

# Moody's



# McGRAW HILL FINANCIAL

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## Comparison:

Moody's Corp. (MCO)

McGraw-Hill Financial (MHFI)

***A Focus on the Credit Rating Agencies***

March 2016

@find\_me\_value

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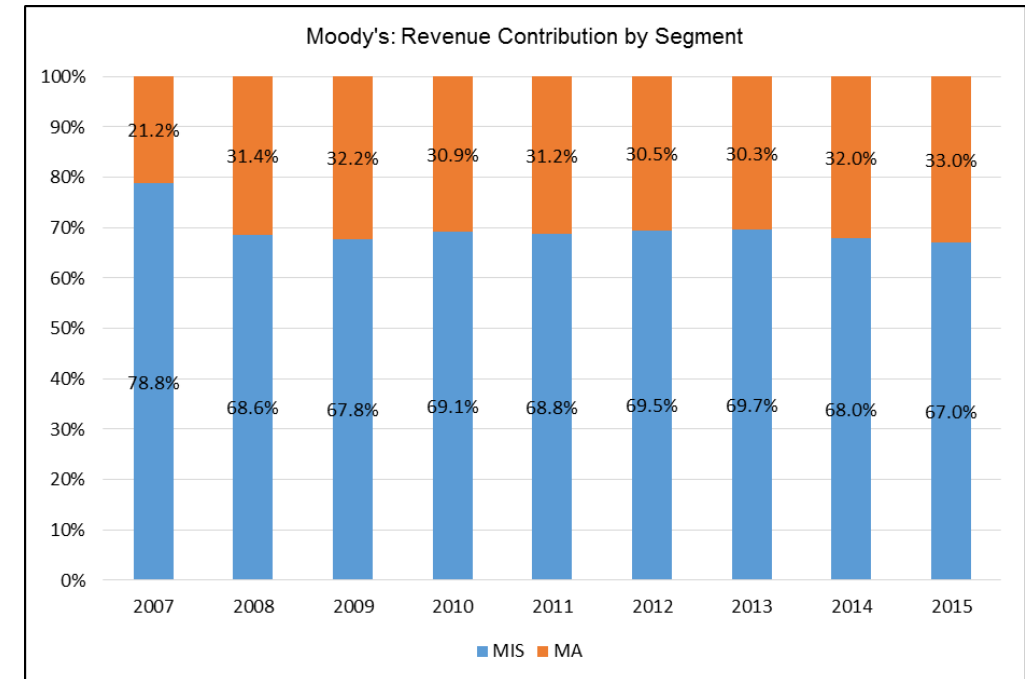
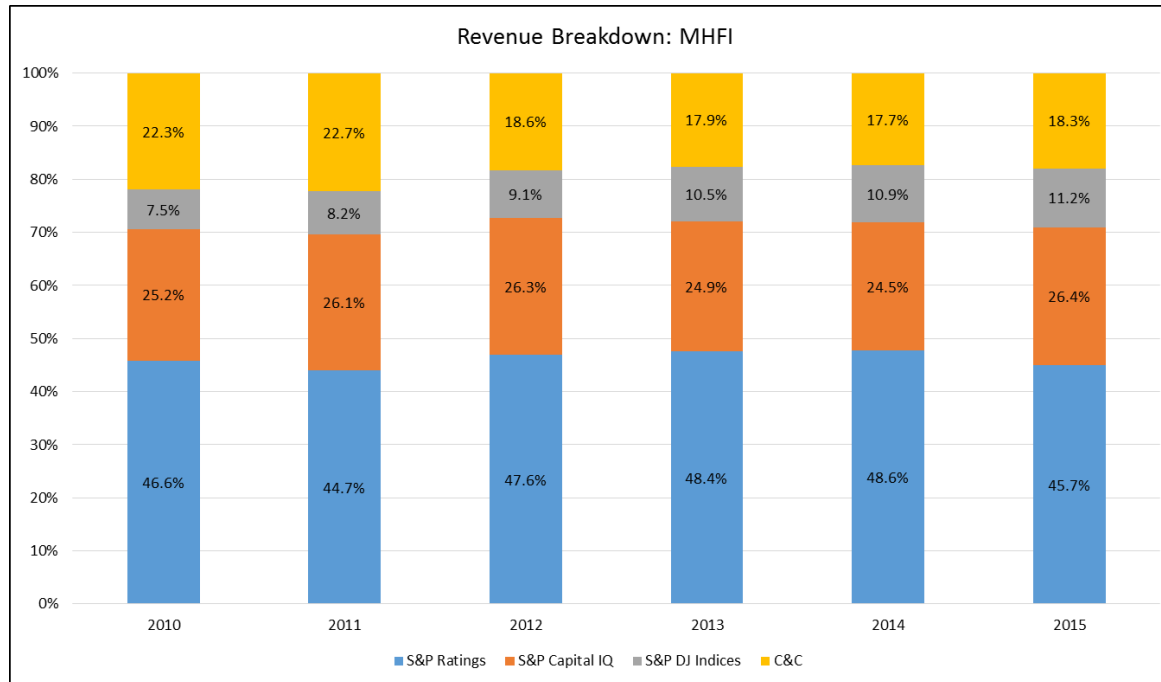
# Conclusions:

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- Moody's business is more of a pure-play ratings business, with mid-80% of operating income coming from the "ratings business" versus MHFI at mid-50%
  - MHFI is pushing harder to expand both the analytics and non-ratings related businesses with the acquisition of SNL Kagan and the other businesses (DJ Indices, C&C)
- Moody's Rating business is more U.S. dominant, both in terms of % and dollar amount
- However, S&P Ratings has about 48% more total credit ratings outstanding than Moody's (2014), and thus about 40% more recurring revenue
- Their ratings businesses have similar revenues, but Moody's has higher operating margins, likely due to:
  - More U.S. business (dollar amount, and % amount: 61% versus S&P Ratings at 57%)
  - More transaction based (61% versus S&P Ratings at 46%)
  - Moody's being strong in some structured products categories
- It is likely than Moody's earnings will be more volatile than MHFI due to:
  - MHFI being more diversified, in terms of other businesses (C&C, DJ Indices), more recurring revenue, and the Ratings business less dominant in revenue and earnings as a total
  - MHFI has less transaction revenue, which is more cyclical
  - MHFI generates more revenue from outside the U.S.

