



Moody's Corporation (MCO)

Updated February 20th, 2021 by Josh Arnold

Key Metrics

Current Price:	\$280	5 Year CAGR Estimate:	5.7%	Market Cap:	\$52 B
Fair Value Price:	\$251	5 Year Growth Estimate:	7.0%	Ex-Dividend Date:	02/24/21
% Fair Value:	112%	5 Year Valuation Multiple Estimate:	-2.2%	Dividend Payment Date:	03/18/21
Dividend Yield:	0.9%	5 Year Price Target	\$352	Years Of Dividend Growth:	12
Dividend Risk Score:	A	Retirement Suitability Score:	C	Last Dividend Increase:	10.7%

Overview & Current Events

Moody's was created back in 1909, becoming the first company to analyze securities and rate their investment quality for investors on a large scale. Moody's began with its *Analyses of Railroad Investments* in 1909 and has blossomed into the company we know today, with \$5.6 billion in annual revenue and a market capitalization of about \$52 billion.

Moody's is still one of the largest players in the traditional ratings business but has transformed itself in recent years by investing heavily in data and analytics, which is less cyclical and has very strong margins.

Moody's reported fourth quarter and full year earnings on February 12th, 2021 with results coming in mixed as revenue slightly beat estimates, but profits were light. Total revenue was \$1.3 billion for the quarter, up 5% from the year-ago period, but marking much slower growth than the full-year gain of 11%. Forex translation favorably impacted the top line by 2% in Q4, so organic growth was just 3%.

Operating expenses totaled \$846 million in Q4, up 16% from the same period a year ago. However, 11% of the 16% was attributable to severance and restructuring charges associated with the exit of real estate and strategic reorganization units and other one-time costs. In addition, forex translation unfavorably impacted operating expenses by -1% during the quarter, but organic expense growth was roughly in line with revenue growth.

Operating income came to \$531 million on an adjusted basis, down -5% from the year-ago period. Forex translation was a -3% headwind here, and adjusted operating margins came to 41.2% of revenue.

These factors combined to produce adjusted earnings-per-share of \$1.91 in Q4, down -5% year-over-year. For the full year, earnings-per-share soared from \$8.29 to \$10.15. We expect the massive growth seen in 2020 to be difficult to replicate this year and expect \$10.45 in earnings-per-share for 2021.

Moody's also raised its payout once again, this time increasing its payment 10.7% to a new annualized rate of \$2.48 per share, its 12th year of consecutive dividend increases.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$2.49	\$3.05	\$3.60	\$4.21	\$4.60	\$4.81	\$6.07	\$7.39	\$8.29	\$10.15	\$10.45	\$14.66
DPS	\$0.54	\$0.64	\$0.90	\$1.12	\$1.36	\$1.48	\$1.14	\$1.76	\$2.00	\$2.24	\$2.48	\$4.18
Shares¹	222	224	214	203	196	191	191	191	187	187	185	180

Moody's earnings-per-share history is quite strong as it has seen profit growth in every year in the past decade. Moody's earnings growth has averaged 15% per year over the last decade. While we do not believe that sort of performance is sustainable in the long run, we see 7% earnings-per-share growth moving forward.

Moody's can achieve this result by continuing its long tradition of buying growth, as we saw with the Bureau van Dijk purchase and the smaller purchases made in the years since, as well as a smaller amount of organic revenue growth. The company's operating costs have hampered earnings growth at times in the past as growing revenue at rapid rates can be expensive, and we believe this will continue to be the case moving forward. Indeed, some of this was present in Q4

¹ Share count in millions

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results. However, longer term tailwinds are in place for Moody's as it continues to feed seemingly insatiable investor demand for real-time analytical data on a wide variety of global securities. Keep in mind the core US business is growing slowly and as such, Moody's relies almost entirely upon the global business for expansion, exposing it to currency risk over time as well. This, too, was seen in Q4 results with a big headwind from forex translation.

We see the dividend as growing at roughly the same rate as earnings-per-share and we are forecasting a payout of \$4.18 in five years. Moody's has not shown the dividend to be a priority, as it is instead focused on business growth.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	13.5	13.5	17.5	20.8	22.3	20.4	20.6	22.3	23.7	26.1	26.8	24.0
Avg. Yld.	1.6%	1.6%	1.4%	1.3%	1.3%	1.5%	0.9%	1.1%	1.0%	0.8%	0.9%	1.2%

The valuation for Moody's has moved around significantly in the past decade after hitting its lowest point in 2011 at 13.5. Today's price-to-earnings ratio of 26.8 is in excess of our estimate of fair value at 24, meaning it still looks somewhat overpriced despite the flat price action from our last report. That implies a modest headwind to annual returns from the valuation declining over time. We see the combination of a higher payout and lower valuation sending the yield up to 1.2% over time from the current 0.9%.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	22%	22%	26%	23%	29%	30%	25%	24%	24%	22%	24%	29%

