

Moody's Corporation (MCO)

\$228.71 (As of 04/07/20)

Price Target (6-12 Months): **\$241.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 11/18/19)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: F

Growth: B

Momentum: D

Summary

Shares of Moody's have outperformed the industry in the past six months. Its earnings surpassed the Zacks Consensus Estimate in each of the trailing four quarters. The company remains well positioned on the back of its dominant position in the credit rating industry, diverse revenue base and strong balance sheet position. The company's inorganic growth strategy will help it further diversify revenue sources and move away from solely providing rating services. However, volatility in macro environment will likely result in a slowdown in global issuance volumes. Additionally, mounting operating expenses mainly owing to investments in franchise and acquisitions are likely to hurt profitability to some extent. Further, stiff competition is expected to put pressure on pricing, which in turn may hurt the company's financials in the long run.

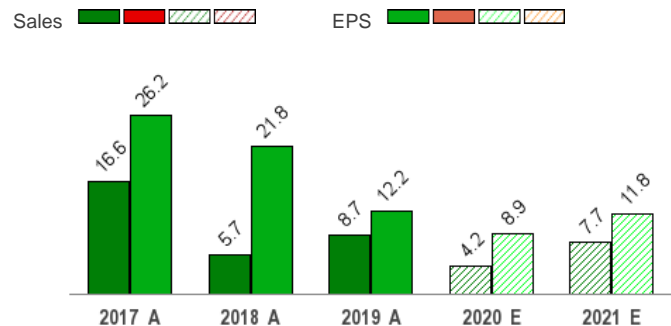
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$287.25 - \$164.19
20 Day Average Volume (sh)	1,749,911
Market Cap	\$42.8 B
YTD Price Change	-3.7%
Beta	1.18
Dividend / Div Yld	\$2.24 / 1.0%
Industry	Financial - Miscellaneous Services
Zacks Industry Rank	Top 32% (80 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.2%
Last Sales Surprise	1.8%
EPS F1 Est- 4 week change	-2.1%
Expected Report Date	04/22/2020
Earnings ESP	-0.2%
P/E TTM	27.6
P/E F1	25.3
PEG F1	2.0
P/S TTM	8.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,296 E	1,316 E	1,376 E	1,368 E	5,417 E
2020	1,222 E	1,231 E	1,285 E	1,285 E	5,031 E
2019	1,142 A	1,214 A	1,241 A	1,233 A	4,829 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$2.54 E	\$2.47 E	\$2.61 E	\$2.52 E	\$10.10 E
2020	\$2.28 E	\$2.17 E	\$2.34 E	\$2.24 E	\$9.03 E
2019	\$2.07 A	\$2.07 A	\$2.15 A	\$2.00 A	\$8.29 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/07/2020. The reports text is as of 04/08/2020.

Overview

Moody's Corporation is a leading provider of credit ratings, research, data & analytical tools, software solutions & related risk management services, quantitative credit assessment services, credit training services and credit process software to banks and other financial institutions.

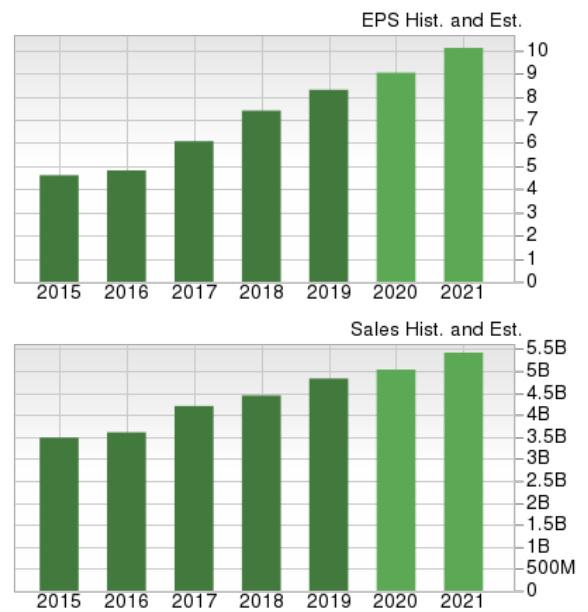
Moody's reports its businesses under the following two operating divisions:

