencies, which are difficult or impossible to predict and may be beyond the group control. Many factors could cause extra results to different materially from those discussed in forward-looking statements, including those referenced under the risk factors in the group public filing. We would like to direct you to read the forward-looking disclosures at the back of our release, particularly with respect to the possible difference between management and IFRS accounts. Matthew, please go ahead.

Matthew Hammond:

Thank you very much. Good afternoon. And thank you all for joining us. I'm maybe reading a little slower today. And so, you'll have to forgive me because COVID can spread literally anywhere. Anyway, Q3 group revenue grew nearly 19% to 30.4 billion roubles in the third quarter with strong year-over-year performance from advertising and education technology services. Community IVAS returned to growth with largely flat performances to MMO Games, given the sort of challenging base effects combined with no major new launches.

When it came to profitability, Q3 Group EBITDA grew 28% to 8.4 billion with a margin of 27.7%, two percentage point improvement year-over-year, driven by the improvements of profitability

across Communications and Social, Games and New Initiatives. Group net profit from consolidated subsidiaries grew 41% to above 3.8 billion roubles. At the same time, the group reported a net loss of 1.4 billions roubles, including the contributions from the key strategic associates and JVs versus a net loss of 415 million roubles a year ago. The main drivers from the JVs, were the 3.9 billion ruble share and the losses reported for the O2O JV and 1.2 billion for AER in the third quarter. JVs remain in investment phase with roughly 26 billion roubles in related investments that we've made in 2021, including 21.5 billion into O2O JV and 4.4 billion into AER. However, we're focused on both growth and unit economics. For example, losses from O2O JV were flat quarter-over-quarter. And most of its components are expected to reach EBITDA breakeven in the next two to three years. Before I move to provide specific comments on key business areas, I'd like to send you over to Boris to comment on our rebranding. Boris, please go ahead.

Boris Dobrodeev:

Thank you very much, Matthew. Good afternoon, everyone.

So, two weeks ago we started a new chapter in our history and our company, having rebranded into VK. The rebranding came as a natural step in the process of our evolution into an ecosystem with a related strategy announced in 2020.

To achieve the leading position on the market in the new Internet era, we're required not only to continue to launch high quality and convenient services for millions of users, but also to maximize links between our products and services. Until now, we were lacking such association in the minds of our users. This came clear from our recent poll showing that nearly 60% of all Russians associate our group with email and less than 10% associate us with social networks, games and other services.

With social and communication products being at the heart of our ecosystem, time has come to change perception by building stronger links between our nearly 200 different services with VKontakte at the core of the group.

Why VK? Because the VK brand is universal. It has major potential, and is highly recognizable. 100% of Russian Internet users know it. And more than 85% use the social network VK every month. And it is the most favorite social media for almost 90% of Zoomers, which means VKontakte is not just about the present, but it is about the future .

Following the rebranding, we're adding VK to product names, fully renaming some of our services and endorsing the others such as those we own partially. All the new products will be launched under the new VK branding. Following multiple experiments carried during the past one-and-a-half years, we already see positive effects from association with VK. For example, VK Jobs following its rebranding from Worki, saw product awareness rise by almost 40% with intention to use increasing by over 50%. We want to scale these effects across the Group and across other use cases. Some of the near-term releases will include VK Ads, VK Music, VK Games, VK Devices with the VK Video, Group's unified video platform, already launched.

Also, Youla is in process of full rebranding into VK Classifieds.

So, the new chapter requires legal entity and ticker changes as well. Based on current timeline, this shall be done before year end.

Rebranding does not lead to major changes in the strategy of the Group as this is the next step in the logical ecosystem development strategy announced a few years back. We have seen major

progress across our ecosystem development since then with multiple visible benefits for the Group already. For example:

the average number of services used within Combo rose by 35% year-on-year in October, with Combo users having nearly 40% more active days in our services per month versus an average user and with user ARPU increasing by almost 30% after joining our loyalty program, including more than 50% higher ARPU for our O2O services

Marusia monthly users grew by more than a quarter, quarter-on-quarter, in Q3 to almost 7 million users following its integration into VKontakte

Total cumulative number of VK ID users outside VKontakte and in Mini Apps rose by almost a third since June exceeding 52mn since launch last summer, with more than 30 connected devices and nearly 370,000 in daily first authentication using VK ID outside VKontakte and Mini Apps.

And we think that this is just the beginning. However, our broader ambition is for the rebranding not only to bring us closer to the aspired local ecosystem leadership, but also lead to revenue and margin benefits for the Group as unification of services means unification of teams and therefore room for higher efficiency.

For example, integration of our advertising team has already resulted in 4x increase in accuracy of click prediction with 3x growth in app installs and 30% lower acquisition costs for advertisers.

We therefore target multiple positive effects from the rebranding, with those benefits across all businesses areas. And we are very excited about this major milestone in the history of the group. Matthew, please continue.

Matthew Hammond:

Boris, thank you very much. Turning back to the key business highlights.

First, on advertising

Advertising grew by 28% year-over-year in the third quarter, exceeding 12 billion roubles, and remains the key driver of our revenue accounting for over 40% of the group's total.

