



McGraw Hill Financial
4th Quarter and Full-Year 2014 Earnings Conference Call
Prepared Remarks
February 12, 2015

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Vice President, Investor Relations
McGraw Hill Financial

Good morning. Thank you for joining us for McGraw Hill Financial's fourth quarter and full-year 2014 earnings call. Presenting on this morning's call are Doug Peterson, President and CEO, and Jack Callahan, Chief Financial Officer.

This morning we issued a news release with our results. I trust you have all had a chance to review the release. If you need a copy of the release and financial schedules, they can be downloaded at www.mhfi.com.

In today's earnings release and during the conference call we're providing adjusted financial information. This information is provided to enable investors to make meaningful comparisons of the Corporation's operating performance between periods and to view the Corporation's business from the same perspective as management's. The earnings release contains exhibits that reconcile the difference between the non-GAAP measures and the comparable financial measures, calculated in accordance with U.S. GAAP.

Before we begin, I need to provide certain cautionary remarks about forward-looking statements. Except for historical information, the matters discussed on the teleconference may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including projections, estimates, and descriptions of future events. Any such statements are based on current expectations and current economic conditions and are subject to risks and uncertainties that may cause actual results to differ materially from results anticipated in these forward-looking statements. In this regard, we direct listeners to the cautionary statements contained in our Form 10-K, 10-Q, and other periodic reports filed with the U.S. Securities and Exchange Commission.

I would also like to call your attention to a recent European regulation. Any investor who has, or expects to obtain, ownership of 5% or more of McGraw Hill Financial should give me a call to better understand the impact of this legislation on the investor, and potentially the Company.

We're aware that we do have some media representatives with us on the call. However, this call is intended for investors and we would ask that questions from the media be directed to Jason Feuchtwanger in our New York office at (212) 512-3151.

At this time, I'd like to turn the call over to Doug Peterson.



Douglas L. Peterson
President and CEO
McGraw Hill Financial

Thank you, Chip. Good morning everyone and welcome to the call.

At the beginning of 2014, during our Investor Day on March 18th, we laid out our vision for creating growth and driving performance at McGraw Hill Financial – and, as your can see, we’ve made great progress.

We completed the rationalization of all of our media assets with the sale of McGraw Hill Construction.

We also resolved significant legal and regulatory matters. While these settlements resulted in a meaningful loss of net income for the quarter, our businesses are performing very well. Our adjusted results, which are the basis that we use to manage our Company, show just how well these businesses are doing.

Despite the headwinds of a strong U.S. dollar and collapsing oil prices, in 2014 the Company achieved 7% growth in revenue from continuing operations as clients around the world increasingly seek the essential intelligence we provide. Importantly, every business unit delivered top-line growth and margin improvement.

The Company also delivered a 280 basis-point improvement in adjusted operating profit margin. The combination of increased revenue and improved profitability led to the generation of more than \$1.0 billion in free cash flow for the year.

We also added talented leaders to the management team. Imogen Dillon Hatcher was named President of S&P Capital IQ and Lucy Fato appointed Executive Vice President and General Counsel. These are capable leaders who are already making a difference.

One of the most significant developments in the quarter was the resolution of legal and regulatory matters with:

- The Department of Justice and the Attorneys General of 19 states and the District of Columbia;
- CalPERS, relating to three structured investment vehicles;
- The U.S. Securities and Exchange Commission and the Attorneys General of New York and Massachusetts; and
- Several private litigations stemming from the financial crisis.

As a result of these settlements, we recorded a fourth quarter charge of \$1.552 billion.

Now let me provide more color on our 2014 accomplishments. During 2014, we expanded our global footprint and reach:

- Platts acquired Eclipse and relocated its head office to London;
- Standard & Poor’s Ratings Services acquired BRC Investor Services in Colombia;
- S&P Capital IQ added private company financial data for scores of Australian, Brazilian, and Indian companies;

- S&P Dow Jones Indices continued to partner with important exchanges around the world reaching or expanding agreements with Bolsa de Valores de Lima, Bolsa Mexicana de Valores, BM&F Bovespa, and the Korea Exchange; and
- J.D. Power launched financial services offerings in Southeast Asia and Australia as well as a digital automotive retail performance improvement platform in China.

As we look at the Company's financial performance over the last three years you can see consistent improvements in revenue, margin, and EPS.

Revenue from continuing operations has grown at a 10% compounded annual growth rate. Our adjusted margins have improved 680 basis points, from 29.1% to 35.9%, and we have achieved a compounded annual growth rate in earnings per share of 24%.

Now, let's turn to our 2014 results:

- Revenue increased 7% year-on-year;
- Adjusted operating profit increased 17%;
- Adjusted operating margin increased 280 basis points; and
- Diluted adjusted EPS increased 20%.

