



# CME Group Inc. (CME)

Updated November 15<sup>th</sup>, 2022 by Samuel Smith

## Key Metrics

|                             |         |                                            |       |                                  |                       |
|-----------------------------|---------|--------------------------------------------|-------|----------------------------------|-----------------------|
| <b>Current Price:</b>       | \$173.9 | <b>5 Year CAGR Estimate:</b>               | 4.9%  | <b>Market Cap:</b>               | \$62.3 B              |
| <b>Fair Value Price:</b>    | \$159.6 | <b>5 Year Growth Estimate:</b>             | 4.4%  | <b>Ex-Dividend Date:</b>         | 12/09/22 <sup>1</sup> |
| <b>% Fair Value:</b>        | 109%    | <b>5 Year Valuation Multiple Estimate:</b> | -1.7% | <b>Dividend Payment Date:</b>    | 12/27/22 <sup>2</sup> |
| <b>Dividend Yield:</b>      | 2.3%    | <b>5 Year Price Target</b>                 | \$198 | <b>Years Of Dividend Growth:</b> | 17                    |
| <b>Dividend Risk Score:</b> | D       | <b>Retirement Suitability Score:</b>       | D     | <b>Rating:</b>                   | Hold                  |

## Overview & Current Events

CME Group is a Chicago-based company that operates futures and derivatives exchanges based on interest rates, equities, currencies, and commodities. The company was founded in 1898 but didn't IPO until 2002. Since then, CME Group has pursued industry consolidation through mergers (CBOT Holdings) and acquisitions (Nymex Holdings). It currently generates about \$4.7 billion in annual revenue.

CME Group reported third quarter earnings on October 26<sup>th</sup>, 2022. The company reported revenue of \$1.2 billion and operating income of \$739 million for the third quarter of 2022. Net income was \$680 million and diluted earnings per share were \$1.87. On an adjusted basis, net income was \$719 million and diluted earnings per share were \$1.98.

## Growth On A Per-Share Basis

| Year                      | 2012   | 2013   | 2014   | 2015   | 2016   | 2017    | 2018   | 2019   | 2020   | 2021   | 2022          | 2027          |
|---------------------------|--------|--------|--------|--------|--------|---------|--------|--------|--------|--------|---------------|---------------|
| <b>EPS</b>                | \$2.70 | \$2.92 | \$3.35 | \$3.69 | \$4.53 | \$11.94 | \$5.71 | \$6.85 | \$6.72 | \$6.67 | <b>\$7.98</b> | <b>\$9.90</b> |
| <b>DPS</b>                | \$1.79 | \$1.80 | \$1.88 | \$2.00 | \$2.40 | \$2.64  | \$2.80 | \$3.00 | \$3.40 | \$3.60 | <b>\$4.00</b> | <b>\$5.00</b> |
| <b>Shares<sup>3</sup></b> | 333.6  | 335.7  | 337.3  | 338.4  | 339.7  | 340.4   | 357.8  | 358.4  | 359.0  | 358.6  | <b>359.7</b>  | <b>360.0</b>  |

Looking ahead we anticipate 4.4% average annual earnings per share growth over the next half decade. The main tailwind for the company is volatility in the public markets for the foreseeable future as there remains enormous uncertainty on how various trade, geopolitical, global growth, and interest rate scenarios will play out to direct the near-term future of the American and global economies.

Additionally, we expect CME to harvest significant synergies from its acquisition of Nymex Holdings, as their product offerings overlap nicely and enhance the overall competitive positioning of the firm. Finally, we see the company's extensive network and large volume enabling it to drive growth through starting ancillary services and exchange products, as well as sell order flow data to third parties. As a result, we expect CME Group to continue growing earnings-per-share at a slow but steady clip for the foreseeable future.

## Valuation Analysis

| Year             | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  | Now         | 2027        |
|------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------------|-------------|
| <b>Avg. P/E</b>  | 11.9  | 18.3  | 17.6  | 23.3  | 24.2  | 19.6  | 9.7   | 25.6  | 24.7  | 32.8  | <b>21.8</b> | <b>20.0</b> |
| <b>Avg. Yld.</b> | 5.60% | 3.40% | 3.20% | 2.30% | 2.20% | 1.10% | 5.10% | 1.70% | 2.00% | 1.70% | <b>2.3%</b> | <b>2.5%</b> |

CME Group's average price to earnings multiple of over the past decade is roughly in-line with where it is today, with the stock currently trading at 21.8 times expected 2022 earnings. We believe that, while the market is experiencing near term expectations of continued increases in volatility to drive growth in earnings, over the next several years growth will slow considerably. As a result, we are maintaining our fair value estimate of 20x earnings and believe the stock is slightly overvalued at present.