- **Moody's Investors Service (MIS)** (representing 58.4% of revenues in 2019) provides credit ratings and research covering debt instruments and securities. Revenues from MIS comprises ratings revenues from Structured Finance; Corporate Finance; Financial Institutions; and Public, Project and Infrastructure Finance.
- **Moody's Analytics (MA)** (41.6%) offers solutions related to financial and risk management activities of institutions. Within its Enterprise Risk Solutions, MA provides risk management software solutions and related services. Research, Data & Analytics provides investor-oriented research and data, including in-depth research on major debt issuers and industry studies.

Over the years, Moody's made several notable acquisitions including Wall Street Analytics (2006), Fermat International (2008), Copal Partners (2011), Barrie & Hibbert (2011), Amba Investment Services (2013), ICRA Ltd. (2014) and Equilibrium (2015). In 2016, the company acquired Korea Investors Service as well as a prominent actuarial software company, GGY.

In 2017, Moody's acquired the structured finance data and analytics business of Frankfurt-based SCDM and Amsterdam, Netherlands-based Bureau van Dijk. In 2018, the company acquired Omega Performance and Reis Inc. In 2019, it acquired ABS Suite from Deloitte & Touche LLP and RiskFirst. In 2020, the company acquired Regulatory DataCorp and London-based RBA International.

It divested the Analytics Knowledge Services business to Equistone in 2019.



Reasons To Buy:

- ▲ Moody's is pursuing growth in areas outside the core credit ratings service. The company has increased its exposure to the banking and insurance industry, branching into the emerging and fast-growing professional services and enterprise risk solutions sectors. Also, a rising share of the analytics business, which is not correlated with the volatility of interest rates, has added stability to top-line growth. Total revenues have witnessed a five-year (2015-2019) CAGR of 8.5%. Improved mix and lower-risk nature of the product portfolio will likely boost the company's revenues.
- ▲ Moody's holds a dominant position in the duopolistic credit rating industry. Higher monitoring revenues related to new ratings has been a key driver in the corporate finance line — the largest revenue contributor at the MIS division. Despite a slowdown in global bond issuances over the last few quarters, the corporate finance division witnessed revenue growth at a three-year CAGR of 1.7% (ended 2019). The company remains focused on investing in technology platform and processes to boost operations. These efforts are expected to strengthen the division's top-line performance in the quarters ahead.
- ▲ Moody's grew meaningfully over the years through several strategic acquisitions, which provided it with increased scale and cross-selling opportunities across products and vertical markets. In 2020, the company acquired Regulatory DataCorp and London-based RBA International. Last year as well, it undertook inorganic expansion initiatives, which are expected to help diversify revenues and be accretive to earnings. The company will continue to pursue opportunistic deals that are strategic fits and complement existing operations.
- ▲ Strong balance sheet and cash flow enable Moody's to pursue growth opportunities and enhance shareholders' value. In February 2020, the company announced a 12% hike in quarterly dividend. Also, the company has a share repurchase authorization in place. In December 2019, the company authorized an additional \$1 billion worth of share buyback program. As of Dec 31, 2019, Moody's had nearly \$1.3 billion worth of share buyback authorization remaining. Driven by its capital strength and favorable dividend payout ratio, the company will be able to sustain enhanced capital deployments.

Moody's is well positioned for growth on the back of its dominant position in the credit rating industry, constant efforts to diversify revenue base and synergies from strategic acquisitions.