Performance advertising remained the key driver with 40% year-over-year growth in the third quarter. Within advertising formats, we saw 52% year-over-year growth of in-stream video ad revenues, significantly above the 36% growth rate seen in Q1, with further monetization of video being amongst the key strategic priorities.

The SME subsegment continues to increase as a percentage of ad revenues. And the number of advertisers continues to rise, with the largest 10 advertisers now just below 15% of total ad revenue, with related concentration down by almost 3 percentage points year-over-year as of the first nine months of this year.

Above market advertising revenue growth is driven by constantly improving our AdTech. For example, we recently saw ad clicks per user per day reaching a three year high with only about half of the previous numbers of ad impressions needed to get one click given the improvement in the predictive models. We also see nearly 50% reduction in cost per install through better predictive models, which drives revenues from app install ads.

2021 has very different base effects in advertising as a result of COVID, with the Q4 2020 base effect higher than Q3, there is obviously an effect. Notwithstanding this, we continue to expect that we will outgrow the broader digital market.

On community IVAS:

IVAS, which accounts for nearly 15% of the group's total revenue, returned to growth with an expansion of almost 6% versus a decline in the first half of the year.

The main driver of IVAS is music, which sits at the heart of our VK Combo loyalty program, where we had over 4.5 million subscribers as of the end of September, with 94% being paying users.

We expect similar growth rates for IVAS in Q4, with moderate growth for the year.

On VKontakte:

VKontakte maintains its local social networking leadership with an average Russian MAU of 72 million, and a DAU of 46.2 million.

Revenue grew 29% year-over-year to above 7 billion in the third quarter, driven by very active engagement with 9 billion newsfeed views, 15 billion messages delivered, and almost 1.2 billion videos views every day.

The Super App development continues with the number of VK Mini Apps rising by almost 70% year-over-year in September to just under 37,000, with a related MAU rising by 26% to 34 million in September and the most popular mini app having MAU in excess of 8 million. Monetization of the platform is also progressing with in-app ads revenue rising by 550% year-over-year in the third quarter, along with growing newsfeed based promotion revenues. Communication products and related technology enhancements continue, with the rollout of unlimited duration free of charge group video calls and video call MAU being around 20 million.

Overall, video remains a major focus area with several significant video platform updates in the third quarter, which help drive 5x year-over-year increase in VKontakte's revenues from video ads, to be further simulated by the rollout of VK Video, which happened in October unifying all the group's video resources in a platform with 40 million video daily active users, which is the largest in the Russian Internet market.

In order to provide further color on the latest development strategy and near-term plans of VKontakte, we plan to host a related teach-in event in November with details to follow.

Games:

MY.GAMES grew 2.3% to 10.1 billion roubles, and was around 33% of the Group's revenues in the third quarter. There were no major new launches to support growth during the first nine months of 2021 versus eight launches made during the same period last year.

Launch activity has been muted given the ongoing adjustment of our marking models and new rules around identification of users across iOS devices. And we expect a more normalized release schedule next year. Q3 EBITDA grew 22.6% to 2.4 billion roubles with a margin 24.2%, rising 4 percentage points versus the third quarter of 2020.

Mobile revenue share stood at 75% in the third quarter, with 77% of revenues coming from markets outside of Russia and the CIS. Average MAU stood at 21 million in the third quarter with a 4.3% share of monthly paying users. War Robots, Warface, Rush Royal, Hustle Castle, and Grand Hotel Mania were the largest revenue contributors for the quarter. We continue to diversify our portfolio through M&A, including 4 minority new studios at studio investments in the third quarter.

In September, we consolidated Mamboo Games, which develops and publishes hyper-casual and hybrid-causal titles, albeit it currently has marginal contribution to our financials given its startup nature. Today, a total of 14 internal studios of MY.GAMES have more than 20 titles in active development across PC, console and mobile platforms, with 5-8 games launches suitable for launch in the next 12 months.

Launches will resume only in 2022. Despite this, we expect revenue growth from MY.GAMES in 2021 versus the expected slight contraction for the broader games market in light of the base COVID effect. Sorry, to be clear, we do expect revenue growth from MY.GAMES. I'm sorry. I read that slightly wrong.

In the meantime, we expect MY.GAMES to deliver EBITDA margin of around 20% in 2021 versus 16% in 2020, with a peak margin in Q4, unlike last year, when active marketing resulted in the 13% margin in the fourth quarter.

Online education:

Online education grew by 56% year-over-year to 2.5 billion and accounted for 8% of the Group's revenues. Units launched more than 160 new courses and programs during the quarter, with most active additions in programming and gaming, design, marketing and management. And the overall number of courses now exceeds 1200. Active ongoing course offer expansion helps drive user growth with cumulative registered students approaching 2 million, up 1.5x year-over-year.

Nearly 37,000 of new paying students were added in the third quarter with their cumulative number approaching 273,000 more than doubling year-over-year. EdTech revenues are now expected to exceed 10 billion roubles in 2021. EBITDA margin improved quarter-over-quarter with a moderate loss of 0.3 billion roubles for the quarter. We target further improvements and profitability in the fourth quarter.