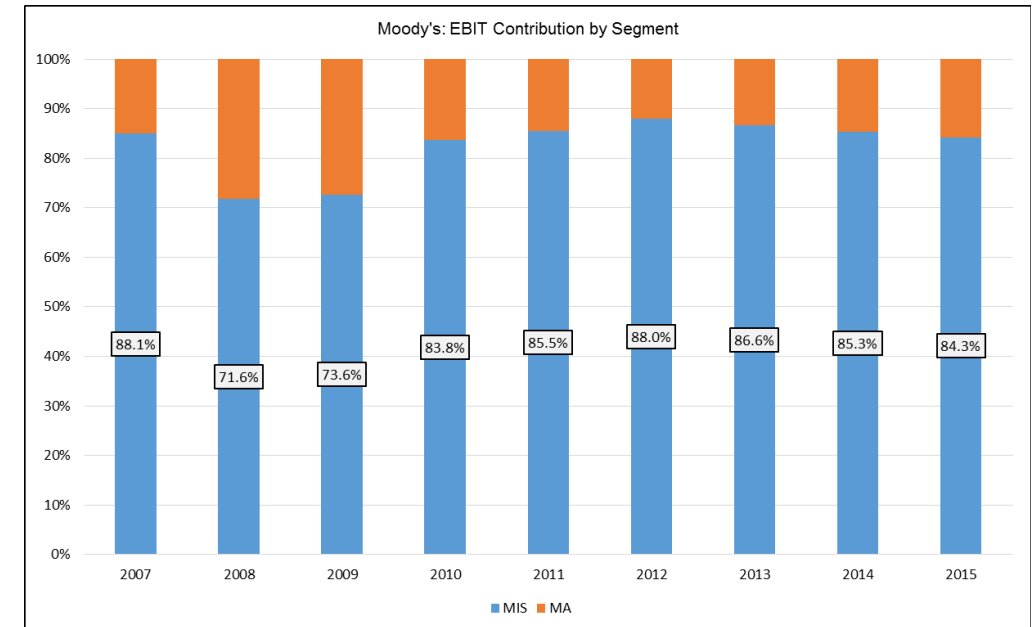
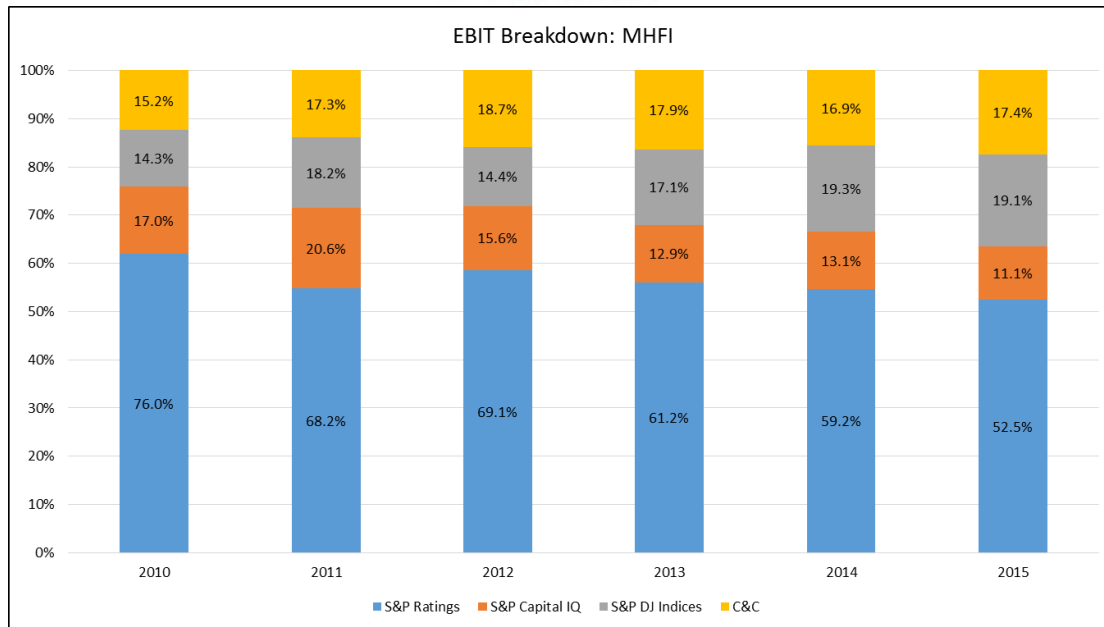
# Revenue by Segment

- MHFI has more revenue from *non-ratings business* (~55%), whereas most of Moody's revenue is from MIS (rating) at high-60%



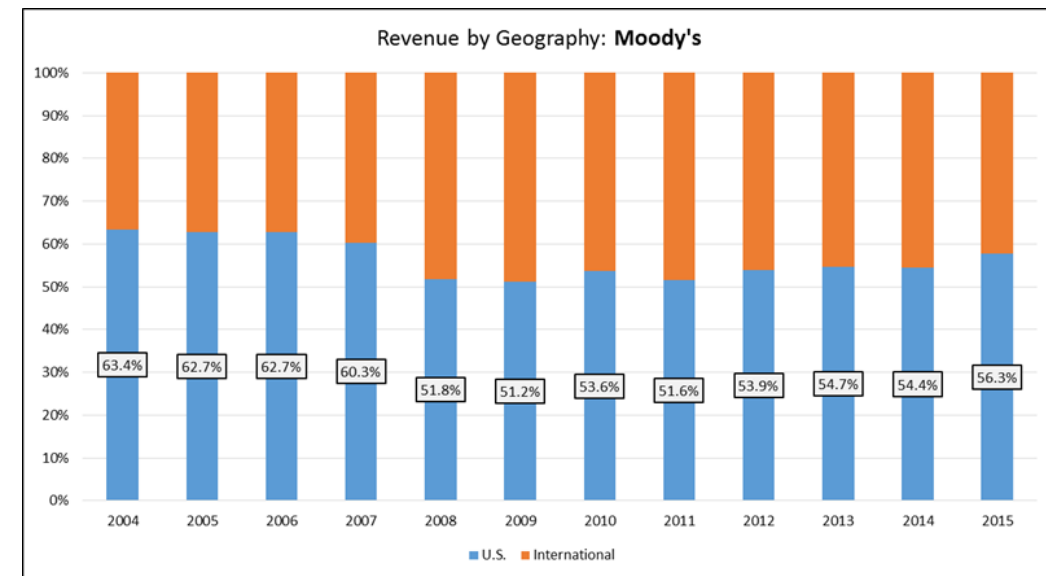
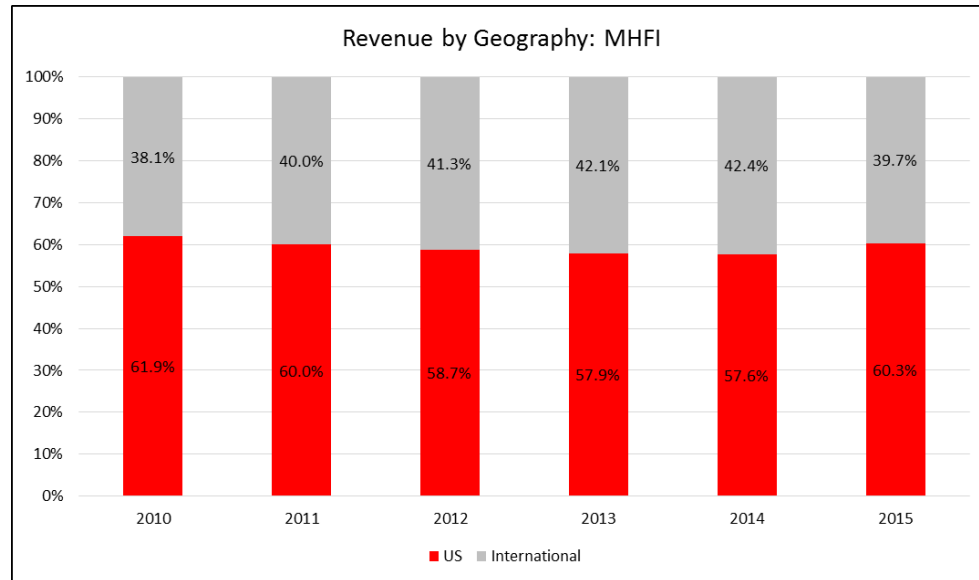
# EBIT Contribution by Segment

- MHFI's non-rating businesses (DJ Indices and C&C) have much higher margins, are different businesses than the traditional ratings + analytics businesses that only Moody's has
- These other businesses MHFI has contribute mid-30% of total MHFI operating income, and S&P ratings contributes only 50-60% of operating income
- Comparatively, Moody's only has the ratings & analytics business, and MIS contributes about mid-80% of total Moody's operating income
- MHFI is more diversified, Moody's is more of a pure-play ratings and analytics business



