Mail.Ru Group Limited

Interim Condensed
Consolidated Financial Statements

For the six months ended June 30, 2014

Contents

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улучшаем мир

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Report on Review of Interim Condensed Consolidated Financial Statements

To the Shareholders of Mail.Ru Group Limited

Introduction

We have reviewed the accompanying interim condensed consolidated financial statements of Mail.Ru Group Limited and its subsidiaries (“the Group”) as at June 30, 2014 which comprise the interim consolidated statement of financial position as at June 30, 2014 and the related interim consolidated statements of comprehensive income, changes in equity and cash flows for the six-month period then ended and explanatory notes. Management is responsible for the preparation and presentation of these interim condensed consolidated financial statements in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting* (“IAS 34”). Our responsibility is to express a conclusion on these interim condensed consolidated financial statements based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34.

Ernst & Young LLC

August 21, 2014

Interim Consolidated Statement of Financial Position

As of June 30, 2014
(in millions of Russian Roubles)

	Notes	As at June 30, 2014 (unaudited)	As at December 31, 2013
ASSETS			
Non-current assets			
Investments in strategic associates	5	20,842	8,289
Goodwill		32,969	32,969
Other intangible assets	6	9,469	10,056
Property and equipment	7	2,388	2,518
Financial assets at fair value through profit or loss	15	1,390	1,330
Deferred income tax assets		496	263
Other non-current assets	8	896	924
Total non-current assets		68,450	56,349
Current assets			
Trade accounts receivable	15	2,401	2,957
Prepaid income tax		738	68
Prepaid expenses and advances to suppliers		780	751
Financial assets at fair value through profit or loss	15	14	66
Other current assets	9	424	404
Short-term time deposits	15	129	315
Cash and cash equivalents	15	26,202	30,987
Total current assets		30,688	35,548
Total assets		99,138	91,897
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Issued capital		–	–
Share premium		46,296	46,283
Treasury shares		(1,308)	(472)
Retained earnings		43,793	35,312
Accumulated other comprehensive income		95	65
Total equity attributable to equity holders of the parent		88,876	81,188
Non-controlling interests		4	6
Total equity		88,880	81,194
Non-current liabilities			
Deferred income tax liabilities		2,598	2,408
Deferred revenue		541	386
Other non-current liabilities		52	–
Total non-current liabilities		3,191	2,794
Current liabilities			
Trade accounts payable	15	1,157	1,292
Income tax payable		66	363
VAT and other taxes payable		1,111	1,368
Deferred revenue and customer advances		2,764	2,615
Other payables, provisions and accrued expenses	10	1,969	2,271
Total current liabilities		7,067	7,909
Total liabilities		10,258	10,703
Total equity and liabilities		99,138	91,897

Interim Consolidated Statement of Comprehensive Income

For the six months ended June 30, 2014
(in millions of Russian Roubles)

	Notes	Six months ended June 30, 2014 (unaudited)	Six months ended June 30, 2013 (unaudited)
Online advertising		4,741	4,063
MMO games		3,801	3,065
Community IVAS		4,988	4,015
Other revenue	11	1,568	1,325
Total revenue		15,098	12,468
Net gain on venture capital investments and associated derivative financial assets and liabilities	15	11	211
Personnel expenses		(3,057)	(3,411)
Office rent and maintenance		(807)	(507)
Agent/partner fees		(1,976)	(1,309)
Marketing expenses		(413)	(330)
Server hosting expenses		(492)	(414)
Professional services		(166)	(104)
Other operating expenses		(323)	(380)
Total operating expenses		(7,234)	(6,455)
EBITDA	4	7,875	6,224
Depreciation and amortisation		(1,416)	(1,348)
Impairment of intangible assets		(352)	(3)
Share of profit of strategic associates		159	144
Finance income		279	162
Other non-operating income/(expense)		22	(17)
Net gain on financial assets and liabilities at fair value through profit or loss over the equity of strategic associates, subsidiaries and other agreements	15	195	14
Net gain on disposal of shares in strategic associates	5	2,673	1,286
Net foreign exchange gains		934	72
Profit before income tax expense		10,369	6,534
Income tax expense	12	(1,870)	(1,802)
Net profit		8,499	4,732
Attributable to:			
Equity holders of the parent		8,481	4,719
Non-controlling interest		18	13
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Exchange differences on translation of foreign operations:			
Differences arising during the period		24	(11)
Available-for-sale financial assets:			
Gains arising during the period		–	1,403
Income tax effect		–	–
Total other comprehensive income net of tax effect of 0		24	1,392
Total comprehensive income, net of tax		8,523	6,124
Attributable to:			
Equity holders of the parent		8,512	6,111
Non-controlling interest		11	13
Earnings per share, in RUR:			
Basic earnings attributable to ordinary equity holders of the parent		40.7	22.6
Diluted earnings attributable to ordinary equity holders of the parent		39.1	22.0

Interim Consolidated Statement of Cash Flows

For the six months ended June 30, 2014
(in millions of Russian Roubles)

