

Moody's Corporation (MCO)

\$264.79 (As of 05/28/20)

Price Target (6-12 Months): **\$280.00**

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: C

Momentum: B

Summary

Shares of Moody's have outperformed the industry in the past year. Its earnings surpassed the Zacks Consensus Estimate in each of the trailing four quarters. First-quarter 2020 results were driven by higher revenues. The company remains well poised for growth on the back of its dominant position in the credit rating industry, diverse revenue base and strong balance sheet position. The inorganic growth strategy will help it diversify revenue sources beyond rating services. Yet, volatility in the macro environment will likely result in a slowdown in global issuance volumes. Additionally, mounting operating expenses mainly owing to investments in franchise and acquisitions will likely hurt profitability to some extent. 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)	905,349
Market Cap	\$49.6 B
YTD Price Change	11.5%
Beta	1.17
Dividend / Div Yld	\$2.24 / 0.8%
Industry	Financial - Miscellaneous Services
Zacks Industry Rank	Top 48% (122 out of 254)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	18.7%
Last Sales Surprise	5.4%
EPS F1 Est- 4 week change	-6.1%
Expected Report Date	07/29/2020
Earnings ESP	0.0%
P/E TTM	29.6
P/E F1	32.3
PEG F1	2.5
P/S TTM	10.0

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,322 E	1,216 E	1,251 E	1,324 E	5,110 E
2020	1,290 A	1,108 E	1,111 E	1,168 E	4,687 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	\$2.52 E	\$2.16 E	\$2.25 E	\$2.34 E	\$9.33 E
2020	\$2.73 A	\$1.77 E	\$1.81 E	\$1.88 E	\$8.21 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 05/28/2020. The reports text is as of 05/29/2020.

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.

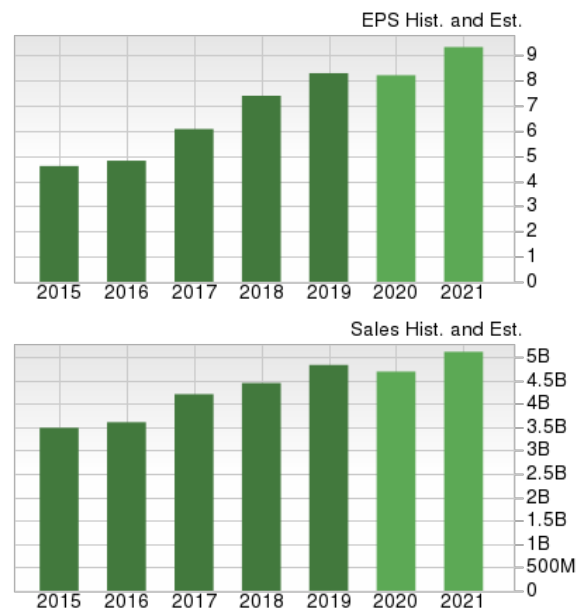
Moody's reports its businesses under the following two operating divisions:

- **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 witnessed a five-year (2015-2019) CAGR of 8.5%, with the momentum continuing in first-quarter 2020. 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 trend persisted in first-quarter 2020. 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.
- ▲ As of Mar 31, 2020, Moody's had total debt worth \$6.8 billion, an undrawn revolving credit facility of \$1 billion, and cash and cash equivalents of \$2.1 billion. Its current total debt total capital of 89.6%, which registered a sequential increase, is significantly higher than the industry average of 65.8%. Nevertheless, the company has debt maturities worth nearly \$1.3 billion through 2021. Also, its times-interest earned of 11.0 at first quarter-end has improved from the prior quarter. These imply that the company has lower credit risk and will likely be able to meet near-term debt obligations even if the economic situation worsens.
- ▲ 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.
- ▲ Moody's capital deployments remain decent. 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 Mar 31, 2020, Moody's had \$1.1 billion worth of shares remaining under the buyback authorization. Notably, it has suspended share repurchases in response to the coronavirus pandemic. Driven by earnings strength and a strong balance sheet position, the company will likely be able to sustain the current 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 the 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 uptrend persisted in first-quarter 2020. Expenses are expected to remain elevated as the company 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 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 earnings estimates for 2020 have moved 6.1% south over the past 30 days. The stock seems overvalued than the broader industry. Its current price/book and price/earnings (F1) ratios are above the respective industry averages. Therefore, given the concerns and downward estimate revisions, the stock has limited upside potential.

Persistent increase in expenses, slowdown in bond issuance volumes, a highly leveraged balance sheet and stiff competition across the credit rating industry are key near-term concerns for Moody's.

Last Earnings Report

Moody's Beats on Q1 Earnings, Revenues Rise Y/Y

Moody's reported first-quarter 2020 adjusted earnings of \$2.73 per share, which outpaced the Zacks Consensus Estimate of \$2.30. Also, the figure improved 32% from the year-ago quarter.