New initiatives:

New initiatives grew 68% to almost 3 billion, with most units demonstrating an improvement in economics and progress towards breakeven. With the level of EBITDA burn at 35% in Q3 versus 83% a year ago.

More specifically, **on Youla**. Youla accounts for more than a third of the segment's revenue. Its sales grew by almost 30% year-over-year in the third quarter to nearly one billion roubles, driven by the rising share of B2B sales. EBITDA losses as a proportion of revenue continued to decline in Q3. Overall, Youla remains on track to deliver 3.6 to 3.9 billion in revenues in 2021 with significant progress towards breakeven.

On VK Clips. We continue to be very encouraged by the ongoing progress of Clips with this video inventory exceeding 8 million from more than 2 million unique authors. 20 million people, which is twice the number a year ago, watched a total of 350 million Clips a day on average in September, with the number of users spending 10 plus minutes per day on Clips expanding by more than 70% year-over-year. There is already certain advertised based monetization in Clips with two main formats used: traditional video promos and special projects, albeit the main near-term focus remains on rising engagement and retention on the platform.

On recommendation platforms. Pulse MAU nearly doubled 70 million with recommendation platforms revenue approaching 0.3 billion in the third quarter, up more than 140% year-over-year. Recommendation systems also delivered a small positive EBITDA versus a loss during the prior year.

Margins and guidance:

Our group is in a very solid position, especially our largest local advertising revenue stream, where we continue to gain market share. We're also very confident about our global MY.GAMES business and its growth prospects. The 2021 presents us with a tough COVID related hurdle rate, which was further complicated by the IDFA related user identification changes.

We decided to take extra time to fully adjust our marketing models, to be able to achieve maximum ROI on our marketing spend in the new iOS reality. With marketing being the largest cost item for MY.GAMES, this and prudently shifting launches into next year. We also saw no major studio acquisitions year-to-date to support near-term growth. Given the scale of the MY.GAMES business, this results in a slight tweak to our full-year growth guidance to 124 to 127 billion in revenue for 2021, with part of MY.GAMES growth effectively shifting into next year.

On the margin side, all of our reporting segments showed quarter-over-quarter improvement and profitability in the third quarter. Margin of the core C&S segment rose by 3 percentage points to 49%, with My.Games profitability improvement by 4 percentage points to 24%. In the meantime, both New Initiatives and EdTech segments made progress towards breakeven. We aim to continue this trend in Q4 with slight year-over-year margin improvement targeted for the year for the group versus the 25.3% delivered 2020.

O2O and AliExpress Russia joint ventures are not part of the consolidated scope of the Group, but given their materiality, ongoing investment levels, and impact on our bottom line, we will also provide some highlights around both.

On O2O:

The GMV of the O2O JV grew by more than 55% year-over-year in the third quarter to nearly 48 billion with 70% of GMV coming from the foodtech assets. The assets remain in active investment phase with EBITDA burn of around 7.6 billion in the third quarter. At the same time, both mobility and foodtech segments of the JV showed sequential margin improvement, with overall O2O EBITDA margin improving to minus 16% as percent of GMV versus minus 20% in Q2 and minus 25% in Q3 2020.

On Delivery Club. Delivery Club grew gross revenues by 53% to 4 billion. Driven by 45% growth in orders to 22 million. With a 64% share in 1P and 17% share of e-grocery orders. This was driven by double-digit growth in active customers and order frequency. Delivery time also continues to improve, reaching 33 minutes on average in Moscow in September. Q3 marked the lowest level of burn at Delivery Club since formation of the O2O JV, at 8% of GMV, an improvement versus 11% in Q3 2020 and high teens prior to that.

Matthew Hammond:

On Samokat. Samokat has more than quadrupled both revenues and orders in Q3 with nearly 7 million in monthly orders in September, and more than 45 million in complete orders as of the nine months. We believe it is the fastest growing local e-grocery platform in Russia today. Its monthly audience exceeds one million, having more than doubled year-to-date. Samokat is present in 22 cities versus four cities in January. It plans to roll out operations in more cities with a plan to reach 1000 dark stores by the end of 2021 versus around 758 in September.

The regions are contributing a rising share of orders with 60% of orders from Moscow and Saint Petersburg in September versus almost 90% in January. Despite the active regional rollout, Samokat saw significant improvements of cash burn as a percentage of GMV in Q3, both on a

year-over-year and quarter-over-quarter basis, with the level of burn versus GMV at the lowest level since the formation of the O2O JV.

On Citymobil. Citymobil completed nearly 45 million rides and delivered almost 15 billion in GMV in the third quarter. With rides growing in the key regions, such as Moscow and Saint Petersburg. High margin B2B and premium segment rides were up more than 3x, and nearly 2x respectively. Increased focus on unit economics was often a 20% increase in contribution profit for passenger ride quarter-over-quarter, with Citymobil turning contribution positive across the platform in October.

We've provided nearly 38 billion in capital to the O2O JV since its inception, including 21.5 billion in 2021.