Reasons To Sell:

- ▼ Elevated operating expenses remain a major concern for Moody's. Operating expenses witnessed a five-year (2015-2019) CAGR of 9.2%, mainly due to rise in operating and SG&A costs. The company expects expenses to keep on rising as it continues to invest in franchise and grow inorganically. Additionally, credit rating agencies including Moody's are subject to increased regulatory scrutiny since the 2008 financial crisis. These increase costs related to compliance and governance, thus leading to further rise in expenses.
- ▼ Moody's faces considerable economic risks related to the volatile macro environment and its effect on the financial markets and bond issuance. The uncertain macro environment will affect the volume of debt securities issued in global capital markets and the demand for credit ratings.
- ▼ Moody's faces stiff competition in most of the markets in which it operates. In the credit rating sector, the company faces competition from Fitch, S&P Ratings Services, Morningstar and many other regional providers. In the analytics segment, it faces competition from Dun & Bradstreet, Bloomberg, IBM, Fiserv and many others. In the risk management software market, the company competes with large software developers including SAS, Oracle, IBM and Mysis. Stiff competition will likely continue to put pressure on pricing that may hurt profitability in the long run.
- ▼ Shares of Moody's have outperformed the industry over the past six months. However, the company's 2020 earnings estimates have moved 2% lower over the past 30 days. Further, the stock seems overvalued compared with the broader industry. Its current price/book (P/B) and price/earnings (P/E) (F1) ratios are above the respective industry averages. Therefore, given the concerns and downward estimate revisions, the stock has limited upside potential.

Continued increase in operating expenses, slowdown in bond issuance volumes, litigation issues and stiff competition across the credit rating industry are major near-term headwinds for Moody's.

Last Earnings Report

Moody's Beats on Q4 Earnings as Issuance Volume Rises

Moody's reported fourth-quarter 2019 adjusted earnings of \$2.00 per share, which outpaced the Zacks Consensus Estimate of \$1.92. Also, the figure improved 23% from the year-ago quarter.

Results were largely driven by impressive global issuance volume and improving operating scenario, which led to rise in revenues. However, higher operating expenses posed an undermining factor.

After taking into consideration certain non-recurring items, net income was \$361 million or \$1.88 per share, up from \$254 million or \$1.29 per share in the prior-year quarter.

In 2019, adjusted earnings per share of \$8.29 beat the consensus estimate of \$8.20 and increased 12% year over year. Net income (GAAP basis) was \$1.43 billion or \$7.42 per share, up from \$1.32 billion or \$6.74 per share in 2018.

Revenues & Costs Rise

Revenues of \$1.23 billion beat the Zacks Consensus Estimate of \$1.21 billion. Also, the top line grew 16% year over year. Foreign currency translation impact was negligible.

In 2019, revenues of \$4.83 billion beat the consensus estimate of \$4.80 billion and improved 9% year over year. Foreign currency translation unfavorably impacted revenues by 1%.

Total expenses were \$729 million, up 7% year over year. The rise was mainly due to increase in compensation expenses, partially offset by beneficial impact of the restructuring plan and cost control initiatives. Notably, foreign currency translation impact was negligible.

Adjusted operating income of \$559 million increased 17% year over year. Adjusted operating margin was 45.3%, up from 45%.

Quarterly Segment Performance

Moody's *Investors Service* revenues grew 21% year over year to \$720 million attributable to rise in issuance activity. Foreign currency translation unfavorably impacted the segment's revenues by 1%.

Corporate finance revenues increased driven by robust bond issuances. Also, financial institutions' revenues grew, primarily backed by rise in activity from infrequent U.S. insurance and non-U.S. banking issuers.

Further, public, project and infrastructure finance revenues increased, reflecting strong U.S. public finance issuance. However, structured finance revenues witnessed a fall, mainly due to lower global collateralized loan obligation activity.

Moody's *Analytics* revenues grew 10% year over year to \$513 million, mainly driven by higher U.S. and international revenues. Foreign currency translation impact on the segment's revenues was negligible.

The segment recorded growth in research, data and analytics revenues, and Enterprise Risk Solutions revenues, while professional services revenues declined.

Strong Balance Sheet

As of Dec 31, 2019, Moody's had total cash, cash equivalents and short-term investments of \$1.9 billion, up from \$1.8 billion as of Dec 31, 2018. Further, it had \$5.6 billion of outstanding debt and \$1 billion in additional borrowing capacity under its revolving credit facility.