	Notes	Six months ended June 30, 2014 (unaudited)	Six months ended June 30, 2013 (unaudited)
Cash flows from operating activities			
Profit before income tax		10,369	6,534
Adjustments for:			
Depreciation and amortisation		1,416	1,348
Bad debt expense		40	84
Net gain on financial assets and liabilities at fair value through profit or loss over the equity of strategic associates, subsidiaries and other agreements	15	(195)	(14)
Net gain on disposal of shares in strategic associates	5	(2,673)	(1,286)
Loss on disposal of property and equipment and intangible assets		6	16
Finance income		(279)	(162)
Dividend revenue from venture capital investments	11	(72)	(6)
Share of profit of strategic associates	5	(159)	(144)
Impairment of intangible assets	6	352	3
Net foreign exchange gains		(934)	(72)
Share based payment expense		89	709
Other non-cash items		6	9
Decrease in accounts receivable		528	100
(Increase)/Decrease in prepaid expenses and advances to suppliers		(92)	51
Increase in other assets		(39)	(74)
Decrease in accounts payable, provisions and accrued expenses		(426)	(278)
Decrease/(Increase) in other non-current assets		97	(156)
Increase in deferred revenue and customers advances		302	62
Decrease/(Increase) in financial assets at fair value through profit or loss	15	(14)	26
Operating cash flows before interest and income taxes		8,322	6,750
Dividends received from financial investments		90	6
Interest received		335	191
Income tax paid		(2,884)	(2,041)
Net cash provided by operating activities		5,863	4,906
Cash flows from investing activities			
Cash paid for investments in strategic associates	5	(12,430)	–
Cash paid for property and equipment		(295)	(789)
Cash paid for intangible assets		(745)	(539)
Dividends received from strategic associates	5	141	134
Proceeds from disposal of shares in strategic associates	5	2,944	1,644
Issuance of loans		(65)	(12)
Collection of short-term and long term deposits		315	829
Acquisition of short-term and long term deposits		(131)	(210)
Net cash (used in) / provided by investing activities		(10,266)	1,057
Cash flows from financing activities			
Cash paid for non-controlling interests in subsidiaries		(7)	–
Proceeds from issuance of common stock, net of share issuance costs paid		–	4
Cash paid for treasury shares		(1,337)	(99)
Dividends paid to shareholders		–	(27,660)
Dividends paid by subsidiaries to non-controlling shareholders		(21)	(14)
Net cash used in financing activities		(1,365)	(27,769)
Net decrease in cash and cash equivalents		(5,768)	(21,806)
Effect of exchange differences on cash balances		983	475
Cash and cash equivalents at the beginning of the period		30,987	27,690
Cash and cash equivalents at the end of the period		26,202	6,359

Interim Consolidated Statement of Changes in Equity

For the six months ended June 30, 2013
(in millions of Russian Roubles)

	Share capital Number of shares issued and outstanding	Amount	Share premium	Treasury shares	Retained earnings	Accumulated other comprehensive income (net of tax effect of 0)	Total equity attributable to equity holders of the parent	Non-controlling interests	Total equity
Balance at January 1, 2013	208,488,527	–	46,216	(611)	35,993	8,513	90,111	4	90,115
Profit for the period	–	–	–	–	4,719	–	4,719	13	4,732
Other comprehensive income									
Foreign currency translation	–	–	–	–	–	(11)	(11)	–	(11)
Net change in cumulative holding gains on available-for-sale investments	–	–	–	–	–	1,403	1,403	–	1,403
Total other comprehensive income	–	–	–	–	–	*1,392*	*1,392*	–	*1,392*
Total comprehensive income	–	–	–	–	4,719	1,392	6,111	13	6,124
Share-based payment transactions	–	–	751	–	–	–	751	–	751
Exercise of options over the shares of the Company	244,383	–	(270)	242	–	–	(28)	–	(28)
Acquisition of treasury shares	(139,261)	–	–	(123)	–	–	(123)	–	(123)
Share-based payment transactions by strategic associates	–	–	26	–	–	–	26	–	26
Share-based payment modification	–	–	(399)	–	–	–	(399)	–	(399)
Dividends by subsidiaries to non-controlling shareholders	–	–	–	–	–	–	–	(14)	(14)
Dividends to shareholders	–	–	–	–	(27,244)	–	(27,244)	–	(27,244)
Other changes in share premium	–	–	(1)	–	–	1	–	–	–
Balance at June 30, 2013	208,593,649	–	46,323	(492)	13,468	9,906	69,205	3	69,208

Interim Consolidated Statement of Changes in Equity (continued)

For the six months ended June 30, 2014
(in millions of Russian Roubles)

	Share capital Number of shares issued and outstanding	Amount	Share premium	Treasury shares	Retained earnings	Accumulated other comprehensive income (net of tax effect of 0)	Total equity attributable to equity holders of the parent	Non-controlling interests	Total equity
Balance at January 1, 2014	208,710,192	–	46,283	(472)	35,312	65	81,188	6	81,194
Profit for the period	–	–	–	–	8,481	–	8,481	18	8,499
Other comprehensive income									
Foreign currency translation	–	–	–	–	–	32	32	(7)	25
Total other comprehensive income	*–*	*–*	*–*	*–*	*–*	*32*	*32*	*(7)*	*25*
Total comprehensive income	–	–	–	–	8,481	32	8,513	11	8,524
Share-based payment transactions	–	–	349	–	–	–	349	–	349
Exercise of options over the shares of the Company	416,464	–	(499)	501	–	–	2	–	2
Acquisition of treasury shares	(1,012,885)	–	–	(1,337)	–	–	(1,337)	–	(1,337)
Acquisitions of non-controlling interests in existing subsidiaries	–	–	(14)	–	–	–	(14)	8	(6)
Share-based payment transactions by strategic associates	–	–	23	–	–	–	23	–	23
Dividends by subsidiaries to non-controlling shareholders	–	–	–	–	–	–	–	(21)	(21)
Issuance of shares and other changes in net assets of strategic associates	–	–	154	–	–	(2)	152	–	152
Balance at June 30, 2014	208,113,771	–	46,296	(1,308)	43,793	95	88,876	4	88,880

Notes to the Interim Condensed Consolidated Financial Statements

1 Corporate information and description of business

These interim condensed consolidated financial statements of Mail.Ru Group Limited (hereinafter “the Company”) and its subsidiaries (collectively – “the Group”) for the six months ended June 30, 2014 were authorised for issue by the directors of the Company on August 21, 2014.