Finally, AER:

They recently published their own update in September about their performance, but a few highlights. AER is demonstrating solid trends, especially its local businesses with the local marketplace nearly tripling GMV on a year-over-year basis in September with ongoing acceleration. When it comes to CB [<IR comment: cross-border>](#), it remains the platform's major competitive edge versus other Russian e-commerce players given its more than 160 million SKUs and attractive profitability profile with potential for profitability already next year. In the meantime, it is already growing at a very healthy rate, including 25% year-over-year growth in September. Last 12 months, active buyers stood at almost 28 million as of September, with 114% growth of local buyers. We provided \$60 million in additional capital to AER in August as part of the funding round, which will be completed in November.

With that, I thank you. And we'll turn to Q&A. And we'll leave as much time as we possibly can.

Operator:

Thank you, sir. If you'd like to ask a question, please signal at this time by pressing star one on your telephone keypad. Please make sure that your mute function is turned off to allow your signal to reach our equipment. We also ask that you please limit yourselves to one question so that we may address as many questions as possible. You're of course, welcome to reenter the queue with star one. So, again, that's star one, if you'd like to ask a question. We'll take our first question from Ulyana Lenvalskaya with UBS.

Ulyana Lenvalskaya:

Hi, everyone. Thanks a lot for this opportunity. Let's maybe start with the key performances VKontakte. Could you please describe a bit the level of competition in social in Russia at the moment? So, I'm looking at the presentation, and see a decline in DAU for second quarter in a row. And also decline in MAU for Mini Apps also for third quarter in a row. So, could you please comment on what is driving this decline?

Boris Dobrodeev:

Ulyana, thank you very much. So, we see actually the both, the daily and the monthly audience continue to grow year-on-year. The growth is not that fast given the market is quite saturated. But we still have positive growth. And we still have very high user loyalty since our stickiness ratio, or the DAU-to- MAU, is about 64%.

Boris Dobrodeev:

So, if you look at the Mini App, so MAU was 28% year-on-year in June and similar to 26% in September. So, the DAU for Mini Apps also grew year-on-year. So, we also see the engagement in Mini Apps also arising same as monetization of this platform. At the same time, I mean, I'm

answering kind of the broader question. I think that the Mini Apps, it's still a fraction of the overall usage breakdown of VK. We see all the major lines of VK case studies doing well.

So, it's for competition. I think as we stated before, we think the only real status quo disturber, it is short video format, which is presented by TikTok. And this is what we're really focused on with Clips having 20 million daily active users. I think just recently we peaked with 400 million daily short video views, Clip video use. And we will continue to pursue the strategy.

We think that generally video and especially, the short video, it's the single biggest engagement driver. This is why we launched VK Video, our unified video, long-form video type of product. And as we said before, we have one of the largest video user base, 40 million people watching video. And we continue to grow [inaudible 00:27:38] we plan to launch standalone app as well as integrate into other third parties. Our ML team is doing some recommendations, which adds a lot to engagement. So, this is generally, how our picture from VK competition landscape looks like.

Operator:

All right, next one [crosstalk 00:28:12], Vladimir Bepalov with VTB Capital.

Vladimir Bepalov:

Hello. Thank you for taking my question. Can I ask you about the financing of your joint ventures? As Matthew mentioned, that this is going to be EBITDA breakeven in two, three years from now. But maybe could you give kind of a broad picture of how much you're going to invest, for example, next year in the joint venture? And apart from financing from the shareholders, do you consider any other options of tracking capital, or maybe borrowing for to finance these joint ventures? Thank you. And I will follow-up later. [crosstalk 00:28:54].

Boris Dobrodeev:

Thank you, Vladimir. I don't think we are now ready to disclose the exact figures for next year's budget. At the same time, probably we expect them as for the O2O JV. We expect them to be lower the budget this year. But of course, this is subject to our continued internal discussions. As of now, we are committed to [inaudible 00:29:31] O2O JV. We're very bullish on this. At the same time, we don't want to currently stress, rule out, or insist on any other external financing means. So, probably we will be analyzing all options. But again, as of now, we're fully committed to finance the JV. We're very bullish. And we're happy to continue to do that.

Operator:

And next we'll go to Cesar Tiron with Bank of America.

Cesar Tiron:

Yes. Hi, everyone. I have two questions, if that's okay. I'll ask the first one. It's on the games cluster. So, it looks like in the past two quarters growth has been very slow. And of course, we understand that the base effect. But I think the press release also mentions some games which were delayed in terms of launches. So, just if you can please explain, do you have the games ready and you haven't launched them? That would be one of the area of questions. And then I've also noticed that you made quite a high profile hire for the games' division. Should we conclude that there would be some kind of change in strategy for that division going forward? Thank you so much.

Boris Dobrodeev:

Thank you very much. So, I will first answer the first question. I think I would thank you very much, Cesar, for your question. So, I would address in a more kind of broad way. So, generally, I think

that gaming has a certain, of course, headwind this quarter, and generally, this year for a number of reasons.