Revenue growth on the back of impressive global bond issuance volume largely drove the results. However, higher operating expenses were an undermining factor.

After taking into consideration certain non-recurring items, net income was \$487 million or \$2.57 per share, up from \$374 million or \$1.93 per share in the prior-year quarter.

Quarter Ending **03/2020**

Report Date	Apr 30, 2020
Sales Surprise	5.37%
EPS Surprise	18.70%
Quarterly EPS	2.73
Annual EPS (TTM)	8.95

Revenues & Costs Rise

Revenues of \$1.29 billion beat the Zacks Consensus Estimate of \$1.22 billion. Also, the top line grew 13% year over year. Foreign currency translation impacted the top line unfavorably by 1%.

Total expenses were \$698 million, up 3% year over year. The rise was supported by disciplined cost management and lower incentive compensation accruals, partly offset by higher bad debt reserves owing to the coronavirus outbreak. Nonetheless, foreign currency translation favorably impacted operating expenses by 1%.

Adjusted operating income of \$649 million increased 25% year over year. Adjusted operating margin was 50.3%, up from 45.4% a year ago.

Segment Performance

Moody's Investors Service revenues grew 19% year over year to \$794 million, attributable to rise in issuance activity. Foreign currency translation unfavorably impacted the segment's revenues by 1%.

Corporate finance revenues increased from the prior-year period, driven by robust bond issuances. Also, financial institutions' revenues grew year over year, primarily backed by rise in activities from U.S. banks and insurance companies.

Further, public, project and infrastructure finance revenues increased from the year-ago level, reflecting strong U.S. public finance issuance, as well as solid project and infrastructure issuance in EMEA. However, structured finance revenues fell from the prior-year figure, mainly due to lower global collateralized loan obligation activity.

Moody's Analytics revenues grew 5% year over year to \$496 million. Foreign currency translation unfavorably impacted the segment's revenues by 1%.

The segment recorded growth in research, data and analytics revenues, as well as Enterprise Risk Solutions revenues.

Strong Balance Sheet

As of Mar 31, 2020, Moody's had total cash, cash equivalents and short-term investments of \$2.2 billion, up from \$1.9 billion on Dec 31, 2019. Further, it had \$6.8 billion of outstanding debt and \$1 billion in additional borrowing capacity under the revolving credit facility.

Share Repurchases Update

During the first quarter, the company repurchased 1.1 million shares for \$253 million. Notably, the company has suspended share repurchases in response to the coronavirus pandemic.

2020 Guidance

Moody's expects the economic implications of the coronavirus outbreak to be more pronounced through the second half of the year. Hence, the company has lowered its 2020 earnings guidance to reflect high level of ambiguity.

Moody's expects adjusted earnings in the range of \$7.80-\$8.40 per share (down from the prior expectation of \$9.10-\$9.30 per share). On GAAP basis, earnings are expected within \$7.25-\$7.85 per share, lower than the earlier guided range of \$8.60-\$8.80 per share.

Moody's now projects revenues to decline in the mid-single-digit percent range versus the prior guidance of revenue growth in the mid-single-digit percent range.

Operating expenses are expected to decrease in the mid-single-digit percent range versus the prior guidance of increase of the same 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 46-48% (down from prior guided range of 48-49%) and operating margin is likely to be within 41-43% (earlier expectation was of approximately 44%).

Moody's expects cash flow from operations in the \$1.3-\$1.5 billion band (down from the \$1.8-\$1.9 billion range) and free cash flow within \$1.2-\$1.4 billion (lower than \$1.7-\$1.8 billion).

Effective tax rate is likely to be in the 19.5-21.5% range (a change projection was 20-22%).

Segment Outlook for 2020

The *MIS segment* revenues are likely to decline in the high-single-digit percent range versus prior view of increase in the low-single-digit percent range. The key reason behind the dismal guidance is the impact of the coronavirus outbreak on the global economy.

Adjusted operating margin is expected within 55-57%, lower than the prior guided range of 58-59%.

Coming to the *MA segment*, Moody's anticipates revenues to grow in the mid-single-digit percent range (versus prior expectation of rise in 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.

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.

Dividend Update

On Apr 22, Moody's announced a quarterly cash dividend of 56 cents per share. The dividend will be paid out on Jun 10 to shareholders of record as of May 20.

Valuation

Shares of Moody's are up 42.2% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Finance sector are down 18.4% and 13.1%, over the past year, respectively.

The S&P 500 index is up 8.4% in the past year.

The stock is currently trading at 30.57X forward 12 months earnings, which compares to 13.06X for the Zacks sub-industry, 16.50X for the Zacks sector and 22.08X for the S&P 500 index.