Share Repurchases Update

During the fourth quarter, the company repurchased 1.2 million shares for \$263 million.

2020 Guidance

Moody's expects adjusted earnings per share to be in the lower end of \$9.10-\$9.30 range. On GAAP basis, earnings are expected within \$8.60-\$8.80 per share.

The company projects revenues to rise in the mid-single-digit percent range.

Operating expenses are expected to increase in the low-single-digit percent range.

The company expects net interest expenses in the range of \$180-200 million.

Adjusted operating margin is expected in the band of 48-49% and operating margin is likely to be 44%.

Moody's expects cash flow from operations in the \$1.8-\$1.9 billion range and free cash flow to be about \$1.7-\$1.8 billion.

Share repurchases are estimated to be \$1.3 billion.

Segment Outlook for 2020

Quarter Ending 12/2019

Report Date	Feb 12, 2020
Sales Surprise	1.75%
EPS Surprise	4.17%
Quarterly EPS	2.00
Annual EPS (TTM)	8.29

MIS segment revenues are likely to increase in the low-single-digit percent range, down from prior outlook of mid-single digit percentage. The key reason behind the dismal outlook is the impact of coronavirus outbreak on the global economy.

Adjusted operating margin is expected to be 58-59%.

Coming to the *MA segment*, Moody's anticipates revenues to grow in the high-single-digit percent range. Adjusted operating margin is expected to be 30%.

Recent News

Moody's Buys RBA International from Parabellum Investments – Mar 2, 2020

Moody's acquired London-based RBA International from Parabellum Investments. Being a leader in providing online retail bank training and certifications, RBA International offers training programs that are required to prepare bankers for the evolving retail banking landscape.

The acquisition strengthens the capabilities of Moody's Analytics Learning Solutions ("MALS"). MALS is a unit of the Moody's Analytics division, which offers online and classroom-based training services as well as credentialing and certification.

The Moody's Analytics division, comprising more than 35% of the company's revenues, offers solutions related to financial and risk-management activities of institutions.

The executive director of MALS, Ari Lehari, said, "Technological advances and automation have raised the bar for retail bankers to provide a higher level of consultation and service to clients. The combined capabilities of Moody's Analytics and RBA will help banks enhance the productivity and effectiveness of their retail professionals, which is an imperative in the current business environment."

The transaction was funded with cash. It is not expected to have a material impact on Moody's 2020 financials.

Evelyn Hunter, the director of RBA International, stated, "RBA was founded to strengthen the status of retail bankers as internationally recognized professionals. We look forward to working as a part of MA to help clients enrich and modernize their skillsets to reflect the dynamic shifts occurring in the retail banking sector."

Moody's Acquires Regulatory DataCorp for \$700 Million – Feb 13, 2020

Moody's acquired Regulatory DataCorp for \$700 million via a deal that complements the earlier acquisition of Bureau van Dijk. Regulatory DataCorp is a leading provider of anti-money laundering and know-your-customer data and due diligence services, which is currently owned by Vista Equity Partners, a leading investment firm focused on enterprise software, data and technology-enabled businesses.

At the time of the deal announcement in January, it was noted that the transaction will likely generate \$55 million of annualized revenues in 2020. Also, the deal will likely be accretive to earnings per share on an adjusted basis in 2022. Considering the estimated impact of amortization expense relating to acquired intangible assets, the deal will likely be accretive to 2024 GAAP EPS.

Moody's stated that including the impact of this transaction, it anticipates repurchasing shares worth \$1.3 billion in 2020.

Moody's Closes Divestiture of Analytics Knowledge Business – Nov 8, 2019

Moody's closed the divestiture of MAKES, its Moody's Analytics Knowledge Services business, to a London-based private equity firm Equistone Partners Europe Limited. The deal was announced in July.

MAKS is one of the prominent providers of knowledge process outsourcing services. Through delivery centers in India, Costa Rica, Sri Lanka and China, it serves more than 250 banks, asset managers and consulting firms.

At the time of announcing the deal, Moody's had noted that it is likely to use the sale proceeds and repatriated offshore cash from this transaction to repurchase nearly \$300 million worth of shares.