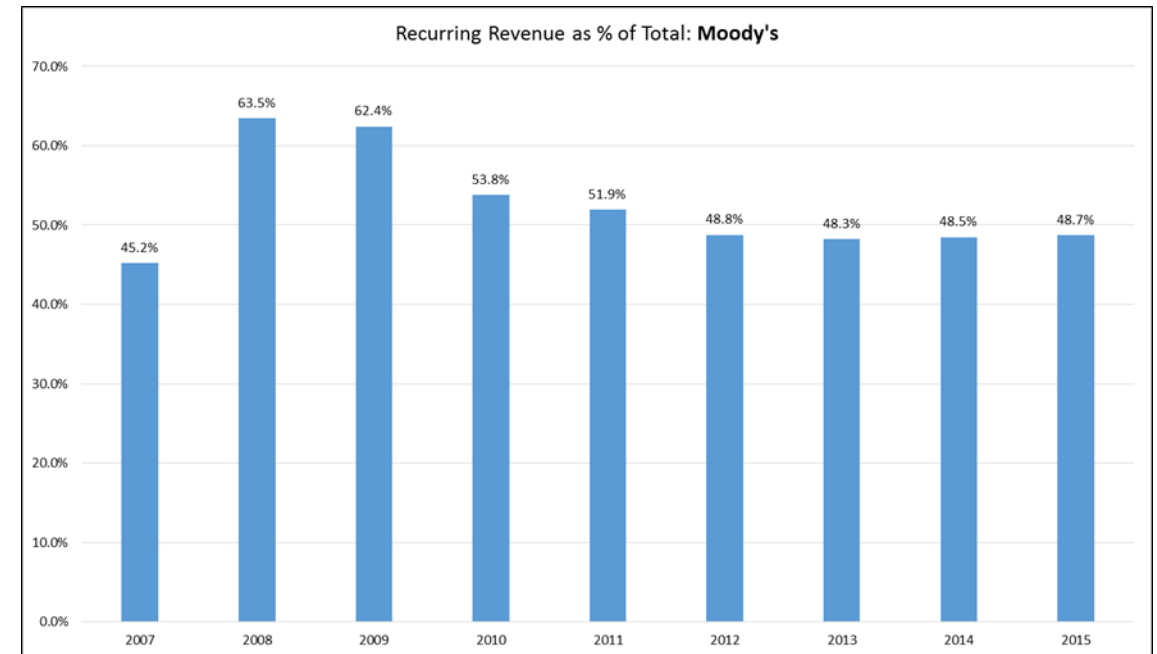
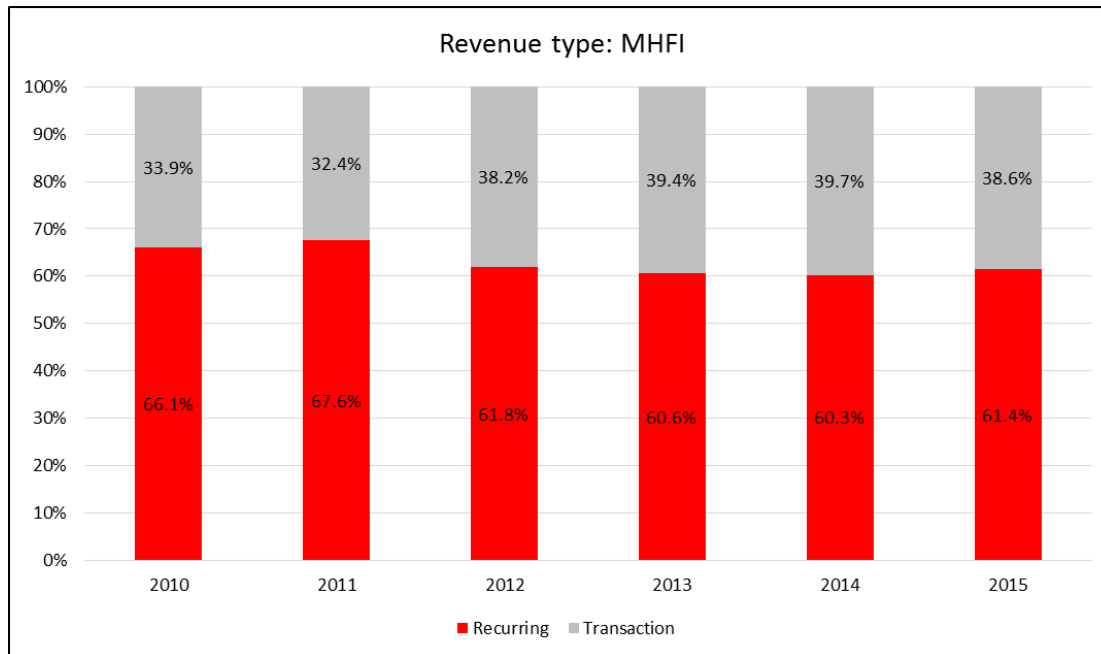
# Revenue by Geography

- MHFI has *more* revenue from U.S. (~60%) versus MCO with mid-low 50% of revenue from the U.S.



# Revenue by Type:

- MHFI has *more* revenue “recurring” at around 60-62% versus MCO at ~48-49%
- This will adjust based on only a couple of quarters of SNL revenue, likely more revenue recurring for MHFI



# Credit Rating Agency (CRA)

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Moody's Investor Service (MIS)  
S&P Ratings ("S&P")

*Note: Some of this is repetitive from the Moody's (MCO) Slide Deck*



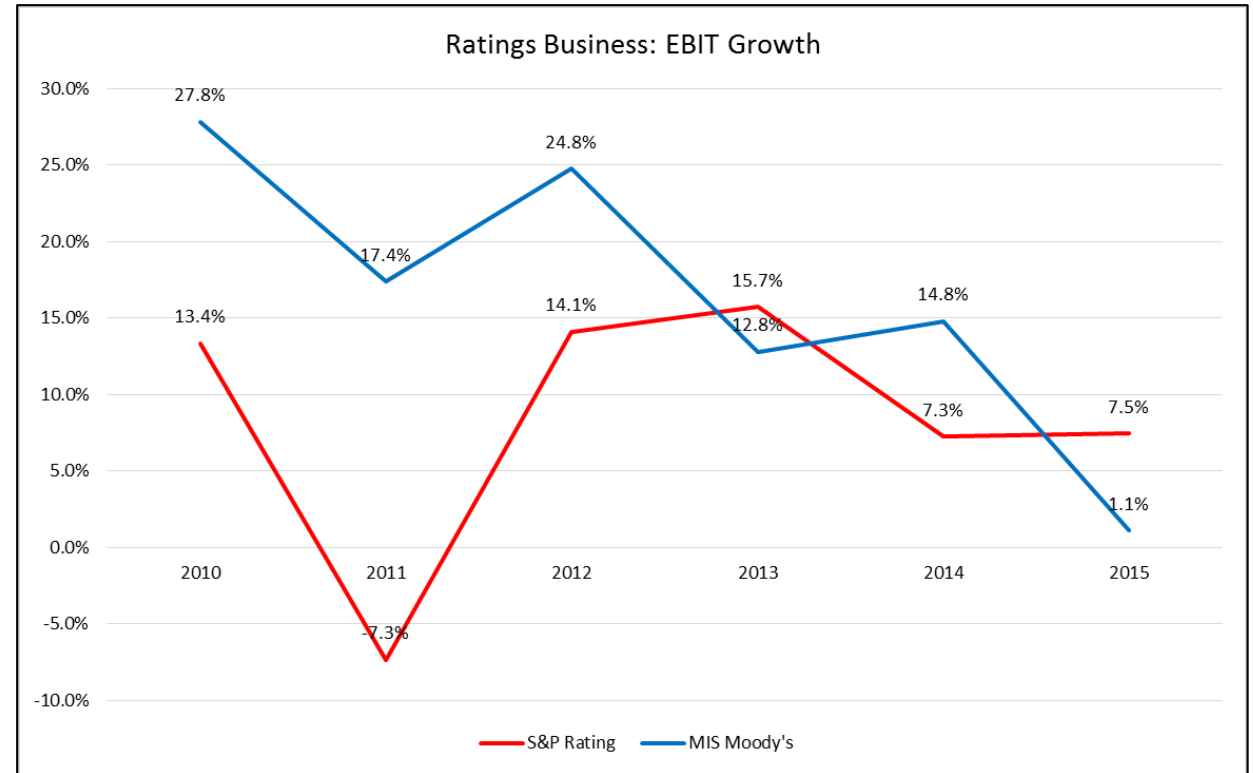
# Summary:

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- Moody's and S&P Ratings have similar revenue numbers, but Moody's Ratings (MIS) generates about 15% more cash flow than S&P Ratings
- Moody's is more transactional (61%) versus S&P Ratings (46%), which is a large contributor to why their margin profiles are different
- Moody's generates more revenue in the U.S. (~\$1.47 billion '15) than S&P Ratings (~\$1.39 billion in '15), and MCO's U.S. business is 61% of total, versus 57% for S&P Ratings
- Moody's consistently has a better margin profile (~ 51%) than S&P Ratings (~44%) but efficiency efforts by MHFI is improving their margin at a fast clip
- Both are winners globally – being #1 and #2 in most categories in new issuance and in total credit ratings outstanding
- Moody's earnings should be more cyclical, as it is more transaction-based

# Summary:

- When things are “strong” (economy, new issuance) then Moody’s Ratings business will grow at a much faster clip, as they are more transaction based (cyclical)
- Moody’s is also more tied to the U.S. economy
- As seen below, coming out of the GFC, Moody’s Ratings operating income grew much faster than S&P Ratings. Now that new issuance (and the economy) is slowing down, and there is more volatility and concern, S&P Ratings does better because they have more recurring business and can increase pricing on that book of business



# NRSRO (U.S.)

- NRSRO began in 1975 to reflect bank capital requirements being appropriately determined by credit rating agencies
- In the 1980s there were 7 NRSROs, which declined to 3 in the 1990s due to mergers
- NRSRO is essentially the U.S. government blessing that the credit rating agency is “official”
- Annual Reports required by the Credit Rating Agency Reform Act of 2006 and Dodd-Frank Act, discussing competition, market share, conflicts of interest
- Total of ten (10) NRSRO’s in the U.S. as of 2015 SEC Report

“While this information indicates the high percentage of outstanding ratings that continue to be issued by Moody’s, S&P, and Fitch, other information demonstrates *that smaller NRSROs have been able to make competitive inroads in certain rating categories.*” – 2015 SEC Annual Report on CRAs

## NRSRO’s as of 2015 SEC Annual Report on CRAs

NRSRO / Categories of Credit Ratings	Registration Date	Principal Office
A.M. Best Company, Inc. (“A.M. Best”) Categories (ii), (iii), and (iv)	September 24, 2007	U.S.
DBRS, Inc. (“DBRS”) Categories (i) through (v)	September 24, 2007	U.S.
Egan-Jones Ratings Company (“EJR”)⁵ Categories (i) through (iii)	December 21, 2007	U.S.
Fitch Ratings, Inc. (“Fitch”) Categories (i) through (v)	September 24, 2007	U.S.
HR Ratings de México, S.A. de C.V. (“HR Ratings”) Category (v)	November 5, 2012	Mexico
Japan Credit Rating Agency, Ltd. (“JCR”) Categories (i), (ii), (iii), and (v)	September 24, 2007	Japan
Kroll Bond Rating Agency, Inc. (“KBRA”) Categories (i) through (v)	February 11, 2008	U.S.
Moody’s Investors Service, Inc. (“Moody’s”) Categories (i) through (v)	September 24, 2007	U.S.
Morningstar Credit Ratings, LLC (“Morningstar”) Category (iv)	June 23, 2008	U.S.
Standard & Poor’s Ratings Services (“S&P”)⁶ Categories (i) through (v)	September 24, 2007	U.S.

# U.S. Market Share Leaders:

- In U.S., the “big three CRAs” issued *95.8% of all ratings* outstanding as of 12/2014, compared to 96.6% in 2013, and 98.8% from 2007 (year NRSROs began reporting)
- While the market share is largely dominated by the same CRAs – **S&P, Moody’s**, and Fitch – there has been some ***minor market share erosion*** over the last 7-8 years
- HHI Inverse has a concentration of 2.68 (If it were 3.0 then means concentration is equal to an industry where entire market evenly divided among three firms).

Chart 10: HHI Inverses for Each Rating Category

Year	Financial Institutions *	Insurance Companies **	Corporate Issuers**	Asset-Backed Securities *	Government Securities*	Total (all rating categories)	Total Excluding Government Securities
2008	3.72	4.05	3.79	2.82	2.83	2.99	3.56
2009	3.85	3.84	3.18	3.18	2.65	2.86	3.58
2010	3.99	3.37	3.17	3.20	2.69	2.88	3.55
2011	4.16	3.76	3.02	3.38	2.47	2.74	3.70
2012	4.04	3.72	3.00	3.44	2.50	2.75	3.68
2013	3.99	3.68	3.03	3.48	2.46	2.72	3.65
2014	4.30	3.83	3.35	3.34	2.40	2.68	3.81

\* Seven credit rating agencies are registered in this rating category. Therefore, the highest possible HHI Inverse (in a perfectly competitive market where all firms have an equal share of business) would be 7.0.

\*\* Eight credit rating agencies are registered in this rating category. Therefore, the highest possible HHI Inverse (in a perfectly competitive market where all firms have an equal share of business) would be 8.0.

Source: NRSRO annual certifications for the 2008-14 calendar years, Item 7A on Form NRSRO

Since 2008:

**More concentrated:**

- Insurance companies
- Corporate issuers
- Government securities
- Total

**Less Concentrated:**

- Financial institutions
- ABS

# U.S. Market Share Leader:

- In U.S., revenue numbers largely favor the top three – S&P, Moody's and Fitch – and that has not changed much, illustrating a continuation of market share dominance

**Chart 12: NRSRO Revenue Information Fiscal Year Percentage of Total Reported NRSRO Revenue**

	2011	2012	2013	2014
<b>S&amp;P, Fitch, and Moody's</b>	94.0%	94.7%	94.5%	94.3%
<b>All Other NRSROs</b>	6.0%	5.3%	5.5%	5.7%
<b>Total</b>	100.0%	100.0%	100.0%	100.0%

Source: Financial reports provided to the Commission under Rule 17g-3 for the fiscal years ended 2011-14

# Europe: Market Share

- Table to right is from ESMA on categories of credit ratings offered by registered CRAs in Europe
- Truly only four (4) comprehensive independent CRAs in Europe:
  - Moody's (MIS)
  - S&P
  - Fitch Ratings
  - DBRS Ratings Limited
- In reality, only Moody's, S&P, and Fitch are the predominant players in the space, with almost 90% share

	2011									2012									2013									2014									2015 (First Semester)															
CRA	FI	IN	CO	SV	SS	PE	SN	SF	CB	FI	IN	CO	SV	SS	PE	SN	SF	CB	FI	IN	CO	SV	SS	PE	SN	SF	CB	FI	IN	CO	SV	SS	PE	SN	SF	CB	FI	IN	CO	SV	SS	PE	SN	SF	CB							
AM Best Europe-Rating Services Ltd. (AMBERS)		IN	CO																																																	
ARC Ratings, S.A.			CO									CO																																								
ASSEKURATA Assekuranz Rating-Agentur GmbH																																																				
Axesor SA																																																				
BCRA-Credit Rating Agency AD		FI		IN	CO			SS				FI		IN	CO			SS					FI		IN	CO			SS																							
Capital Intelligence (Cyprus) Ltd		FI			CO		SV					FI			CO		SV						FI			CO		SV																								
CERVED Group S.p.A.				CO										CO												CO																										
Creditreform Rating AG				CO											CB			CO																																		
CRIF S.p.A.				CO												CO																																				
Dagong Europe Credit Rating Srl (Dagong Europe)																																																				
DBRS Ratings Limited		FI		IN	CO		SV	SS	PE			SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB
The Economist Intelligence Unit Ltd																																																				
Euler Hermes Rating GmbH		FI			CO																																															
European Rating Agency, a.s.																																																				
EuroRating Sp. z o.o.																																																				
Feri EuroRating Services AG																																																				
Fitch Ratings Limited		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH		FI			CO																																															
ICAP Group SA				CO																																																
INC Rating Sp. z o.o.																																																				
modeFinance S.r.l.																																																				
Moody's Investors Service Ltd		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB		FI		IN	CO		SV	SS	PE		SN	SF	CB
Rating-Agentur Expert RA GmbH																																																				
Scope Ratings AG				CO																																																