The Company was registered on May 4, 2005 in the Territory of the British Virgin Islands (“BVI”), pursuant to the International Business Companies Act (the “Act”), Cap. 291. The registered office of the Company is at Trident Chambers, Wickhams Cay, P.O. Box 146, Road Town, Tortola, BVI.

The Company consolidates or participates in businesses that operate in the Internet segment, including portals, social networking and communications, e-payment solutions, online marketplaces, massively multiplayer online games (“MMO games”), social and mobile games. The Group and its associates have leading positions in the CIS states where they are present, including Russia, Ukraine and Kazakhstan.

2 Basis of preparation

The interim condensed consolidated financial statements for the six months ended June 30, 2014 have been prepared in accordance with IAS 34.

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group’s annual financial statements as at December 31, 2013 prepared in accordance with IFRS.

2.1 Application of new and amended IFRS and IFRIC

The accounting policies adopted are consistent with those followed in the preparation of the Group’s annual financial statements for the year ended December 31, 2013, except for the adoption of new standards as of January 1, 2014 listed below:

Recoverable Amount Disclosures for Non-Financial Assets – Amendments to IAS 36
These amendments remove the unintended consequences of IFRS 13 *Fair Value Measurement* on the disclosures required under IAS 36 Impairment of Assets. In addition, these amendments require disclosure of the recoverable amounts for the assets or cash-generating units (CGUs) for which an impairment loss has been recognised or reversed during the period. These amendments did not have a material impact on the Group’s consolidated financial statements, however they resulted in additional disclosures.

IAS 32 Offsetting Financial Assets and Financial Liabilities
These amendments clarify the meaning of “currently has a legally enforceable right to set-off” and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting. These amendments have no impact on the Group.

IAS 39 Novation of Derivatives and Continuation of Hedge Accounting
These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. These amendments have no impact on the Group as the Group does not have any derivatives designated as hedging instruments.

IFRIC 21 Levies
IFRIC 21 clarifies that an entity recognises a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. These amendments have no impact on the Group.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27)
These amendments provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under IFRS 10 *Consolidated Financial Statements*. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. These amendments have no impact to the Group, since the Company does not qualify to be an investment entity under IFRS 10.

Reclassifications
Certain corresponding information presented in the interim condensed consolidated financial statements for the period ended December 31, 2013 has been reclassified in order to achieve comparability with the presentation used in these interim condensed consolidated financial statements.

2.2 Change of statements of comprehensive income presentation

The Group has changed the presentation of the consolidated statement of comprehensive income by grouping together revenue from context and media advertising because, in management’s view, such presentation provides more relevant information to the users of the financial statements. The prior period presentation was adjusted to conform to current year presentation. The change did not materially affect the presentation of the financial statements.

Notes to the Interim Condensed Consolidated Financial Statements (continued)

3 Seasonality of operations

Due to the seasonal nature of the advertising and online games, higher revenues and operating profits are usually expected in the second half of the year than in the first six months. Higher sales during the second half of the year are mainly attributed to the increased demand for online games due to the end of the vacation period and to the fact that a large portion of advertising budgets is spent in the last quarter of the year.

4 Operating segments

In reviewing the operational performance of the Group and allocating resources, the Chief Executive Officer of the Group, who is the Group's Chief Operating Decision Maker (CODM), reviews selected items of each segment's income statement, assuming 100% ownership in all of the Group's key operating subsidiaries, based on management reporting.

Management reporting is different from IFRS, because it does not include certain IFRS adjustments which are not analysed by the CODM in assessing the core operating performance of the business. Such adjustments affect such major areas as revenue recognition, deferred tax on unremitted earnings of subsidiaries, share-based payments, disposals or impairment of investments, business combinations, fair value adjustments, amortisation and impairment thereof, net foreign exchange gains and losses, share in financial results of non-core associates, as well as irregular non-recurring items that occur from time to time and are evaluated for adjustment as and when they occur. The tax effect of these adjustments is also excluded from management reporting.

The financial information of the key subsidiaries acquired during the reporting period or after the reporting period but prior to the date of these consolidated financial statements is included into the segment disclosure starting from the later of:

- the beginning of the earliest comparative period included in the financial statements; and
- the date of the Group's acquisition of its first interest in the respective key subsidiary.

The financial information of subsidiaries disposed of prior to the date of these consolidated financial statements is excluded from the segment presentation starting from the beginning of the earliest period presented.

The Group has identified its operating segments based on the types of products and services the Group offers. The Group has identified the following reportable segments on this basis:

- Email, Portal and IM;
- Social Networks;
- Online Games; and
- E-Commerce, Search and Other Services.

The Email, Portal and IM segment includes email, instant messaging and portal (main page and verticals). It earns substantially all revenues from display and context advertising.

The Social Networks segment includes the Group's two social networks (Odnoklassniki and My World) and earns revenues from (i) user payments for virtual gifts, (ii) commission from application developers based on the respective applications' revenue, and (iii) online advertising, including display and context advertising.

The Online Games segment includes online gaming services, including MMO, social and mobile games. It earns substantially all revenues from (i) sale of virtual in-game items to users and (ii) royalties for games licensed to third-party online game operators.

The E-Commerce, Search and Other Services segment primarily consists of search engine services earning substantially all revenues from context advertising, E-commerce and online hiring / job search services and related display advertising. This segment also includes a variety of other services, which are considered insignificant by the CODM for the purposes of performance review and resource allocation.