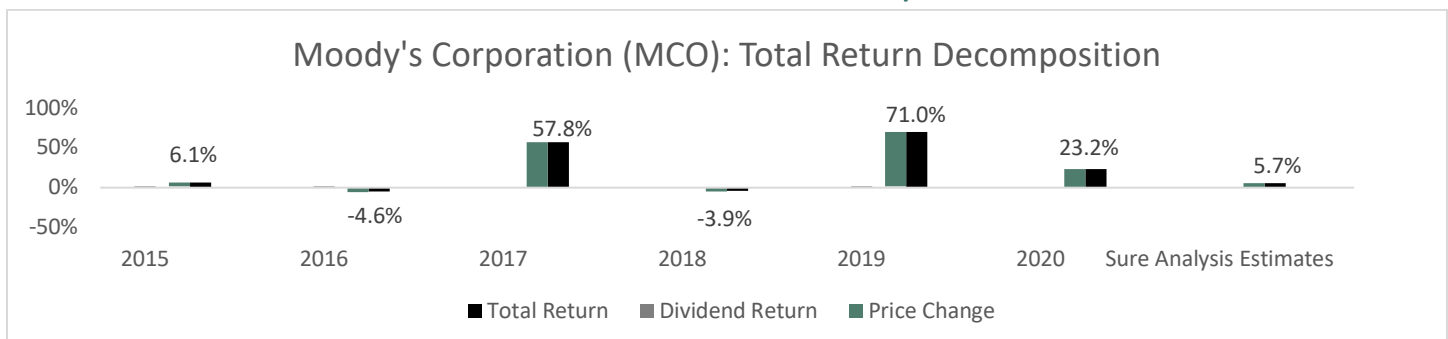
Moody's payout ratio is just one-quarter of earnings, which is in-line with its historical norms. We do not believe that will change materially in the years to come as the company continues to grow earnings rapidly, and as it focuses on growth more than a high dividend yield.

Moody's competitive advantage is that it was the company that basically created the industry more than 100 years ago. Its recent acquisitions and internal product advancements have kept it relevant with data-hungry investors. Moody's product assortment is strong at a time when competition is tougher than ever, and we think that will serve Moody's well during future recessions, which should not crimp earnings unduly.

Final Thoughts & Recommendation

Overall, Moody's looks like a strong growth story that is still overvalued despite the stock having essentially not moved since our last update. We are forecasting 5.7% in total annual returns moving forward, consisting of the 0.9% current yield, 7% earnings-per-share growth and a headwind from a lower valuation. Moody's looks well-positioned for further growth, but the valuation is still a concern. We reiterate the stock at a hold rating following 2020 results.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	2,281	2,730	2,973	3,334	3,485	3,604	4,204	4,443	4,829	5,371
Gross Profit	1,597	1,935	2,150	2,404	2,508	2,585	2,988	3,197	3,442	3,896
Gross Margin	70.0%	70.9%	72.3%	72.1%	72.0%	71.7%	71.1%	72.0%	71.3%	72.5%
SG&A Exp.	630	752	822	869	921	931	986	1,080	1,167	1,229
D&A Exp.	79	94	93	96	114	127	158	192	200	---
Operating Profit	895	1,102	1,254	1,446	1,480	1,528	1,844	1,925	2,075	2,447
Op. Margin	39.2%	40.4%	42.2%	43.4%	42.5%	42.4%	43.9%	43.3%	43.0%	45.6%
Net Profit	571	690	805	989	941	267	1,001	1,310	1,422	1,778
Net Margin	25.1%	25.3%	27.1%	29.7%	27.0%	7.4%	23.8%	29.5%	29.4%	33.1%
Free Cash Flow	736	778	885	944	1,109	1,144	664	1,370	1,606	2,146
Income Tax	262	324	353	455	430	282	779	352	381	452

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	2,876	3,961	4,395	4,669	5,103	5,327	8,594	9,526	10,265	12,409
Cash & Equivalents	760	1,755	1,920	1,220	1,757	2,052	1,072	1,685	1,832	2,597
Acc. Receivable	490	622	694	792	802	887	1,147	1,287	1,419	---
Goodwill & Int.	897	864	887	1,367	1,275	1,320	5,385	5,347	5,220	---
Total Liabilities	3,035	3,564	4,047	4,626	5,436	6,355	8,709	8,870	9,434	10,646
Accounts Payable	16	14	16	19	22	28	22	30	38	---
Long-Term Debt	1,244	1,671	2,102	2,547	3,381	3,363	5,541	5,676	5,581	---
Total Equity	-169	385	337	-188	-565	-1,225	-328	459	612	1,763
D/E Ratio	-7.36	4.34	6.24	-13.56	-5.98	-2.75	-16.91	12.37	9.12	---

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	21.1%	20.2%	19.3%	21.8%	19.3%	5.1%	14.4%	14.5%	14.4%	15.7%
Return on Equity	-239%	638%	223%	1325%	-250%	-29.8%	-129%	---	266%	150%
ROIC	56.4%	43.8%	35.6%	39.2%	33.4%	9.9%	25.8%	---	22.3%	43.5%
Shares Out.	222	224	214	203	196	191	191	191	187	187
Revenue/Share	9.94	12.05	13.30	15.53	17.13	18.45	21.65	22.85	25.20	28.37
FCF/Share	3.21	3.43	3.96	4.40	5.45	5.85	3.38	7.05	8.38	11.34

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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