Legend:

FI	Corporate - Financial	PE	Public entities
IN	Corporate - Insurance	SN	Supranational
CO	Corporate - Non Financial	SF	Structured Finance
SV	Sovereign	CB	Covered Bonds
SS	Sub-sovereign		Non registered



# Europe: Market Share

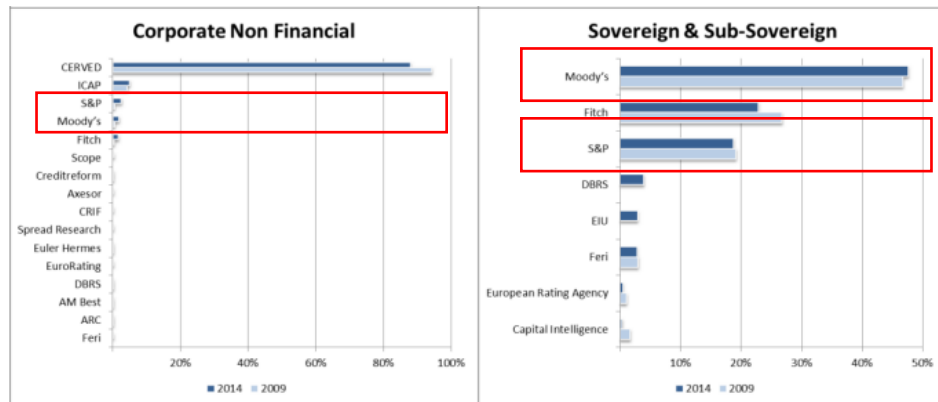
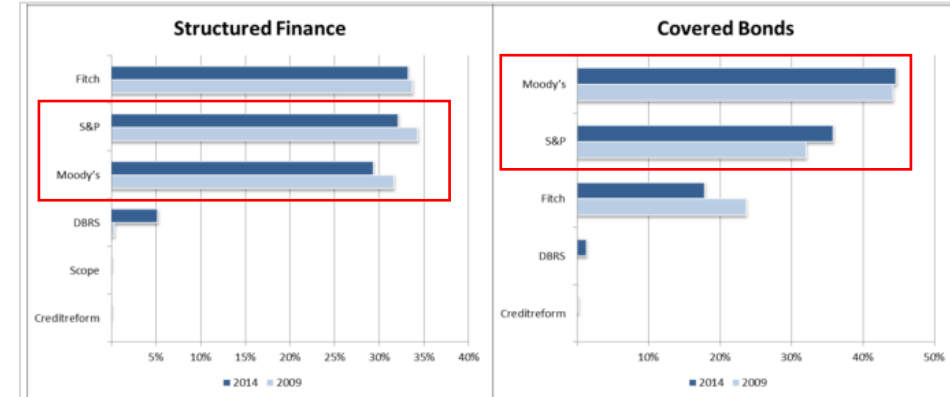
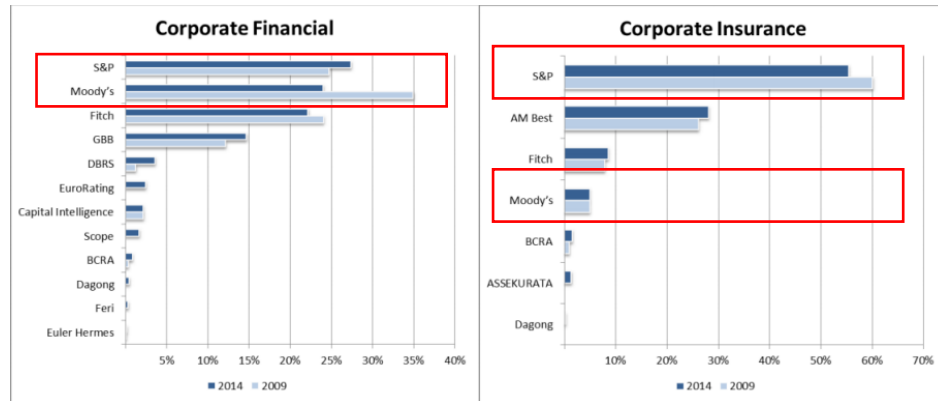
- Table to right is from ESMA on the market share of credit ratings offered by registered CRAs in Europe, using revenues
- Market Share:
  - S&P = 40.42%
  - Moody's Corp. = 34.67%
  - Fitch Group = 16.80%
  - All other: 8.11%

**Table 2: Market share calculation based on 2014 turnover from credit rating activities and ancillary services at group level in the EU**

Registered Credit Rating Agency	Market share
AM Best Europe-Rating Services Ltd. (AMBERS)	0.79%
ARC Ratings, S.A.	0.02%
ASSEKURATA Assekuranz Rating-Agentur GmbH	0.21%
Axesior S.A.	0.61%
BCRA-Credit Rating Agency AD	0.02%
Capital Intelligence (Cyprus) Ltd	0.12%
CERVED Group S.p.A.	1.20%
Creditreform Rating AG	0.50%
CRIF S.p.A.	0.33%
Dagong Europe Credit Rating Srl	0.02%
DBRS Ratings Limited	1.47%
Euler Hermes Rating GmbH	0.20%
European Rating Agency, a.s.	0.00%
EuroRating Sp. Zo.o.	0.00%
Feri EuroRating Services AG	0.64%
Fitch Group <sup>9</sup>	16.80%
GBB-Rating Gesellschaft für Bonitätsbeurteilung mbH	0.32%
ICAP Group SA	0.55%
INC Rating Sp. Zo.o. <sup>10</sup>	0.00%
ModeFinance S.A. <sup>11</sup>	0.00%
Moody's Group <sup>12</sup>	34.67%
Rating-Agentur Expert RA GmbH <sup>13</sup>	0.00%
Scope Credit Rating GmbH	0.14%
Spread Research SAS	0.11%
Standard & Poor's Group <sup>14</sup>	40.42%
The Economist Intelligence Unit Ltd	0.87%
<b>TOTAL</b>	<b>100</b>