The Group measures the performance of its operating segments through a measure of earnings before interest, tax, depreciation and amortisation (EBITDA). Segment EBITDA is calculated as the respective segment's revenue less operating expenses (excluding depreciation and amortisation and impairment of intangible assets), including Group corporate expenses allocated to the respective segment.

EBITDA is not a measure of financial performance under IFRS. The calculation of EBITDA by the Group may be different from the calculations of similarly labeled measures used by other companies and it should therefore not be used to compare one company against another or as a substitute for analysis of the Group's operating results as reported under IFRS. EBITDA is not a direct measure of the Group's liquidity, nor is it an alternative to cash flows from operating activities as a measure of liquidity, and it needs to be considered in the context of the Group's financial commitments. EBITDA may not be indicative of the Group's historical operating results, nor is it meant to be predictive of the Group's potential future results. The Group believes that EBITDA provides useful information to the users of the consolidated financial statements because it is an indicator of the strength and performance of the Group's ongoing business operations, including the Group's ability to fund discretionary spending such as capital expenditure, acquisitions and other investments and the Group's ability to incur and service debt.

Notes to the Interim Condensed Consolidated Financial Statements (continued)

4 Operating segments (continued)

The Group's share of profits of strategic associates is not attributed to any operating segment and not included in the calculation of EBITDA. The Group's share of profits of key strategic associates (Qiwi plc and VK.Com Limited) is included in Net profit reviewed by the CODM and is based on the ownership percentages as of the date of the financial statements (see also Note 5). The net profit of key strategic associates is calculated using accounting principles used for the segment financial information of the Group's consolidated operations. The Group's share of profits of non-core strategic associates (Nikita Management Limited, Molotok Holdings Limited and Haslop Company Limited) is not included in the financial information reviewed by the CODM.

The information about the breakdown of revenue from external customers by the customers' country of domicile and non-current assets by country is not available to the management of the Group, and it considers that the cost to develop such information would be excessive.
The income statement items for each segment for the six months ended June 30, 2014, as presented to the CODM, are presented below:

	Email, portal and IM	Social networks	Online games	E-commerce, search and other	Eliminations	Group
Revenue						
External revenue	2,160	5,872	4,315	2,796	–	15,143
Intersegment revenue	15	15	–	167	(197)	–
Total revenue	2,175	5,887	4,315	2,963	(197)	15,143
Total operating expenses	1,110	1,711	2,676	1,796	(197)	7,096
EBITDA	1,065	4,176	1,639	1,167	–	8,047
Net profit						6,276

The income statement items for each segment for the six months ended June 30, 2013, as presented to the CODM, are presented below:

	Email, portal and IM	Social networks	Online games	E-commerce, search and other	Eliminations	Group
Revenue						
External revenue	2,048	4,628	3,349	2,417	–	12,442
Intersegment revenue	14	15	–	149	(178)	–
Total revenue	2,062	4,643	3,349	2,566	(178)	12,442
Total operating expenses	954	1,245	2,146	1,569	(178)	5,736
EBITDA	1,108	3,398	1,203	997	–	6,706
Net profit						4,973

A reconciliation of total revenue, as presented to the CODM, to IFRS consolidated revenue of the Group for the six months ended June 30, 2014 and 2013 is presented below:

	2014	2013
Total revenue, as presented to the CODM	15,143	12,442
Adjustments to reconcile revenue as presented to the CODM to consolidated revenue under IFRS:		
Differences in timing of revenue recognition	(154)	(19)
Barter revenue	37	39
Dividend revenue from venture capital investments	72	6
Consolidated revenue under IFRS	15,098	12,468

Notes to the Interim Condensed Consolidated Financial Statements (continued)

4 Operating segments (continued)

A reconciliation of EBITDA, as presented to the CODM, to IFRS consolidated profit before income tax expense of the Group for the six months ended June 30, 2014 and 2013 is presented below:

	2014	2013
Group aggregate segment EBITDA, as presented to the CODM	8,047	6,706
Adjustments to reconcile EBITDA as presented to the CODM to consolidated profit before income tax expenses under IFRS:		
Differences in timing of revenue recognition	(154)	(19)
Net gain on venture capital investments and associated derivative financial assets and liabilities	11	211
Share-based payments expenses	(89)	(709)
Dividend revenue from venture capital investments	72	6
Other	(12)	29
EBITDA	7,875	6,224
Depreciation and amortisation	(1,416)	(1,348)
Impairment of intangible assets	(352)	(3)
Share of profit of strategic associates	159	144
Finance income	279	162
Other non-operating income/(expense)	22	(17)
Net gain on financial assets and liabilities at fair value through profit or loss over the equity of strategic associates, subsidiaries and other agreements	195	14
Net gain on disposal of shares in strategic associates	2,673	1,286
Net foreign exchange gains	934	72
Profit before income tax expense	10,369	6,534

A reconciliation of net profit, as presented to the CODM, to IFRS consolidated net profit of the Group for the six months ended June 30, 2014 and 2013 is presented below:

	2014	2013
Total net profit, as presented to the CODM	6,276	4,973
Adjustments to reconcile net profit as presented to the CODM to consolidated net profit under IFRS:		
Share-based payments expenses	(89)	(709)
Differences in timing of revenue recognition	(154)	(19)
Effect of operations disposed of, difference in shareholding percentages and acquisition dates of subsidiaries and associates	(3)	128
Amortisation of fair value adjustments to intangible assets and impairment thereof	(1,198)	(831)
Gain on financial instruments at fair value through profit or loss	206	225
Net gain on disposal of shares in strategic associates	2,673	1,286
Net foreign exchange gains	934	72
Share in financial results of non-core associates	24	(9)
Other	2	(12)
Tax effect of the adjustments and tax on unremitted earnings	(172)	(372)
Consolidated net profit under IFRS	8,499	4,732

5 Investments in strategic associates

In April 2014 the Group acquired 12.00% of economic interest in strategic associate VK.Com Limited (“VK”) for an aggregate consideration including RUR 12,430 in cash and a written call option to acquire 100% of Headhunter. As a result of the acquisition the Group increased its economic interest in VK to 51.99%, but did not acquire control over VK and the Group continued to account for the investment using the equity method. The Group allocated RUR 9,908 to goodwill as part of the equity method investment, RUR 3,159 to intangible assets as part of the equity method investment and RUR 437 to the acquired share in net liabilities of VK. The intangible assets mainly represent VK’s trademark and customer base and are to be amortised over the useful life of 10 years.