Moody's Acquires Minority Stake in SynTao – Oct 28, 2019

Moody's acquired minority stake in China-based SynTao Green Finance, a leading provider of environmental, social and governance (ESG) data and analytics. Terms of the deal were not disclosed.

Moody's investment in SynTao aligns with its ongoing global commitment to promoting transparent standards for evaluating ESG risks.

Hao Shi, managing director, country manager for Moody's China operations stated, "Since its founding, STGF has solidified its position in China as a local standard setter and leading domestic platform for ESG data and analytics. STGF's China-specific data sets provide opportunities to enhance Moody's global ESG research and data. Together we will seek to leverage our respective strengths and capabilities to provide a range of solutions for investor and issuer ESG needs, including joint research, product development and technical cooperation."

Moody's Acquires ABS Suite Business From Deloitte - Oct 2, 2019

Moody's announced that it acquired ABS Suite from Deloitte & Touche LLP, as part of its efforts to strengthen the Moody's Analytics division.

ABS Suite is a software platform that is used by issuers and trustees for management and supervision of asset-backed and mortgage-backed securities programs.

The Moody's Analytics division, which represents more than 35% of Moody's revenues, offers various solutions related to financial and risk-management activities of institutions. Under its Enterprise Risk Solutions, it provides risk-management software solutions and related services. Its Research, Data & Analytics provides investor-oriented research and data, including in-depth research on major debt issuers and industry studies.

The president of Moody's Analytics, Mark Almeida, said, "The acquisition of ABS Suite deepens Moody's Analytics' presence with issuers of securitized transactions. Adding the expertise and experience of the ABS Suite team to our already formidable capabilities enables us to provide more and better solutions that improve funding decisions, increase operational efficiency and promote transparency and efficiency in the securitization financial markets."

Employees of ABS Suite will join the Structured Solutions business of Moody's Analytics.

Moody's Announces Acquisition of RiskFirst – Jul 25, 2019

With an aim of strengthening the MA segment's performance, Moody's acquired RiskFirst, a leading FinTech company that provides risk analytic solutions for the asset management and pension fund communities.

While the terms of the deal were not disclosed, it is expected to be accretive to GAAP EPS in 2022. On an adjusted basis, the transaction is expected to be accretive to earnings in 2021.

Dividend Update

On Feb 12, Moody's announced a quarterly cash dividend of 56 cents per share, representing a hike of 12% from the prior payout. The dividend was paid out on Mar 18 to shareholders of record as of Feb 25.

Valuation

Shares of Moody's are up 22.6% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 28.2% and 23.6%, over the past year, respectively.

The S&P 500 index is down 8.1% in the past year.

The stock is currently trading at 24.55X forward 12 months earnings, which compares to 8.76X for the Zacks sub-industry, 11.68X for the Zacks sector and 16.91X for the S&P 500 index.

Over the past five years, the stock has traded as high as 30.55X and as low as 16.04X, with a 5-year median of 21.51X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$241 price target reflects 25.86X forward earnings.

The table below shows summary valuation data for MCO

Valuation Multiples - MCO					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	24.55	8.76	11.68	16.91
	5-Year High	30.55	14.15	16.19	19.34
	5-Year Low	16.04	8.69	11.23	15.19
	5-Year Median	21.51	11.35	13.95	17.44
P/CF	Current	26.03	2.82	17.64	13.83
	5-Year High	49.86	8.42	NA	22.67
	5-Year Low	13.62	2.29	11.08	11.67
	5-Year Median	20.75	5.83	21.73	16.37
P/S F12M	Current	8.26	1.14	4.93	2.92
	5-Year High	10.44	1.91	6.65	3.44
	5-Year Low	4.22	1.05	4.93	2.54
	5-Year Median	6.1	1.39	6.03	3

As of 04/07/2020

Industry Analysis Zacks Industry Rank: Top 32% (80 out of 253)