All of our business units delivered revenue growth, increased adjusted operating profit and improvement in adjusted operating margin. This balanced contribution across all business units is a core strength of McGraw Hill Financial.

As we look at the fourth quarter, we finished the year with strong results:

- Revenue grew 7%, with all business units contributing mid to high single-digit growth;
- Meaningful adjusted margin expansion continued. Although it should be noted that in the fourth quarter of 2013 S&P Dow Jones Indices recorded a \$26 million non-cash impairment charge impacting those results. Notwithstanding this charge, the adjusted margin would still have increased significantly; and
- Fourth quarter diluted adjusted EPS increased 23%.

Our global footprint continues to expand as international revenue growth of 8% outpaced domestic growth of 7%. In this chart, you can see that Commodities & Commercial Markets in particular delivered the strongest international revenue growth.

Standard & Poor's Ratings Services

Now, let me turn to the individual businesses. And I'll start with Standard & Poor's Ratings Services.

In 2014:

- Revenue increased 8%;
- Adjusted operating profit grew 13%; and
- The adjusted operating margin increased 190 basis points to 43.8%.

During the quarter:

- Revenue increased 8%;
- Adjusted operating profit jumped 18%; and

- The adjusted operating margin increased 380 basis points to 42.2%.

S&P Rating Services continues to make progress in improving margins. In fact, adjusted expenses in the quarter only increased 1% despite elevated costs related to recently-resolved legal and regulatory matters.

Reviewing the next slide, non-transaction revenue growth both in 4Q and for the full year was driven by annual fees (predominantly frequent-issuer relationship fees and surveillance) and Rating Evaluation Service revenue.

Demand for corporate debt ratings and bank loan ratings drove overall 2014 transaction revenue, while in the fourth quarter growth was driven by demand for corporate and public finance ratings.

If we turn to issuance, U.S. and European trends diverged in the fourth quarter with a 20% increase in U.S. issuance and a 12% decrease in European issuance. And this mirrors the macro economic trends of growth in the U.S. and uncertainty that we saw in the fourth quarter in Europe.

Fourth quarter issuance in the U.S. was quite strong across all dimensions:

- Investment-grade increased 22%;
- High-yield increased 17%;
- Public finance was up 23%; and
- Structured finance also rose 14% driven by CLOs, ABS, and RMBS.

In Europe, although corporate issuance was very weak, structured finance increased 49% especially through a surge in RMBS due to a refocusing of the United Kingdom Funding For Lending Scheme away from mortgage lending.

This next chart depicts the number of European corporate issuers – a very important trend that we are watching. You can see a significant increase in our European customer base in the past two years. In order for European companies to meet their borrowing needs, they are increasingly turning to the capital markets. While quarterly issuance volumes ebb and flow, this is a very bullish long-term trend.

S&P Capital IQ

Now, let me turn to Capital IQ. In 2014, in S&P Capital IQ organic revenue grew 7%, adjusted segment operating profit grew 18%, and the adjusted margin increased 190 basis points. After two years of investments, the business delivered adjusted operating margin improvement for the year. And the fourth quarter results were largely consistent with the full-year results.

Let me add a bit more color on full-year revenue growth in the three business lines in 2014:

- S&P Capital IQ Desktop & Enterprise Solutions revenue increased 8%, and this was principally driven by an 11% increase in Desktop revenue.
- S&P Credit Solutions revenue increased 6% from a 10% increase in RatingsXpress®.
- In the smallest category, S&P Capital IQ Markets Intelligence revenue decreased 3% overall. While Leveraged Commentary & Data and Global Markets Intelligence continued to deliver double-digit growth, declines in Equity Research Services and the shutdown of FMR Europe more than offset those gains.

S&P Dow Jones Indices

Turning to S&P Dow Jones Indices; in 2014, this business delivered a 12% increase in revenue with a 32% increase in adjusted operating profit. Revenue growth was achieved across every dimension of the business: ETF AUM, mutual fund AUM, derivatives, and data subscriptions.

In 2014, every dollar of incremental revenue growth resulted in a dollar of incremental adjusted operating profit. This resulted in a 2014 adjusted segment operating profit margin of 63.6%.

The fourth quarter results generally mirrored the results for the full year except that the impact from the \$26 million impairment charge in the fourth quarter of 2013 had an impact on year-over-year comparisons.

If we turn to the key business drivers, the ETF industry experienced record inflows of \$331 billion in 2014. The trend toward passive investing continues and S&P Dow Jones Indices, with its broad and innovative array of indices, is at the forefront of this trend.

ETF AUM associated with our indices increased 25% from the end of 2013 to \$832 billion. Importantly, 15% of this growth was the result of new inflows.