Over the past five years, the stock has traded as high as 30.57X and as low as 16.04X, with a 5-year median of 21.52X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$280 price target reflects 32.33X 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	30.57	13.06	16.5	22.08
	5-Year High	30.57	14.15	16.5	22.08
	5-Year Low	16.04	8.7	11.58	15.23
	5-Year Median	21.52	11.59	13.94	17.49
P/CF	Current	30.37	7.83	14.62	15.5
	5-Year High	49.86	8.42	NA	22.72
	5-Year Low	13.62	2.26	11.19	11.69
	5-Year Median	21.24	5.84	21.65	16.36
P/S F12M	Current	10.22	1.02	5.81	3.42
	5-Year High	10.44	1.91	6.7	3.44
	5-Year Low	4.22	1.02	4.99	2.53
	5-Year Median	6.18	1.38	6.05	3.01

As of 05/28/2020

Industry Analysis Zacks Industry Rank: Top 48% (122 out of 254)



Top Peers

Company (Ticker)	Rec	Rank
Globe Life Inc. (GL)	Neutral	3
InterCorp Financial Services Inc. (IFS)	Neutral	4
Jefferies Financial Group Inc. (JEF)	Neutral	2
Standard Life PLC Un-sponsored ADR (SLFPY)	Neutral	3
SP Global Inc. (SPGI)	Neutral	3
TransUnion (TRU)	Neutral	4
CIT Group Inc. (CIT)	Underperform	4
Euronet Worldwide, Inc. (EFT)	Underperform	5

Industry Comparison Industry: Financial - Miscellaneous Services				Industry Peers		
	MCO	X Industry	S&P 500	CIT	GL	JEF
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	4	3	2
VGM Score	D	-	-	F	B	F
Market Cap	49.65 B	191.48 M	21.49 B	1.89 B	8.20 B	4.18 B
# of Analysts	7	3	14	3	4	1
Dividend Yield	0.85%	0.00%	1.98%	7.28%	0.97%	4.02%
Value Score	F	-	-	F	B	C
Cash/Price	0.05	0.47	0.06	2.35	0.05	2.01
EV/EBITDA	24.43	4.95	12.50	5.39	5.86	10.16
PEG Ratio	2.50	2.53	2.87	NA	2.26	NA
Price/Book (P/B)	62.14	0.88	2.95	0.35	1.26	0.44
Price/Cash Flow (P/CF)	27.96	8.02	11.81	2.11	6.40	8.14
P/E (F1)	32.23	14.23	21.33	NA	11.07	32.44
Price/Sales (P/S)	9.98	1.56	2.28	0.61	1.81	0.92
Earnings Yield	3.10%	6.07%	4.50%	-12.85%	9.03%	3.08%
Debt/Equity	8.47	0.43	0.76	1.52	0.21	1.10
Cash Flow (\$/share)	9.47	0.60	6.96	9.11	12.04	1.83
Growth Score	C	-	-	F	C	F
Hist. EPS Growth (3-5 yrs)	17.21%	11.02%	10.87%	6.84%	12.88%	NA
Proj. EPS Growth (F1/F0)	-1.02%	-24.11%	-10.48%	-148.75%	3.15%	-65.15%
Curr. Cash Flow Growth	9.81%	5.63%	5.39%	4.00%	6.55%	71.72%
Hist. Cash Flow Growth (3-5 yrs)	12.36%	13.16%	8.55%	-11.97%	6.53%	8.58%
Current Ratio	1.70	1.26	1.29	0.98	0.07	1.63
Debt/Capital	89.45%	32.97%	44.54%	58.00%	17.12%	52.78%
Net Margin	30.88%	9.20%	10.59%	-6.87%	16.32%	24.03%
Return on Equity	235.22%	7.95%	16.26%	2.77%	10.86%	5.63%
Sales/Assets	0.49	0.22	0.55	0.06	0.18	0.09
Proj. Sales Growth (F1/F0)	-2.95%	0.00%	-2.53%	0.40%	2.32%	-2.20%
Momentum Score	B	-	-	D	B	D
Daily Price Chg	2.32%	0.00%	-0.65%	-6.24%	-1.73%	-4.91%
1 Week Price Chg	2.19%	2.45%	4.99%	12.33%	5.50%	6.08%
4 Week Price Chg	8.56%	4.05%	4.28%	1.26%	-6.39%	8.75%
12 Week Price Chg	4.82%	-11.69%	-3.05%	-45.21%	-14.02%	-24.11%
52 Week Price Chg	41.37%	-25.31%	0.01%	-60.87%	-10.88%	-17.80%
20 Day Average Volume	905,349	91,640	2,425,602	2,600,054	706,465	2,048,013
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-6.10%	-0.12%	-1.70%	0.00%	0.00%	0.00%
(F1) EPS Est 12 week change	-10.86%	-25.07%	-16.00%	-138.99%	-2.79%	-53.06%
(Q1) EPS Est Mthly Chg	-13.16%	-6.75%	-3.25%	78.10%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	C
Momentum Score	B
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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