In June 2014 the Company sold 4.50% (2013: 6.31%) of economic interest in strategic associate Qiwi plc (“Qiwi”) during Qiwi’s secondary public offering (“SPO”) for an aggregate net cash consideration of RUR 2,942 (2013: 1,644). As a result of the disposal the Company recognised a gain in the amount of RUR 2,673 under “Net gain on disposal of shares in strategic associates“ in the interim consolidated statement of comprehensive income (2013: 1,286). After partial disposal of the investment the Company retained a 5.92% economic interest and power to participate in the financial and operating policy decisions through its representation on Qiwi’s Board of Directors. Accordingly the Company retained significant influence over Qiwi and continued to account for the remaining investment using the equity method.

Notes to the Interim Condensed Consolidated Financial Statements (continued)

5 Investments in strategic associates (continued)

Movement in investments in strategic associates for the 6 months ended June 30, 2014 is presented below:

Investments in strategic associates at January 1	8,289
Acquisition of shares in associates	12,629
Disposals of shares in associates	(271)
Share in net profits of associates	159
Share in equity-settled share-based payments of associates	23
Dividends from associates	(141)
Issuance of shares and other changes in net assets of strategic associates	154
Investments in strategic associates at June 30	20,842

Although certain indicators of impairment were identified for some of the Group's associates as of June 30, 2014, the recoverable amount of the investments based on value in use was higher than the respective carrying values and accordingly, no impairment was recorded in the first half of 2014.

6 Intangible assets

During the six months ended June 30, 2014, the Group capitalised software development costs and otherwise acquired intangible assets with a cost of RUR 764 (2013: RUR 588). The Group did not acquire any intangible assets or goodwill through business combinations in the six months ended June 30, 2014 or in the six months ended June 30, 2013.

In the six months ended June 30, 2014, the Group recognised RUR 352 (2013: RUR 3) of impairment losses with respect to online game software with recoverable amount calculated as value in use based on discount rate 16.7% in the amount of RUR 737. The impairment entirely belongs to the Online Games operating segment and is explained by underperformance of related games.

7 Property and equipment

During the six months ended June 30, 2014, the Group acquired property and equipment with a cost of RUR 292 (2013: RUR 799).

8 Other non-current assets

Other non-current assets consist of the following:

	June 30, 2014	December 31, 2013
Advance under office lease contract	813	910
Other non-current assets	83	14
Total other non-current assets	896	924

9 Other current assets

Other current assets consist of the following:

	June 30, 2014	December 31, 2013
Inventory	33	35
VAT receivable	267	225
Interest receivable	6	62
Loans receivable	70	17
Other current assets	48	65
Total other current assets	424	404

Notes to the Interim Condensed Consolidated Financial Statements (continued)

10 Other payables, provisions and accrued expenses

Other payables, provisions and accrued expenses consist of the following:

	June 30, 2014	December 31, 2013
Payables to personnel	1,107	1,470
Accrued vacations	511	437
Accrued professional consulting expenses	69	54
Advance received under fit-out contract	70	72
Other current payables and provisions	212	238
Total other payables, provisions and accrued expenses	1,969	2,271

11 Other revenue

Other revenue consists of the following:

	Six months ended June 30	
	2014	2013
Online recruitment services	1,376	1,160
Listing fees	45	59
Dividend revenue from venture capital investments	72	6
Other	75	100
Total other revenue	1,568	1,325

12 Income tax

The major components of income tax expense in the interim consolidated statement of comprehensive income are as follows:

	Six months ended June 30	
	2014	2013
Current income tax expense	1,915	1,837
Deferred income tax expense/(benefit)	(45)	(35)
Total income tax expense	1,870	1,802

The reconciliation between income tax expense and the product of accounting profit multiplied by BVI’s domestic tax rate for the six months ended June 30, 2014 and 2013 is as follows:

	Six months ended June 30	
	2014	2013
Profit before income tax expense	10,369	6,534
BVI statutory income tax rate at 0%	–	–
Foreign tax rate differential	(1,412)	(1,380)
Tax on dividends	(39)	(45)
Other	(21)	–
Adjustments in respect of current income tax of previous year	(14)	(2)
Tax on unremitted earnings	(381)	(291)
Utilization of previously unrecognized tax loss	38	–
Non-deductible expenses	(41)	(84)
Total income tax expense	(1,870)	(1,802)

Notes to the Interim Condensed Consolidated Financial Statements (continued)

13 Commitments, contingencies and operating risks

13.1 Operating environment of the Group

The Company is registered in BVI, but most of the Group's operations are in Russia. Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. The global financial crisis has resulted in uncertainty regarding further economic growth, availability of financing and cost of capital, which could negatively affect the Group's future financial position, results of operations and business prospects. Management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances.