Source: ESMA

# Europe: Market Share



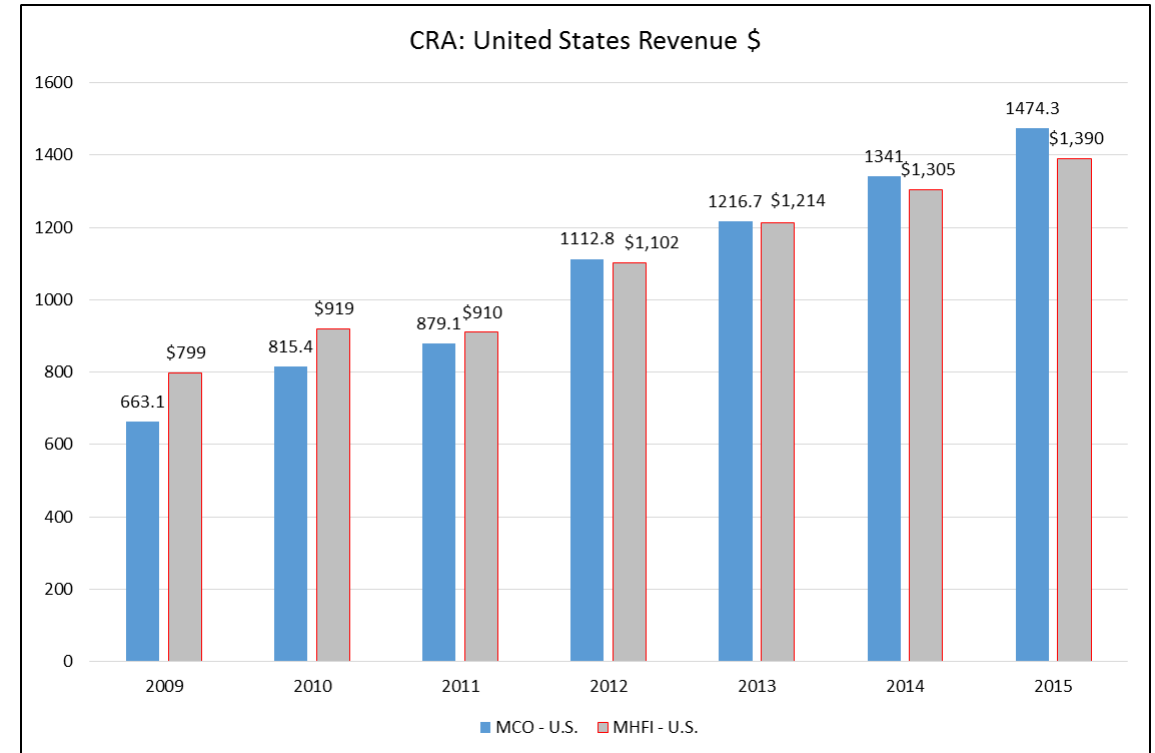
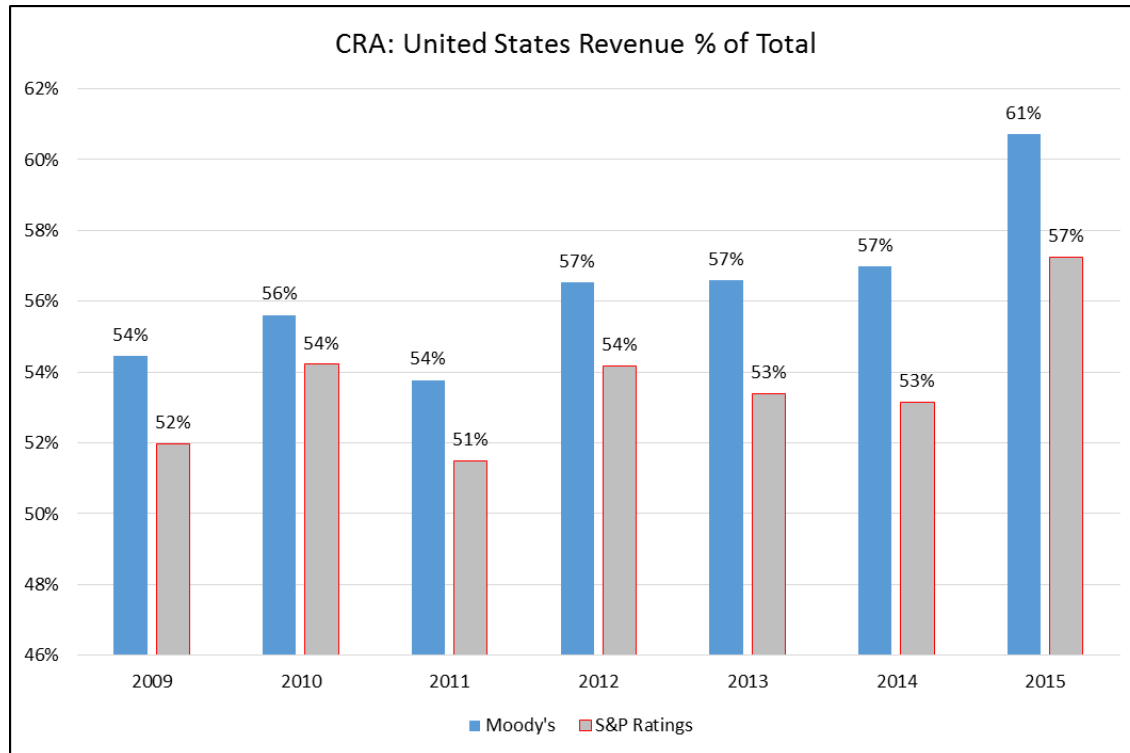
## Comments:

1. In each category in Europe, they are heavily dominated by 3 or fewer CRAs, which makes sense due to issuers "double checking" the rating and providing additional ratings information for investors to gain confidence
2. Moody's and S&P Ratings both in top 3 in 4 of the 6 categories
3. Moody's is #1 in two categories: covered bonds and sovereign & sub-sovereign.
4. S&P Ratings is #1 in two categories: Corporate Financial and Corporate Insurance



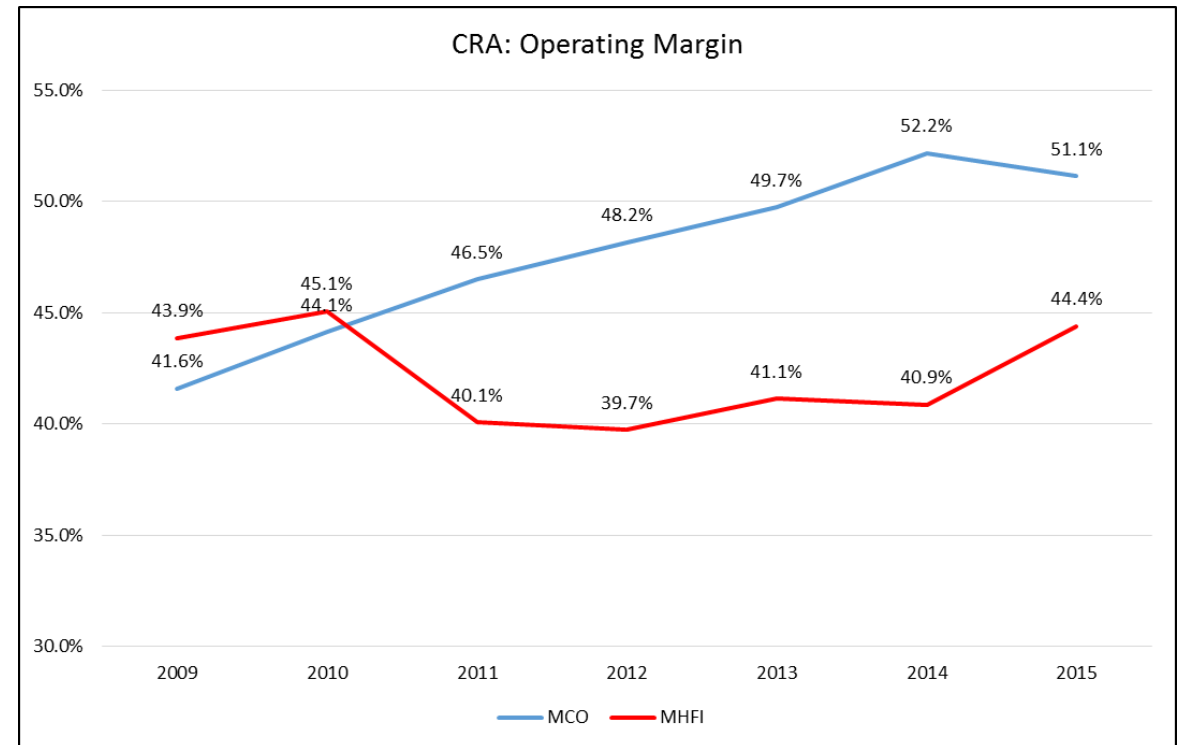
# Revenue by Geography:

- Moody's ratings business generates *more* revenues from the U.S., which is consistent each year
- Additionally, since 2012 Moody's generates more revenue in the U.S. than S&P Ratings
- Moody's rating business is more U.S. focused – they generate more revenue as a percentage from the U.S., and their business generates more revenue in absolute dollars