First, we have tough year-on-year comparison. On another hand, we see the general gaming advertising market condition not favorable for a number of reasons. The first reason is that well, obviously, the auctions are quite overheated. We think that pricing is still quite high for the marketing. And as you know, we are very [inaudible 00:32:08] CAC/LTI driven.

So number two, of course, the IDFA changes were also affected the way we acquire marketing. I think our marketing team coped with the problem quite well. They put a lot of work and have a lot of technology to cope with that. But still, that also had an effect and contributed toward this. So, I think given that, we took a prudent decision not to pursue with a great marketing and especially, launch of new titles because we think now just the time for launching is not favorable.

So, this year for us, more like profitability versus growth. So, this is why we have quite a good pipeline with 20 games in development across our 14 studios, which will be ready for rollout. And we think that 5-8 titles will be issued in 12 months. So, again, it's mostly a prudent approach. So, that market has now adapted and is adapting to this new reality. I think if you, at least we've been looking at [inaudible 00:33:39], [<IR Comment: We analyzed gaming market performance in H1 2021. MY.GAMES performance was broadly in line \(slightly better\) with the market in H1 2021. So, we believe MY.GAMES is performing in line with the market \(or even better\) this year>](#). So, this is where, and what was the second question?

Cesar Tiron:

So, yeah. So, I just observed that you've made quite a high profile hire into that division. Does it change anything in the longer term in terms of strategy?

Boris Dobrodeev:

There is absolutely no changes in the strategy. I think we've been quite consistently executing our 360 degree strategy where we create a lot of gains and insight where we do a lot of M&A. We do venture investments. We also, license games. We also, of course, since we're already have 77% of our audience outside of Russia [<IR Comment: 77% of MY.GAMES revenue was generated outside Russia and CIS in Q3 2021>](#), we grow our international presence a lot. We have a strategy to create big franchise of shooters. So, I think generally, that there is no change in strategy. It's mostly execution of our strategy, which we talked about before. So, it is just another step in the strategy.

Cesar Tiron:

Thank you so much.

Boris Dobrodeev:

Thank you.

Operator:

All right. And once again, everyone that's star one, if you'd like to ask a question. We'll next go to Slava Degtyarev with Goldman Sachs.

Slava Degtyarev:

Yes. Thank you very much for the call. There was a solid improvement in Communication and Social margins in Q3. Can you help us decompose how much was coming from IVAS? And if there was an improvement in non-IVAs profitability? And would you expect Communication and

Social margins to be structurally high in the medium term compared to the levels that we have seen over the last couple of years? Thank you.

Boris Dobrodeev:

Well, look. I think everything's improved. It was a broad based improvement in both revenue and costs. As we said before, 2020 was real peak investment year for this segment and for lot of tech heavy and product heavy directions. Since we saw COVID and we saw a lot of new opportunities, we wanted to grasp including communications, video, which we just launched. So, I think this is kind of both the top and bottom line effect. So, we don't want to give forward-looking statement, but probably we will continue to see margin closer to current level, maybe slightly better going ahead.

<IR Comment: we can see Q4 margin in Communications and Social segment around Q3 level. But for the full 2021 level we stated previously that we expect to be around the 2020 level. See the management comment below. On previous calls we also said that the Communications and Social segment is currently seen delivering margins in the mid-40s in the mid-term>

Slava Degtyarev:

Thank you very much.

Boris Dobrodeev:

Thank you.

Operator:

And next we'll go to Luke Holbrook with Morgan Stanley.

Luke Holbrook:

Good afternoon, all. And I just had a question on Samokat. You're increasing quite aggressively the number of dark stores that you have. And now, you're entering into cities with less than 500,000 population. I mean, how do you see the unit economic working there to justify that investment compared to larger or denser cities? And have you closed any dark stores in the course of where economics just isn't working?

Boris Dobrodeev:

We actually think it's a very sound business from economic perspective. Most of the cities with 12 months maturity become contribution positive. So, we already have more than 20 cities indeed. And we continue to grow, and actually so far, what we see, we see really no big difference in economic level of this new cities that we open versus [inaudible 00:38:14]old. We prefer to continue to scale and maybe we'll continue to scale even more. So, we're focused not on closing, but on opening the dark stores. And I think that you can see [inaudible 00:38:34] transition of dark store openings into the growth of users and orders grew >4x year-on-year, just significantly. So, we plan to do so. Yes. And we seek growth across the board.

Operator:

Right next question will come from... I'm sorry. Go ahead, sir.

Luke Holbrook:

No. I was just going to quickly, if I could, just a follow-up just on the O2O on Citymobil. I think rides were down 10% year-on-year. Just any color on that? Didi entrants into more cities or driver shortages, any color there would be helpful.

Boris Dobrodeev:

Yes. I think that there is indeed, I think you're absolutely right. I think for some time, [crosstalk 00:39:28] Didi was scaling back some investment. But there was some time of quite strong push

from Didi. There also is very strong labor shortage that we see. I think we see it across all the segments. We see it in drivers. We see it also in courier. So, we see it in across the board.

And then the same time, the team is now much more focused on unit economics and on economics. So, currently, it has kind of more rationalization stage. So, in October it turned contribution positive in most of, a lot of key cities. So, this where the focus is now.