Recently, the United States, the European Union and certain other countries have ordered sanctions against certain prominent Russian and Ukrainian officials and businessmen and Russian private banks and companies in response to the situation in Ukraine and Russia's signing of an agreement with the Republic of Crimea on the accession of the Republic of Crimea and the city of Sevastopol to the Russian Federation and on forming two new constituent entities within the Russian Federation. While the current sanctions do not target the Group or the Group's industry, these sanctions could have the indirect effect of damaging the Russian economy, further accelerating capital flight from Russia, exacerbating the negative investor sentiment towards Russia and making it harder for Russian companies to access international financial markets for debt and equity financing, all of which could have a material adverse effect on the Group's business, financial conditions, results of operations and prospects and the value of the Company's GDRs.

13.2 Taxation

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

The Group's management believes that its interpretation of the relevant legislation is appropriate and is in accordance with the current industry practice and that the Group's tax, currency and customs positions will be sustained. However, the interpretations of the relevant authorities could differ and the effect of additional taxes, fines and penalties on these consolidated financial statements, if the authorities were successful in enforcing their different interpretations, could be significant.

13.3 Legal proceedings

The Group has been and continues to be the subject of legal proceedings and adjudications from time to time, none of which have had, individually or in the aggregate, a material adverse impact on the Group. Management believes that the resolution of all current and potential legal matters will not have a material impact on the Group's financial position or operating results.

Subsequent to the Group's acquisition of Bullion Development Ltd., the Group became a defendant in a number of claims from other shareholders of VK relating to the conduct of the affairs of VK. The financial impact of these claims cannot be estimated at this time as they do not contain any specific damages, but the Group does not expect any reasonably possible outcome of the claims to have a material effect on the Group's consolidated financial statements.

13.4 Competition

The development by domestic and large international internet companies of Russian language versions of the services competing with the services the Group provides could decrease the Group's user base and make it less attractive to advertisers.

Increased competition could result in a reduction in the number of users who buy Group's IVAS – including games – which, in turn, would result in lower revenue and net income. Similarly, the Group may be required to spend additional resources to promote or improve its services in order to compete effectively, which could require additional capital or adversely affect Group's profitability.

13.5 Private information

To become registered on the website operated by the Group, users have to input their personal data, which is then protected by the Group from access by third parties. Should such data become available to third parties as a result of hackers' attacks, the Group may become a party to litigations from its users. Management believes it takes all necessary steps to reduce the related risk to an acceptable level.

13 Commitments, contingencies and operating risks (continued)

13.6 Intellectual property rights

The Group may be subject to infringement claims from third parties in the future resulting from the technology and intellectual property used in the provision and marketing of its services. If the Group is found liable for infringement, it may be required to pay significant damages, and if it is unable to license or develop non-infringing technology on a timely basis, it may be unable to continue offering the affected services without risk of liability. Similarly, third parties may obtain and use the Group's intellectual property without authorisation. The validity, application, enforceability and scope of protection of intellectual property rights for many Internet-related activities are uncertain and still evolving, which may make it more difficult for the Group to protect its intellectual property, which could have a material effect on its business, results of operations and financial condition. The Group and its associates have been subject to such proceedings in the past. Although none of them was individually significant, similar potential claims may potentially subject the Group to significant losses in the future, which currently cannot be reliably estimated.

13.7 Development

A failure to innovate, to provide popular products and services or to react quickly to changes in the market could affect the popularity of the Group's sites and, in turn, could affect advertising revenue. An inability to develop products and services which are compatible with new mobile devices could result in a failure to capture a significant share of an increasingly important market.

13.8 Regulation

New laws and regulations, or new interpretations of existing laws and regulations, could require the Group to invest in restructuring certain services or could lead to a reduction in their take-up by users, with a resulting effect on revenue and profitability.

The law on amending the Federal Law "On Information, Information Technologies and Protection of Information" (the "Anti-extremism Law") came into force on February 1, 2014. According to the Anti-Extremism law, the Prosecutor General of Russia (or his deputies) may apply to Roscomnadzor to block websites on which the Prosecutor finds any prohibited information concerning appeals to mass riots, extremist activities or participation in mass (public) actions held in infringement of the established order. The website may be blocked without the need for any court order or a mandatory preliminary notification to the site. Access is granted anew after the prohibited information is removed and Roscomnadzor is notified. The Group's failure or the failure of Group's third party providers, to accurately comply with the Anti-extremism Law or takedown requests could create liability for the Group, result in adverse publicity, or could otherwise have a material adverse effect on Group's business, results of operations and financial condition.

In May 2014, the new Law No. 97-FZ was adopted, which will come into force on August 1, 2014 ("Law on Bloggers"). The new Law on Bloggers introduces requirements to the sites and/or services that enable users to publish and share information to, amongst others, notify the authorities about the commencement of such activities, store the data on receipt, transfer, processing of the users' information in the Russian Federation for the period of 6 months, share the information on users' actions with the authorized governmental body upon a relevant request, and be in line with certain technical requirements set by authorities. In addition, owners of web-sites and internet pages with more than 3,000 daily users are required to be identified, registered with a special register and comply with certain requirements in respect of the materials published on web-sites and internet pages under their control. Non-compliance with the Law on Bloggers may lead to blocking of internet domains. In order to meet the requirements, the Group may need to incur significant costs to expand its infrastructure. The Group's failure or the failure of Group's third party providers, to accurately comply with the Law on Bloggers could create liability for the Group, result in adverse publicity, or could otherwise have a material adverse effect on Group's business, results of operations and financial condition.

The Group complies with the new laws and none of the Group's Russian properties have been blocked up to date, and no blockings have materially affected the Group's consolidated financial statements.