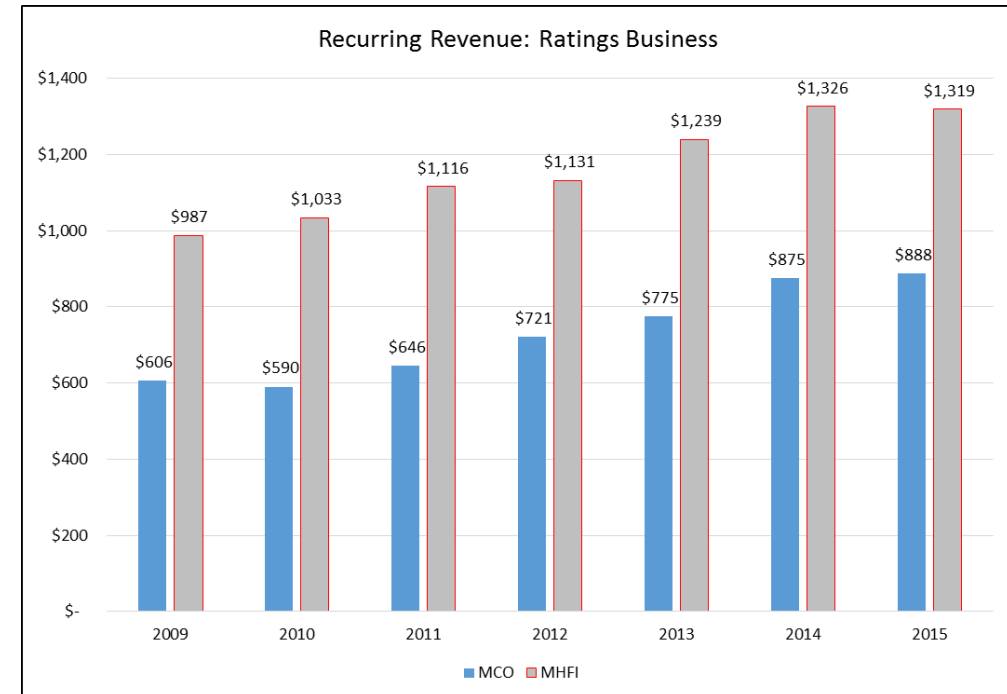
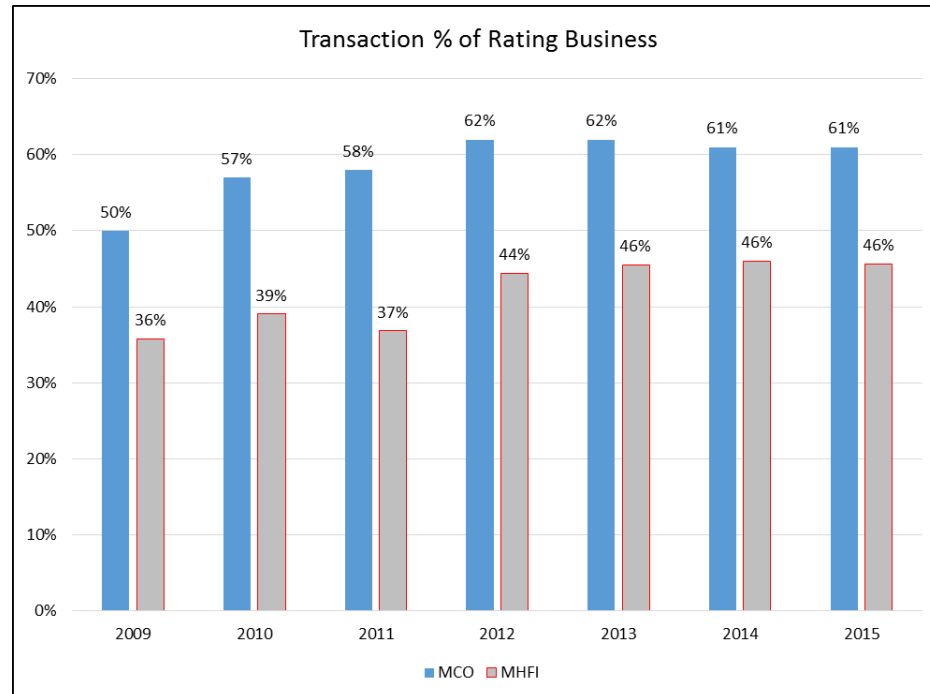
# Operating Margin: Moody's outperforms

- Moody's ratings business, since 2011, has handily outperformed S&P Ratings
- There are a number of potential reasons for this:
  - MCO has less international business, thus less FX exposure (more of a recent "issue")
  - MCO is more U.S. dominant, and the U.S. might have higher margins/pricing power than international
  - MCO is more dominant in certain categories that are higher margin, specifically structured products
  - MCO's management runs a "tighter ship" historically



# Recurring vs. Transaction

- S&P Ratings business has about 40% more outstanding credit ratings (end 2014) than Moody's, thus it makes sense S&P Ratings should have higher "recurring" revenue than Moody's with the amount of subscription/maintenance contracts from these ratings outstanding
- S&P Ratings had \$1.326 billion in recurring revenue in 2014, had 1,176,200 ratings outstanding
- Moody's had \$875 million in recurring revenue in 2014, had 841,419 ratings outstanding



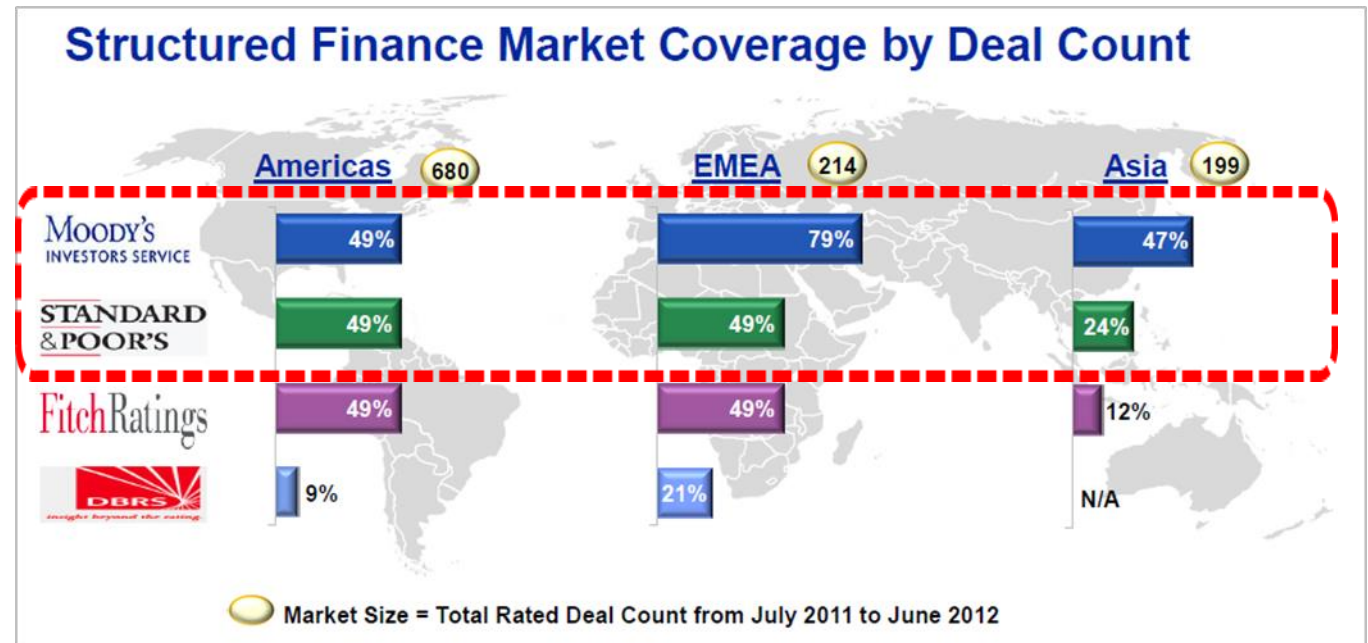
# More Ratings Outstanding = More Recurring Revenue = Lower Margins