Top Peers

InterCorp Financial Services Inc. (IFS)	Outperform
CIT Group Inc. (CIT)	Neutral
Globe Life Inc. (GL)	Neutral
Jefferies Financial Group Inc. (JEF)	Neutral
Standard Life PLC Unsponsored ADR (SLFPY)	Neutral
S&P Global Inc. (SPGI)	Neutral
TransUnion (TRU)	Neutral
Euronet Worldwide, Inc. (EFT)	Underperform

Industry Comparison Industry: Financial - Miscellaneous Services				Industry Peers		
	MCO Neutral	X Industry	S&P 500	CIT Neutral	GL Neutral	JEF Neutral
VGM Score	D	-	-	B	C	C
Market Cap	42.82 B	175.05 M	18.38 B	1.70 B	7.66 B	3.67 B
# of Analysts	7	3	13	4	4	1
Dividend Yield	0.98%	0.00%	2.31%	8.05%	1.05%	4.57%
Value Score	F	-	-	A	B	A
Cash/Price	0.05	0.40	0.06	2.69	0.02	2.50
EV/EBITDA	21.17	5.65	11.23	4.01	5.67	7.28
PEG Ratio	1.96	1.34	1.91	0.41	1.59	NA
Price/Book (P/B)	51.96	0.74	2.45	0.28	1.06	0.41
Price/Cash Flow (P/CF)	24.15	5.94	9.63	1.91	5.92	7.16
P/E (F1)	25.33	9.46	15.92	4.13	9.99	27.94
Price/Sales (P/S)	8.87	1.07	1.94	0.52	1.69	0.81
Earnings Yield	3.95%	10.29%	6.15%	24.21%	10.01%	3.58%
Debt/Equity	7.30	0.51	0.70	1.11	0.18	1.03
Cash Flow (\$/share)	9.47	0.57	7.01	9.11	12.04	1.83
Growth Score	B	-	-	C	D	D
Hist. EPS Growth (3-5 yrs)	16.41%	11.32%	10.92%	12.02%	12.36%	NA
Proj. EPS Growth (F1/F0)	8.94%	0.65%	-0.12%	-16.85%	5.74%	-64.39%
Curr. Cash Flow Growth	9.81%	5.23%	5.93%	4.00%	6.55%	71.72%
Hist. Cash Flow Growth (3-5 yrs)	12.36%	11.18%	8.55%	-11.97%	6.53%	8.58%
Current Ratio	1.92	1.22	1.24	0.97	0.05	1.77
Debt/Capital	87.96%	35.18%	42.36%	50.52%	15.61%	51.05%
Net Margin	29.44%	14.30%	11.64%	16.11%	16.80%	24.03%
Return on Equity	261.43%	8.97%	16.74%	8.97%	10.97%	5.56%
Sales/Assets	0.50	0.21	0.54	0.06	0.18	0.09
Proj. Sales Growth (F1/F0)	4.50%	0.00%	0.85%	-4.36%	4.08%	-2.39%
Momentum Score	D	-	-	C	C	F
Daily Price Chg	-0.20%	0.25%	0.69%	4.44%	-0.79%	0.15%
1 Week Price Chg	-5.18%	-6.57%	-4.40%	-22.38%	-10.25%	-15.48%
4 Week Price Chg	0.49%	-16.43%	-10.67%	-34.62%	-9.44%	-28.06%
12 Week Price Chg	-8.31%	-33.93%	-23.70%	-61.54%	-31.40%	-39.83%
52 Week Price Chg	22.53%	-39.39%	-15.92%	-64.46%	-15.34%	-33.75%
20 Day Average Volume	1,749,911	105,001	4,068,329	3,468,968	909,079	3,082,248
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-2.14%	-1.74%	-5.24%	-13.11%	-0.35%	-52.04%
(F1) EPS Est 12 week change	0.12%	-9.64%	-6.86%	-17.90%	-0.52%	-69.68%
(Q1) EPS Est Mthly Chg	-6.55%	0.00%	-8.25%	-23.39%	-0.56%	-127.27%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	B
Momentum Score	D
VGM Score	D

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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