Mutual Fund AUM associated with our indices reached another major milestone in 2014 surpassing the \$1 trillion mark.

With volatility roaring back in the fourth quarter, derivative trading volumes picked up with daily activity based on S&P Dow Jones Indices growing 20%. But for all of 2014, yearly volumes only increased 4% as volatility was very, very low for most of the year.

Commodities & Commercial Markets

On to Commodities & Commercial Markets.

As a reminder, McGraw Hill Construction was sold and its results moved to discontinued operations, thus our financials for 2014 and 2013 do not include these results.

On a continuing operations basis, 2014 organic revenue, excluding the impacts of the Eclipse acquisition and the Aviation Week divestiture, grew 9%. The adjusted operating margin increased 130 basis points to 34.3%.

The 130 basis-point adjusted margin improvement from continuing operations is only part of the story. Taking into consideration the sale of McGraw Hill Construction, as well as margin improvements for continuing operations, the adjusted operating margin actually increased 370 basis points.

Fourth-quarter organic revenue from continuing operations increased 7% and the adjusted operating margin decreased 120 basis points. During the fourth quarter, margins were impaired by timing of investments in J.D. Power to fully operationalize NextGen platforms and extend PIN data. By investing in new global products, global workflow tools, and client delivery platforms, we are enabling J.D.

Power to achieve continued revenue growth. In addition, the acquisition of Eclipse had a modest negative impact on margins.

For Platts, fourth-quarter revenue was the strongest of the year capping high single-digit organic revenue growth for 2014.

With a backdrop of a dramatically reduced oil prices, Petroleum, the largest category, delivered high single-digit growth in both the quarter and the year through increased demand for price assessments and market data subscriptions. By providing transparent pricing data and analysis, Platts assists its customers in managing commodity price volatility.

Based on recent investments in Steel Business Briefing and Kingsman, Metals & Agriculture delivered the greatest rate of revenue growth in 2014 at 34%.

Global Trading Services' revenue increased in the fourth quarter, primarily in Metals & Agriculture, but was down for the year. Despite increased oil volatility, trading based upon our pricing remained subdued due to regulation and the exit of several financial institutions from the business.

Finally, J.D. Power finished the year with its highest revenue quarter, delivering low single-digit revenue growth in the quarter and high single-digit revenue growth for the year. Asia revenue led the way with 10% growth for the year.

Overall in both the quarter and the year, growth was paced by gains in the auto business, thanks to PIN and our consulting business.

The second largest contributor to 2014 growth was advertising licensing revenue from customers' usage of the J.D. Power brand. And this advertising extends well beyond the auto sector.

Global Services Industries, which is all of our non-auto businesses, delivered low single-digit growth in 2014.

In summary, the Company delivered solid yearly results, while also completing our portfolio rationalization and resolving significant legal and regulatory matters. It has been gratifying; particularly with all our business units contributing to growth in revenue from continuing operations and significant margin improvement.

Thanks to the efforts of some 17,000 employees around the world, we delivered continued adjusted operating profit margin improvement of 280 basis points for the Company. And the combination of strong revenue growth and adjusted margin expansion yielded strong diluted adjusted earnings per share of \$3.88.

As we turn to 2015, I want to reiterate our focus on creating growth and driving performance. We are introducing guidance of mid single-digit revenue growth and adjusted earnings per share of \$4.35 to \$4.45.

As we launch 2015, the entire organization is aligned around key themes and these include:

- Strengthening customer and stakeholder engagement;
- Accelerating our international growth;
- Sustaining our margin expansion and having discipline in capital allocation;
- And, all the while, managing and mitigating risks throughout the Company.

With that, I want to thank all of you for joining the call this morning and now I'm going to hand it over to Jack Callahan, our Chief Financial Officer.

Jack Callahan

Executive Vice President and CFO
McGraw Hill Financial

Thank you, Doug. Good morning to everyone joining us on the call.

I want to discuss several items in more detail related to fourth quarter and full-year performance:

- I will recap consolidated income statement results both for the quarter and the year;
- Review the recent charges related primarily to legal/regulatory items;
- I will also review the restructuring actions taken across the portfolio in the quarter, including an update on our progress on the \$100 million cost reduction program that we introduced early last year;
- Discuss free cash flow results;
- Provide a return of capital update; and
- Finally, I will provide additional color on our 2015 guidance.

Let me start by reviewing our fourth-quarter results. Please note that these figures are adjusted financials, as our GAAP results were materially impacted by the settlements and, to a lesser extent, restructuring actions. I will discuss the GAAP results in just a moment.