Operator:

All right. Your next question will come from the line of Anna Kupriyanova with Gazprombank.

Anna Kupriyanova:

Good afternoon. Thank very much for presentation. My question will be regarding of VKontakte and other possible integration with your JVs assets. Indeed great results of social communication growth, do you see any impact particular from e-commerce segment? Maybe some share of revenues coming from AliExpress, or maybe you can give us some understanding how positively your JV can impact your major segments? Thank you.

Boris Dobrodeev:

Thank you very much. So, I don't think that there is really material impact on our results. I think that we are contributing certain amount of GMV, I mean, if you're talking about VK, right? So, for VK, I think social commerce remain quite minor, insignificant revenue driver at this time. And we continue to [inaudible 00:41:53] focus on product. So, social commerce, it's not such a big contributor.

So, most of the money where we get from it is generally, commerce. It is financing fintech, and its education, which were especially strong this quarter. And the key success is attributed to I would say to big improvements in AdTech with such lines if advertiser, advertiser segment, and advertising products, such as performance, growing significantly more than the core revenue. Also, so in-stream video [inaudible 00:42:40] growing much better. And also, SMEs continue to track well. So, these were the key four points of growth. So, it's also I think it's a great concept <IR Comment: social commerce is a great concept>, but now it's more product than big revenue contribution for us.

<IR Comment: Social commerce accounted for 6% of AER GMV during its H1 FY2020 (April 2021-September 2021). But effect of social commerce on VK's social networks is insignificant so far>

Anna Kupriyanova:

Thank you very much. And maybe a quick follow-up. Do you see any changes in your online advertising, specifically following the recent lockdowns in Russia?

Boris Dobrodeev:

We haven't noticed it yet. So, I think it is yet to be seen. As you saw, we had quite a good quarter. And actually, very strong September and given that the lockdowns just started and it is just too early to judge.

Anna Kupriyanova:

Thank you.

Boris Dobrodeev:

Thank you.

Operator:

All right. Now, we'll go back to Vladimir Bespalov with VTB Bank.

Vladimir Bespalov:

Thank you for taking my follow-up question. So, I have a question on your guidance. You downgraded your revenue guidance for the full year. If we take it into account the upgrade of your guidance for revenue guidance for EdTech, so the net downgrade would be around four billion. So, is it right to understand that this is attributed to the game segment, and kind of the delay of the games and that kind of stuff?

Vladimir Bespalov:

And the second question here, maybe you could help me understand. If this is about cutting marketing spend on new games and that kind of stuff, and as you mentioned, the focus on profitability rather than growth, why that margin guidance hasn't changed with this change in the revenue guidance? Thank you.

Boris Dobrodeev:

So, it is mainly lack of new launches and lack of new aggressive marketing, which would have had significant impact on revenue. And that work with both into next year. I would say the majority of the, guidance decrease comes from this line.

Vladimir Bespalov:

Okay. But then on the profitability side, why the margin guidance remained unchanged? You're still guiding slightly higher than a year ago, as far as I understand, but on much lower [crosstalk 00:45:34]-

Boris Dobrodeev:

We didn't specify our guidance and we are indeed targeting an improvement, including driven by games with 20% margin for the year. And so, we saw significant increase in the gaming EBITDA year-on-year. So, I think it actually already reflects that in our metrics, if you look at them. And Matthew will follow-up on that.

Matthew Hammond:

Yeah. So, just a bit to comment that obviously, a large part of the margin driver is the revenue mix. And with advertising continuing to do well, that obviously, is supportive of the margin. But at the same time, the losses in the new initiatives continue to decline, as we were very clear. And so, you put all of that together, and hence, that is where we see the margin improvement coming through for the full year.

Vladimir Bespalov:

Okay. Thank you.

Operator:

Okay. Next question will come from the line of Anna Kurbatova with Alfa-Bank.

Anna Kurbatova:

Yes. Good afternoon. Two question from my side, please. First of all, still on the Communication and Social margins with the very good number of 49% this quarter. But I remember that you were in the first half of the year, navigating us that the new products and services that you introduce, like music, clips, et cetera, you are starting to monetize them with some lag, and that investments continue.

Anna Kurbatova:

So, still the question remains for me personally, the nature of this high margin in the third quarter and what should we expect going forward to in the fourth quarter let's say? And the second question, if any comments, or if you have own potential impact on your business, on your revenue margins from these IDFA changes? So, as far as I understand, the most change will come again on the game side. Yes, because the changes introduced on iOS platform. And so, as far as you have 70 or almost 80% of your games business coming from international markets developed, so it's mostly exposure for this segment. So, any comments on the potential impact would be very helpful. Thank you.

<IR Comment: Please note that VK Clips are booked within the New Initiatives since the beginning of 2021.>

Boris Dobrodeev:

So, I think in terms of the second question, we already see IDFA impact on our gaming revenue. As we said, we think it's not that simple. It's not just IDFA. But I think that it's a mix of IDFA and general marketing environment. And I think it's already kind of factored into our results and into our guidance. And we expect us to adapt and things to normalize next year. So, as for the advertisement segment, we also saw some effect on our performance in [inaudible 00:49:19]performance advertisement.