13.9 Personnel

As competition in Russia's internet industry increases, the Group's business and operations could be adversely affected by difficulties in hiring, motivating and retaining highly-skilled people. Competition for senior managers is high. One or more could join a competitor, or set-up a competing company, with the result that operations and profitability could be affected by a loss of strategic direction, users, know-how and additional staff.

13.10 Infrastructure and capacity

If the infrastructure in Russia were not able to support increased demand, the Group's services could be interrupted or the Group's systems damaged. A limited availability of third-party providers of network and server capacity could limit the Group's ability to offer certain services or to expand. Network or power failures could result in the loss of data and in a reduction in the number of users, which could have a material effect on the Group's business, results of operations and financial condition.

Notes to the Interim Condensed Consolidated Financial Statements (continued)

14 Balances and transactions with related parties

The following table provides the total amount of transactions which have been entered into with related parties during the six month periods ending June 30, 2014 and June 30, 2013 as well as balances with related parties as of June 30, 2014 and December 31, 2013, excluding directors and key management of the Group (see below). All related party transactions were made in accordance with contractual terms and conditions agreed between the parties.

	Sales to related parties	Purchases from related parties	Amounts owed by related parties	Amounts owed to related parties
2014				
Strategic associates	92	70	76	4
Other entities	–	15	–	3
2013				
Strategic associates	79	85	72	4
Other entities	1	11	2	4

The Group's sales to and receivables from related parties mainly include sales to and receivables from Haslop Company Limited ("Mamba") and VK.com Limited ("VK").

The Group's sales to, and receivables from Mamba primarily arise from a revenue sharing arrangement relating to IVAS generated by a dating website operated by Mamba.

The Group's receivables from VK primarily arise from the Group's social games offered via the VK social network. The arrangement with VK is entered into on terms equivalent to those that prevail in arm's length transactions. Total revenue earned by the Group through the VK platform was RUR 62 (2013: 68), total commission due to VK was RUR 27 (2013: 30) and is included in "Purchases from related parties" in the table above.

The Group's purchases from, and payables to related parties mainly include purchases from and payables to Qiwi and primarily arise from revenue collection services. The arrangement with Qiwi is entered into on terms equivalent to those that prevail in arm's length transactions.

14.1 Directors of the Company

Total cash remuneration of the members of the Board of Directors (each a "Director" and collectively, "Directors") of the Company amounted to RUR 24 for the six months ended June 30, 2014 (2013: RUR 23). No options over the shares of the Company were granted to Directors for the six months ended June 30, 2014 (2013: nil). During the six months ended June 30, 2014, Directors did not forfeit any options (2012: nil) and did not exercise any options over shares of the Company (2013: 26,766). The corresponding share-based payment expense was a negative RUR 73 for the six months ended June 30, 2014 (2013: a positive 19).

14.2 Key management of the Group

Total cash remuneration of the key management of the Group (excluding Directors) amounted to RUR 205 for the six months ended June 30, 2014 (2013: RUR 282). In the six months ended June 30, 2014, key executive employees of the Group (excluding Directors) were not granted any options over shares of the Company (2013: 301,000 options at the exercise price of USD 19.6 per share and 60,000 options at the exercise price of USD 17.5 per share). During the six months ended June 30, 2014, key management of the Group (excluding Directors) forfeited 7,500 options (2013: nil) and exercised 572,738 options over ordinary shares of the Company (2013: 520,538). The corresponding share-based payment expense amounted to RUR 270 for the six months ended June 30, 2014 (2013: RUR 612).

14.3 The ultimate controlling party

Starting from June 7, 2013, the Group is ultimately controlled by Mr Alisher Usmanov. The Group did not have an ultimate controlling party prior to that date.

Notes to the Interim Condensed Consolidated Financial Statements (continued)

15 Financial instruments

The carrying amounts of the Group's financial instruments approximated their fair values as of June 30, 2014 and December 31, 2013 and are presented by category of financial instruments in the table below:

	Category*	June 30, 2014	December 31, 2013
Financial assets			
Financial investments in associates	FAFVPL	1,352	1,293
Derivative financial assets over the equity of investees	FAFVPL	8	20
Convertible note	FAFVPL	–	46
Financial derivatives under lease and hosting contracts	FAFVPL	44	37
Long-term deposits	LR	1	1
Trade accounts receivable	LR	2,401	2,957
Loans and interest receivable	LR	90	87
Short-term time deposits	LR	129	315
Cash and cash equivalents	LR	26,202	30,987
Total financial assets		30,227	35,743
Current		28,822	34,404
Non-current		1,405	1,339
Total derivative financial assets		51	103
Current		14	66
Non-current		37	37
Financial liabilities			
Trade accounts payable	FLAC	1,157	1,292
Total financial liabilities		1,157	1,292
Current		1,157	1,292
Non-current		–	–

* Financial instruments used by the Group are included in one of the following categories:
- FAFVPL – financial assets at fair value through profit or loss;
- AFSFA – available-for-sale financial assets;
- LR – loans and receivables;
- FLFVPL – financial liabilities at fair value through profit or loss; or
- FLAC – financial liabilities at amortised cost.

Fair value of cash and cash equivalents, short-term time deposits, short-term accounts receivable, other current assets, trade accounts payable approximate their carrying amounts largely due to the short-term maturities of these instruments.