<sup>1</sup> Estimate

<sup>2</sup> Estimate

<sup>3</sup> In millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year   | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2027 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 66%  | 62%  | 56%  | 54%  | 53%  | 22%  | 49%  | 44%  | 51%  | 54%  | 50%  | 51%  |

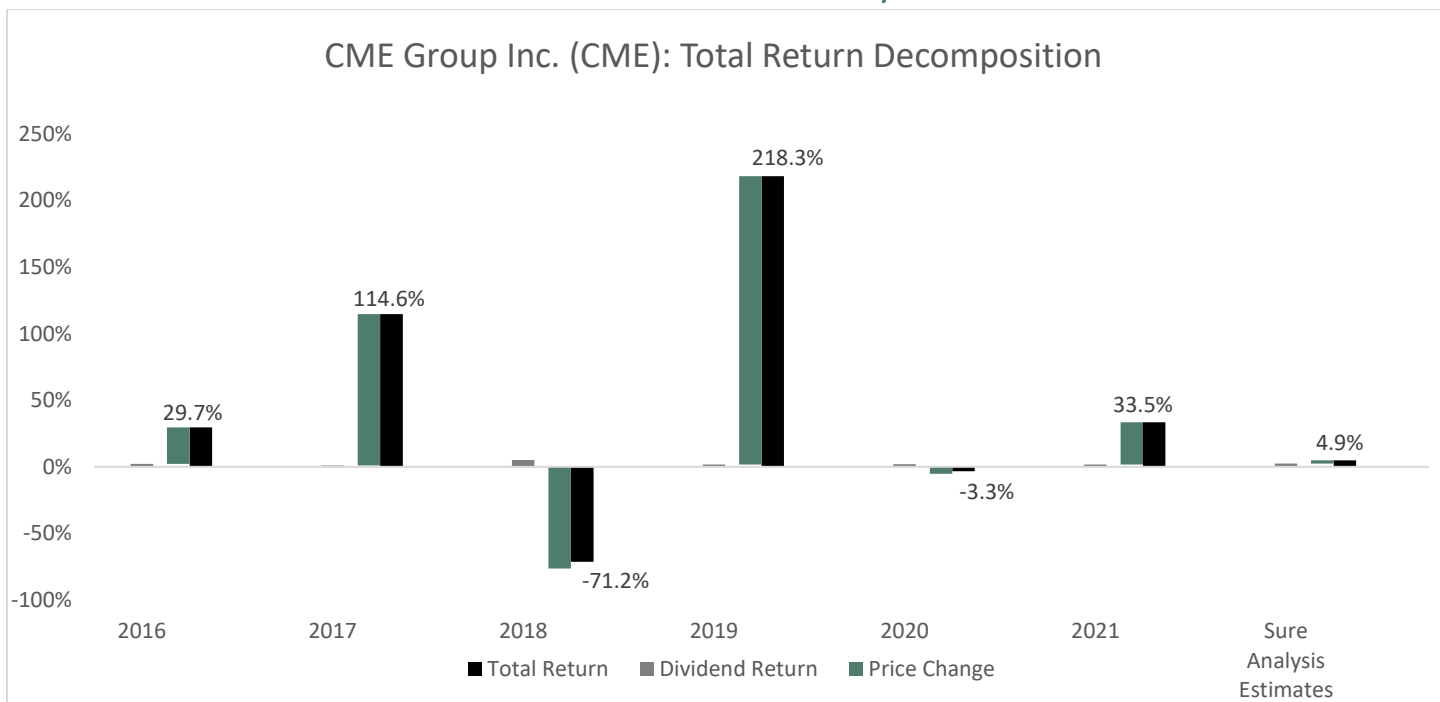
CME Group's biggest competitive advantage is its network effect as a consolidator in the financial exchange space. Thanks to its large volume, it offers customers considerable liquidity, which is an extremely attractive feature for this industry. The company's large volume also gives it economies of scale, enabling it to offer competitive pricing without considerably hurting profitability. This not only enables the company to retain customers, but also attracts new ones. As its customer count grows, its network effect only grows stronger, which in turn drives further liquidity and cost advantages, resulting in a virtuous cycle. Given that more than half of all interest rate-related futures in the world and nearly all North American interest rate-related futures are traded on the company's exchanges, it is clear that the company has established a dominant network effect in its core business.

While the company is not directly impacted by changes in stock market valuations, it did suffer during the last recession due to depressed market sentiment and customer bankruptcies, dramatically reducing activity on the exchanges. From peak to trough, CME Group's trailing twelve-month earnings per share fell from ~\$3.45 in mid-2008 to \$2.40 in mid-2009. The biggest long-term risk to the company is the potential for new regulation to disrupt the company's business model, which could break up its exchange and clearing operations or even limit the volatility on the exchanges or its pricing power. However, we do not see any threat developing in the near future, making the business fairly low-risk from a long-term perspective.

## Final Thoughts & Recommendation

CME Group benefits from increased volatility. Given the increasing geo-political and macroeconomic uncertainties in the world today, this could bode well for the business. At the same time, the valuation currently stands at a slight premium. As a result, with a 4.9% expected annualized return over the next half decade, we rate shares as a Hold.