But again, it's already reflected in our results. But I think we managed to cope quite well because we as holding cover 90% of Russian Internet population. We also have our own tools such as VK ID, which actually help us to mitigate this risk a lot in online advertisement. And actually you saw that actually on opposite, we made progress in the performance of our ad business. And may I ask you to repeat the first question? So, I would answer it correctly.

Anna Kurbatova:

Yes. Surprisingly, good EBITDA margin in the Communications and Social segments. So, I remember that at the beginning of the year you were providing kind of the guidance that you introduce, you launch a lot of new services and functionalities on the platform. And that you start monetizing them very carefully. Yes. So, the effect on revenue comes with some lag, and while investments continue. So, for me, this margin came as a surprise. And I wonder what should we expect in the next quarter? And I really suspect some kind of maybe one-off in third quarter which drove such margin. Thank you.

Boris Dobrodeev:

No, I don't think there is any one-off . Probably we were a little bit conservative in our forecasting, on one hand. Again, and as I said before, it's a mix of couple of factors. You saw the advertising revenue growth was good. IVAS was good while it was declining in first half. And it's operating leverage in general, higher revenues and with a larger proportion of fixed costs. That's what gives you the margin and operating leverage.

I think this is the first quarter when we start to see it because again, we were quite open about it. A lot last year was an investment year for us where when we invested a lot into product, hired a lot of people, launched a lot of directions. And at least to date, this looks like it was the peak period. So, now, you have no use really, really. We do, of course, continue to develop a lot of products and invest. But there are no similar sizeable investments on Communications and Social. <IR Comment: Margin improvement of Communications and Social segment was driven by more moderate personnel expense growth, with also muted marketing expenses >

Tatiana Volochkovich:

Operator, did we lose Boris?

Operator:

Yes. It looks like Boris has disconnected.

Tatiana Volochkovich:

Yeah, let's continue for now. And he can comment when he's back.

Operator:

Okay. We'll move on to Dmitry Vlasov with Wood&Co.

Dmitry Vlasov:

Hi. Thank you for the opportunity to ask a question. I had one on games. And I one small follow-up on Communication and Social as well. So, the first one you mentioned that you had the marketing model adjustments and efficiency improvements in the game segment in '21. And I was just wondering if you're capable of sustaining so the 20% level of margin into '22? Assuming you will have five or eight launches. That's my first question.

And the second one, just to follow-up on Slava's question on margin. Boris mentioned that you would probably continue to see margins closer to current level going forward. And the current level is at third quarter 2021 or broadly 2021? Thank you.

Fedor Rubtsov:

Yeah, it's Fedor here. I think I can take this two. So, with respect to the Games margin. So, currently we are in the middle of the budgeting for the next year. So, we can't really give any specific comments on the '22 margin. And as you know, in general, the gaming margin is basically a function of the games mix and also of the timing of the new launches.

However, we would like to reiterate the guidance that we gave for the gaming margin when we promised to double it from the 2018 level in 2022. So, that promise still stands. So, I would say for now, you could probably target that level. As for the C&S margin, yes we actually meant that it'll probably for this year, it will not be worse than for the total of the last year, which hopefully, was a low point for the percentage margin of the Communications and Social segment.

And hopefully, it will increase going forward. But for that, we will need the investments that we have made into social to pay off. So, on the timing of that, I don't think we can give any more details. And yeah, I think to be more specific on the Games' margin for 2022, I think right now, we can safely assure that we will achieve the 10 billion roubles in EBITDA in 2022 for Games

Operator:

All right. And one moment, it looks like Boris' line is rejoining. We're just waiting for him to actually come back here. One second.

Tatiana Volochkovich:

Operator, we can continue for now.

Operator:

Okay. Well, let's go ahead and-

Boris Dobrodeev:

Sorry, I got cut off.

Operator:

All right. We'll move on to our next question will be from Anna Kupriyanova with Gazprombank again.

Anna Kupriyanova:

Thank you for the opportunity to ask a follow-up question, it will be on EdTech margins. You mentioned that you're seeing potential reaching breakeven on EBITDA. Can you please tell in more details about that?

Boris Dobrodeev:

Well, generally, you saw improvement in margin. You saw improvement in EBITDA margin as percent of burn. We see the current trend to continue for the Russian business. So, for Skillbox and GeekBrains. As we said before, the business is fundamentally unit economic positive. So, generally, all of its investments see positive ROI. The guys invest a lot in the courses and the products. Again, we see most of these investments bring a lot of multiples on investments.

So, we think that, yeah. We don't want be overly bullish. But again, first, as you remember, they already were profitable last year. And there were many periods when they were profitable. Just a testament to the profitability of the business model. So, this year, they were investing in growth. You see this investment, the rate, quarter-on-quarter. I think they have good chance of being positive either in Q4 or in Q1 next year.

Anna Kupriyanova:

Thank you very much.

Boris Dobrodeev:

Thank you.

Operator:

And next, we'll go to Sebastian Patulea with Jefferies.