15.1 Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments based on the observability of the inputs used in measuring fair value:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices);
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

As at June 30, 2014 and December 31, 2013 the Group held the following financial instruments measured at fair value:

	June 30, 2014	Level 1	Level 2	Level 3
Financial assets measured at fair value				
Financial assets at fair value through profit or loss:				
Financial investments in associates	*1,352*	–	–	*1,352*
Derivative financial assets over the equity of investees	*8*	–	–	*8*
Financial derivatives under hosting contract	*7*	–	–	*7*
Financial derivatives under lease contract	*37*	–	–	*37*
Total financial assets at fair value through profit or loss	1,404	–	–	1,404

Notes to the Interim Condensed Consolidated Financial Statements (continued)

15 Financial instruments (continued)

15.1 Fair value hierarchy (continued)

	December 31, 2013	Level 1	Level 2	Level 3
Financial assets measured at fair value				
Financial assets at fair value through profit or loss:				
Financial investments in associates	*1,293*	–	–	*1,293*
Derivative financial assets over the equity of investees	*20*	–	–	*20*
Convertible note	*46*	–	–	*46*
Financial derivatives under lease contract	*37*	–	–	*37*
Total financial assets at fair value through profit or loss	1,396	–	–	1,396

The balance of Level 3 measurements as of December 31, 2013 is reconciled to the balance of those measurements as of June 30, 2014 as follows:

	Balance as of January 1, 2014	Reclassification	Purchases	Issue of option as part of consideration for VK	Sales	Gains/(losses) recognized in profit and loss	Balance as of June 30, 2014
Financial assets measured at fair value							
Financial assets at fair value through profit or loss:							
Financial investments in associates	*1,293*	*46*	*69*	–	*(67)*	*11*	*1,352*
Financial derivatives under lease contract	*37*	–	–	–	–	–	*37*
Financial derivatives under hosting contract	–	–	–	–	–	*7*	*7*
Convertible note	*46*	*(46)*	–	–	–	–	*0*
Derivative financial assets over the equity of investees	*20*	–	–	–	–	*(12)*	*8*
Total financial assets at fair value through profit or loss	1,396	–	69	–	(67)	6	1,404
Financial liability measured at fair value							
Financial liabilities at fair value through profit or loss – derivative over the equity of subsidiary	–	–	–	*(200)*	–	*200*	–
Total financial liabilities measured at fair value	–	–	–	(200)	–	200	–

In March 2014 the Group issued a three months call option over 100% of Headhunter as a part of consideration for VK additional stake acquisition (Note 5) with a fair value of RUR 200. In June 2014 the option expired unexercised. The Group de-recognised the respective financial liability and recognized a gain under “Net gain on financial assets and liabilities at fair value through profit or loss over the equity of strategic associates, subsidiaries and other agreements” in its consolidated statement of comprehensive income.

15.2 Valuation techniques

Financial investments in associates are the Group’s investments in various smaller Internet businesses that form the Group’s venture capital portfolio and are managed exclusively on the basis of their fair values, even though the Group may have significant influence over the respective investees.

The fair values of financial investments in associates either were determined using discounted cash flow (“DCF”) models or based on recent cash transactions, depending on which valuation technique produced more reliable results. The DCF models use cash flow projections from financial budgets approved by senior management covering an seven-year period. The main assumptions used in the DCF models as of June 30, 2014 and December 31, 2013 are as follows:

	June 30, 2014	December 31, 2013
Terminal growth rate	5.0%	5.0%
Discount rates	30%-35%	30%-35%

Notes to the Interim Condensed Consolidated Financial Statements (continued)

15 Financial instruments (continued)

15.3 Risk assessment

The Group's investments in equity securities are susceptible to market price risk arising from uncertainties about future values of the investment securities. The Group's financial instruments exposed to the equity price risk primarily relate to the Group's financial investments in associates and available-for-sale equity investments. The Group's derivative financial instruments are also subject to equity price risk, inasmuch as the underlying assets represent equity instruments of the Group's investees.

The inherently high equity price risk of the Group's venture capital investments and associated derivative financial instruments is mitigated by the Group through a highly selective approach to venture capital investments, regular reviews of the fair values of existing and potential investees by a team of highly qualified venture capital investment professionals and maintaining the composition of the venture capital portfolio that includes a large number of investments in ventures operating in different segments of the Internet industry. Additionally, the overall impact of venture capital activities on the Group's operations is mitigated by a limited size of the venture capital investment portfolio in relation to the aggregate operations of the Group.

At the reporting date, the Group's exposure to unlisted equity securities at fair value through profit or loss and derivative financial instruments was equal to the carrying amounts of the respective financial instruments as of the reporting date. A 10% decrease in the overall earnings stream of the valuations performed for the Group's unlisted investments could have a negative impact of approximately RUR 13 (2013: RUR 24) on the Group's pre-tax income. A 500 basis point increase in the discount rate used in the valuation models could result in a negative impact of RUR 15 (2013: RUR 31) on the Group's pre-tax income. A 5% increase in significant unobservable inputs used in recent cash transaction models for valuations of some unlisted Group's investments could have a positive impact of approximately RUR 49 (2013: RUR 45) on the Group's pre-tax income. The effect of a 100 basis point increase in risk-free rate on the Group's pre-tax income is not significant in all periods presented in these interim condensed consolidated financial statements.

16 Events after the reporting period

16.1 Disposal of investment in a strategic associate

In July 2014 the Group sold 0.64% of the economic interest in its strategic associate Qiwi for an aggregate net cash consideration of RUR 442. After partial disposal of the investment the Group retained a 5.28% economic interest and power to participate in the financial and operating policy decisions through its representation in Qiwi's Board of Directors. Accordingly the Group retained significant influence over Qiwi and continued to account for the remaining investment using the equity method.

16.2 Changes in structure of USM Holdings Ltd. shareholders

In August 2014, Mr Alisher Usmanov's voting power in USM Holdings Ltd. ("USM") decrease to 48%. USM is the beneficial owner of New Media and Technology Investment L.P and Ardoe Finance Limited, the shareholders of the Company.