## Total Return Breakdown by Year



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## Income Statement Metrics

| Year             | 2012  | 2013  | 2014  | 2015  | 2016  | 2017    | 2018  | 2019  | 2020  | 2021  |
|------------------|-------|-------|-------|-------|-------|---------|-------|-------|-------|-------|
| Revenue          | 2,915 | 2,936 | 3,113 | 3,327 | 3,595 | 3,645   | 4,309 | 4,868 | 4,884 | 4,690 |
| Gross Profit     | 2,378 | 2,382 | 2,528 | 2,745 | 3,052 | 3,081   | 3,637 | 3,969 | 4,027 | 3,853 |
| Gross Margin     | 81.6% | 81.1% | 81.2% | 82.5% | 84.9% | 84.5%   | 84.4% | 81.5% | 82.5% | 82.2% |
| SG&A Exp.        | 337   | 360   | 398   | 404   | 378   | 366     | 454   | 548   | 635   | 581   |
| D&A Exp.         | 253   | 238   | 233   | 229   | 225   | 209     | 249   | 473   | 464   | 385   |
| Operating Profit | 1,692 | 1,637 | 1,768 | 1,989 | 2,201 | 2,311   | 2,608 | 2,588 | 2,637 | 2,645 |
| Operating Margin | 58.1% | 55.8% | 56.8% | 59.8% | 61.2% | 63.4%   | 60.5% | 53.2% | 54.0% | 56.4% |
| Net Profit       | 896   | 977   | 1,127 | 1,247 | 1,534 | 4,063   | 1,962 | 2,117 | 2,105 | 2,636 |
| Net Margin       | 30.8% | 33.3% | 36.2% | 37.5% | 42.7% | 111.5%  | 45.5% | 43.5% | 43.1% | 56.2% |
| Free Cash Flow   | 1,078 | 1,155 | 1,151 | 1,418 | 1,640 | 1,669   | 2,324 | 2,427 | 2,518 | 2,275 |
| Income Tax       | 787   | 623   | 645   | 710   | 754   | (1,537) | 814   | 574   | 616   | 737   |

## Balance Sheet Metrics

| Year                 | 2012   | 2013   | 2014   | 2015   | 2016   | 2017   | 2018   | 2019   | 2020    | 2021    |
|----------------------|--------|--------|--------|--------|--------|--------|--------|--------|---------|---------|
| Total Assets         | 38,863 | 54,278 | 72,242 | 67,359 | 69,369 | 75,791 | 77,476 | 75,215 | 124,660 | 196,780 |
| Cash & Equivalents   | 1,605  | 2,470  | 1,366  | 1,693  | 1,869  | 1,904  | 1,375  | 1,551  | 1,633   | 2,835   |
| Accounts Receivable  | 268    | 303    | 341    | 358    | 364    | 360    | 553    | 492    | 461     | 435     |
| Goodwill & Int. Ass. | 27,596 | 27,486 | 27,382 | 27,282 | 27,186 | 27,091 | 33,481 | 33,036 | 32,839  | 31,235  |
| Total Liabilities    | 17,438 | 33,117 | 51,318 | 46,808 | 49,029 | 53,379 | 51,510 | 49,056 | 98,308  | 169,381 |
| Accounts Payable     | 42     | 36     | 37     | 29     | 26     | 31     | 116    | 62     | 69      | 49      |
| Long-Term Debt       | 2,857  | 2,857  | 2,108  | 2,229  | 2,231  | 2,233  | 4,401  | 3,743  | 3,444   | 3,445   |
| Shareholder's Equity | 21,419 | 21,155 | 20,924 | 20,552 | 20,341 | 22,412 | 25,919 | 26,129 | 26,320  | 27,399  |
| LTD/E Ratio          | 0.13   | 0.14   | 0.10   | 0.11   | 0.11   | 0.10   | 0.17   | 0.14   | 0.13    | 0.13    |

## Profitability & Per Share Metrics

| Year             | 2012  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  |
|------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Return on Assets | 2.3%  | 2.1%  | 1.8%  | 1.8%  | 2.2%  | 5.6%  | 2.6%  | 2.8%  | 2.1%  | 1.6%  |
| Return on Equity | 4.2%  | 4.6%  | 5.4%  | 6.0%  | 7.5%  | 19.0% | 8.1%  | 8.1%  | 8.0%  | 9.8%  |
| ROIC             | 3.7%  | 4.0%  | 4.8%  | 5.4%  | 6.8%  | 17.2% | 7.1%  | 7.0%  | 7.1%  | 8.7%  |
| Shares Out.      | 333.6 | 335.7 | 337.3 | 338.4 | 339.7 | 340.4 | 357.8 | 358.4 | 359.0 | 358.6 |
| Revenue/Share    | 8.77  | 8.78  | 9.26  | 9.85  | 10.61 | 10.71 | 12.54 | 13.59 | 13.62 | 13.07 |
| FCF/Share        | 3.24  | 3.45  | 3.42  | 4.20  | 4.84  | 4.91  | 6.76  | 6.78  | 7.02  | 6.34  |

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

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