Sebastian Patulea:

Hello, everyone. Thank you for the presentation. I've got a question on games, please. Given the Game segment has become quite sizeable, should we expect a big impact on growth when new mobile games are launched? And could you quantify the potential impact of mobile games you currently have in the pipeline? Thank you very much.

Boris Dobrodeev:

So, sorry. Could you please repeat the second part of the question? Quantify what parts of mobile games?

Sebastian Patulea:

Yeah. So, I was [crosstalk 00:58:53]... Sorry?

Boris Dobrodeev:

[crosstalk 00:58:57] you mentioned the part regarding the mobile? Repeat the part regarding the mobile games, please.

Sebastian Patulea:

Yes. I was saying that the mobile games segment has become quite sizeable. And I'm asking if a single mobile launch would actually have a big impact on growth? And the second part of the question was you clearly have a pipeline of mobile games that you are you're planning to launch.

And if in any way you can give us some sort of hint on their size and how this could impact the growth of the segment?

Boris Dobrodeev:

Well, obviously, games are a huge part of our revenue. It's the second, well it competes with advertising to become the first single largest revenue component. So, of course, new gaming launches, they can have a huge impact on our revenue. So, and of course, mobile is a very, very big driver of our gaming revenue. So, 75% of our gaming revenue is now mobile. So, of course, if we execute well on our gaming strategy next year, that can give quite significant uptick in not just gaming revenue, but in the group revenue. So, it concerns both. I wouldn't single out mobile or PC title. It can happen with any title.

So, we have titles like War Robots, which generate more than 100, maybe, I don't know, but with current ruble/dollar rate, 130 probably million dollars. So, yes. One, two, gaming, successful gaming launches can significantly improve the growth profile. And then again, as per your second question, mobile is a huge proportion of our current revenue. But we're still bullish on all the segments. So, what we try to do is we still have kind of certain proportion of launches on desktop and on console. And we also try to launch as many franchises as possible. So, generally, we have a successful title on one platform. We'd probably try to port it to another platform as well.

Sebastian Patulea:

Thank you very much.

Boris Dobrodeev:

Thank you.

Operator:

All right. Looks like we have one more question in the queue. We'll take that from Vladimir Beshpalov with VTB Capital.

Vladimir Beshpalov:

Thank you for taking one more question from me. So, I have kind of technical. First, on capex. I see a significant increase in capex in nine months of this year versus last year. Maybe could you comment what is behind? What should we expect for the full year? And the other also technical, is on that. So, what is the ceiling for you in terms of leveraging the company, as you have borrowed quite a lot? Where would you stop, I would say? Thank you.

Fedor Rubtsov:

Yeah. Well, thank you for the questions. Fedor here. I think I can take both. So, on capex, basically we have always guided to kind of a long-term, 10% revenue benchmark. But we have all this that actually can fluctuate in any specific year or quarter. So, this year it'll probably be higher than that mostly driven by some content investments and also by a new data center construction.

But longer term, we don't see the current level of capex as a percentage of revenue as kind of sustainable. We think that the longer term target of 10% of revenue still stands. However it can actually fluctuate up or down in any given specific year. With respect to the debt, we are currently pretty comfortable with the current leverage levels. And we are pretty safe in terms of our debt covenants, our financial covenants with respect that to be the levels.

We will say that we will probably not be comfortable with debt to EBITDA staying at about 2x for a prolonged period of time even though it can potentially go above 2x for a short period of time. So, that I think is our longer term thinking about leverage.

Sebastian Patulea:

Thank you very much.

Operator:

All right. And next, we'll go to Anna Kurbatova with Alfa-Bank.

Anna Kurbatova:

Yes. Thank you very much for taking my follow-up. Could you give some more color on your remark in the press release with regards to the prospects of payment and fintech JVs, so you reassessed the probability in current structure? So, please give us some more color on what's going on with those JVs. Thank you.

Vladimir Gabrielyan:

Hello, Anna this Vladimir Gabrielyan speaking. Yeah. As we had a long stop date in our documents, and now it's passed. So, we don't consider the deal as highly probable. But anyway, we're still looking for opportunities on this topic.

Anna Kurbatova:

Okay. So, does it mean so that you break your plans with your partners like MegaFon, Alibaba lag, Ant Group, you will be looking for new partners? Or, it's just about changing the deal, potential deal terms with the same partners?

Boris Dobrodeev:

We cannot at this stage disclose the exact mechanics. But it's inching towards the second deal, second part of deal. So, now, we're approaching a technical deadline. So, with no conclusion yet. At the same time, we will continue to explore this opportunity with at least most of the current partners of the deal.

Anna Kurbatova:

Thank you very much.

Boris Dobrodeev:

Thank you.

Operator:

Okay. It looks like we have no further questions at this time. So, I'd like to turn it back to our speakers for any additional or closing remarks.

Tatiana Volochkovich:

Thank you everyone for joining us today for this results call. If we didn't cover all of your questions, or you have other follow-ups, feel free to contact us at IR team. Again, thank you much. And have a great rest of the day. Goodbye.