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- S&P Ratings business has about 40% more outstanding credit ratings (end 2014) than Moody's and about 48% higher recurring revenues than Moody's
- This likely explains why Moody's has higher margins: transaction revenue is much higher margin than recurring revenue, but S&P still has a very large book of recurring business
- In addition, Moody's has more U.S. business (as a % and as dollar amount) versus S&P Ratings

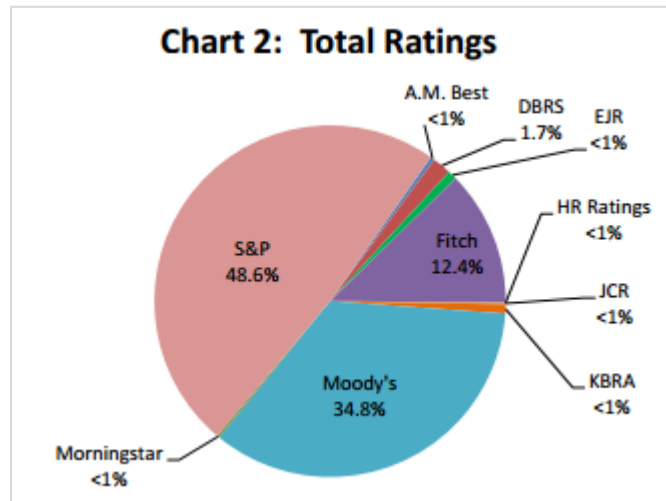
# Market Share: Structured Products

- Moody's ratings business and S&P Ratings (in 2012) had similar market shares in structured products in the Americas
- However, Moody's was much stronger internationally than S&P Ratings



# U.S. Market Share:

- In terms of outstanding credit ratings (end 2014), S&P Ratings is the leader with about 48.6% of the total ratings, versus Moody's at 34.8%



## 2015 SEC Annual Report on CRA's

**Chart 1: Number of Outstanding Credit Ratings as of December 31, 2014 by Rating Category\***

NRSRO	Financial Institutions	Insurance Companies	Corporate Issuers	Asset-Backed Securities	Government Securities	Total Ratings
A.M. Best	N/R	7,910	1,526	26	N/R	9,462
DBRS	10,176	147	3,732	11,497	16,650	42,202
EJR	11,956	1,025	7,013	N/R	N/R	19,994
Fitch	46,260	3,011	15,558	42,237	194,086	301,152
HR Ratings	N/R	N/R	N/R	N/R	277	277
JCR	807	57	2,206	N/R	399	3,469
KBRA	14,809	49	2,856	2,626	37	20,377
Moody's	52,049	3,336	41,364	71,504	673,166	841,419
Morningstar	N/R	N/R	N/R	5,542	N/R	5,542
S&P	61,000	6,800	53,000	85,200	970,200	1,176,200
<b>Total</b>	<b>197,057</b>	<b>22,335</b>	<b>127,255</b>	<b>218,632</b>	<b>1,854,815</b>	<b>2,420,094</b>

\*N/R indicates that the NRSRO is not registered for the rating category indicated.

Source: NRSRO annual certifications for the 2014 calendar year, Item 7A on Form NRSRO<sup>34</sup>

# MIS: Structured Finance - CMBS

- Moody's has much stronger U.S. and Global market share for CMBS (Collateralized Mortgage-Backed Securities)
- Moody's did about \$45 billion more CMBS business than S&P in 2015, which is almost 3x as much.
- Global Market Share
  - Moody's = 69.1% (#1)
  - S&P Ratings = 27.0% (#6)
- U.S. Market Share
  - Moody's = 70.8% (#1)
  - S&P Ratings = 25.6% (#6)

		2015 Issuance (\$Mil.)	No. of Deals	Market Share (%)	2014 Issuance (\$Mil.)	No. of Deals	Market Share (%)	'14-'15 % Chg.
<b>Global CMBS</b>								
1	Moody's	73,370.3	81	69.1	62,582.2	68	62.7	17.2
2	Kroll	58,557.6	70	55.1	53,790.1	65	53.9	8.9
3	Fitch	58,511.7	73	55.1	49,742.7	58	49.8	17.6
4	Morningstar	44,179.0	56	41.6	31,129.7	45	31.2	41.9
5	DBRS	31,003.2	44	29.2	40,807.0	52	40.9	-24.0
6	S&P	28,666.3	51	27.0	33,699.5	58	33.8	-14.9
	<b>TOTAL</b>	<b>106,210.9</b>	<b>174</b>	<b>100.0</b>	<b>99,838.0</b>	<b>148</b>	<b>100.0</b>	<b>6.4</b>

		2015 Issuance (\$Mil.)	No. of Deals	Market Share (%)	2014 Issuance (\$Mil.)	No. of Deals	Market Share (%)	'14-'15 % Chg.
<b>US CMBS</b>								
1	Moody's	71,525.7	77	70.8	62,036.7	66	65.9	15.3
2	Kroll	58,557.6	70	58.0	53,790.1	65	57.2	8.9
3	Fitch	55,720.2	67	55.2	45,406.6	48	48.3	22.7
4	Morningstar	44,179.0	56	43.7	31,129.7	45	33.1	41.9
5	DBRS	28,429.5	35	28.1	37,183.5	43	39.5	-23.5
6	S&P	25,900.9	43	25.6	31,614.2	53	33.6	-18.1
	<b>TOTAL</b>	<b>101,008.5</b>	<b>160</b>	<b>100.0</b>	<b>94,084.4</b>	<b>134</b>	<b>100.0</b>	<b>7.4</b>

# MIS: Structured Finance – ABS/MBS

- Moody's and S&P Ratings are **essentially equal** in total ABS and MBS business – with around \$130 billion in issuance in 2015
- S&P was much stronger in 2014 than Moody's, but *lost market share* to DBRS and Kroll, whereas Moody's maintained market share in 2015
- 2015 Market Share:
  - S&P Ratings = 54.0% (#1)
  - Moody's = 53.6% (#2)

		2015		Market	2014		Market	
ABS/MBS		Issuance (\$Mil.)	No. of Deals	Share (%)	Issuance (\$Mil.)	No. of Deals	Share (%)	'14-'15 % Chg.
1	S&P	132,022.1	222	54.0	158,760.4	268	65.5	-16.8
2	Moody's	130,886.7	203	53.6	130,329.6	178	53.8	0.4
3	Fitch	123,438.9	195	50.5	126,250.7	186	52.1	-2.2
4	DBRS	65,834.4	173	26.9	41,002.9	136	16.9	60.6
5	Kroll	28,462.5	85	11.6	23,739.3	59	9.8	19.9
6	Morningstar	11,903.3	25	4.9	6,751.1	12	2.8	76.3
7	A.M. Best	115.0	1	0.0	88.8	1	0.0	29.4
	TOTAL	244,361.2	483	100.0	242,253.2	449	100.0	0.9

		2015		Market	2014		Market	
ABS		Issuance (\$Mil.)	No. of Deals	Share (%)	Issuance (\$Mil.)	No. of Deals	Share (%)	'14-'15 % Chg.
1	S&P	128,651.4	212	60.3	149,757.0	241	67.9	-14.1
2	Moody's	123,620.2	182	57.9	129,352.5	175	58.7	-4.4
3	Fitch	115,824.6	169	54.2	121,224.8	170	55.0	-4.5
4	DBRS	44,913.1	97	21.0	24,557.7	65	11.1	82.9
5	Kroll	21,572.0	63	10.1	19,556.2	46	8.9	10.3
6	Morningstar	7,317.8	16	3.4	6,751.1	12	3.1	8.4
7	A.M. Best	115.0	1	0.1	88.8	1	0.0	29.4
	TOTAL	213,518.2	380	100.0	220,426.9	363	100.0	-3.1



Thank You. Feedback is Appreciated.

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Moody's Investor Service (MIS)  
S&P Ratings ("S&P")