As Doug noted, our portfolio of businesses is performing quite well, and closed out 2014 with solid results. In the fourth quarter:

- Revenue grew 7%;
- Adjusted segment operating profit grew 25%, with all four business units contributing to this growth.
- Adjusted unallocated expense was flat versus a year ago.
- Total expenses declined more than 1%, contributing to an adjusted consolidated operating profit growth of 28%, a 570 basis-point increase in the Company's adjusted profit margin.
- The tax rate on an adjusted basis was 32%, as the full year came in a bit better than expected.
- Adjusted net income increased to 22%, and adjusted diluted earnings per share increased 23% to \$0.95. The average adjusted diluted shares outstanding decreased by 1% due in part to share repurchase activity completed in the first half of 2014.
- The impact of foreign exchange in the quarter was a bit more significant versus previous quarters, although it was relatively modest overall:
 - Revenue was negatively impacted by approximately one point of growth; and
 - Operating profit benefited by approximately 2 points of growth due to the forex impact on non-U.S. denominated expenses.

Now, let's turn to the full-year results:

- Revenue grew 7% to well over \$5 billion; the impact of forex on full-year revenue is negligible.
- Adjusted segment operating profit grew 16%, with all four business units contributing to this growth.
- Adjusted unallocated expense increased 7%, primarily due to an impairment charge associated with the sale of the corporate aircraft and a one-time expense associated with the sale of a data center that were recorded in the second quarter.
- Total adjusted expenses for the full year increased less than 3% contributing to adjusted operating profit growth of 17%, driving a 280 basis-point increase in the Company's adjusted profit target.
- The tax rate on an adjusted basis was 33.1%, a reduction of 80 points versus a year ago.
- Overall, adjusted net income increased 19%, and adjusted diluted earnings per share increased 20% to \$3.88. The average adjusted diluted shares outstanding decreased by 1%.

Overall, a strong year of performance.

Because of the significant legal and restructuring charges, we added this bridge which I hope will be instructive. During the year, the Company recorded \$1.7 billion in charges largely associated with legal/regulatory matters and, to a lesser amount, restructuring. These charges were predominantly recorded in the fourth quarter. The after-tax impact of these items was approximately \$1.4 billion. The effective tax rate is approximately 20% in aggregate as a result of all of these charges.

To provide additional clarity, we have broken out all of the second-half charges related specifically to legal/regulatory matters, which total just over \$1.6 billion. We would expect all of these payments to be made by the first quarter of 2015. I would note that in addition to significant settlements with the Department of Justice, the Attorneys General of said 19 states and the District of Columbia, and CalPERS, there was \$17 million in additional charges associated with the final settlement with the SEC, New York, and Massachusetts; and \$35 million associated with settlements in several private litigation items stemming from the financial crisis.

Because of the strong balance sheet we have maintained, we have ample flexibility to make these payments. Most of the payments will come out of cash on hand – and our \$1 billion credit facility, which remains untapped at this point in time.

Now, let me provide some color on restructuring actions in the quarter.

Last year, we established a cost reduction target of at least \$100 million by the end of 2016. One aspect of that program was identifying efficiency opportunities in our work processes without compromising the quality and timeliness in how we serve customers. As a result, there have been restructuring actions across the portfolio. During the second half of 2014, we took restructuring charges totaling \$86 million, with \$41 million in the fourth quarter. These actions are a meaningful part of our ongoing cost reduction program to sustain margin expansion.

Now, let me provide an update on the progress we are making overall on this cost reduction program that we discussed at our Investor Day last year. Our goal has been to achieve more than \$100 million in cost reductions over a three-year period. The pieces of the pie have been sized to display the actual costs savings that we have identified in: restructuring our workforce; streamlining our real estate portfolio; leveraging our procurement scale; and reducing corporate costs. We are very much on

track with this cost reduction program, and now target exceeding the initial target as \$140 million in opportunities have been identified. We expect that more than three quarters of these savings will be realized by the end of 2015.

Let me remind you that some of our cost reduction will be reinvested in growing our business. For example, while Platts is reducing its workforce in some areas, it is adding to it in others, namely its Metals & Agriculture business.

Now let me update you on free cash flow. Our guidance was to achieve free cash flow of approximately \$1 billion, and we achieved that. Our cash balance at the end of 2014 was approximately \$2.5 billion.

In 2014, our return of capital in dividends and share repurchases was \$688 million. 2014 share repurchases totaled 4.4 million shares. We did not repurchase any shares during the fourth quarter.

Next, I would like to provide you with a broader view of our return of capital. The Company has an outstanding record of returning cash to shareholders. We have returned approximately \$3.3 billion in the last three years in share repurchases and dividends.

We announced today that for 2015, the Board of Directors has authorized a 10% increase in the dividend to an annual payout of \$1.32 per share. This marks the 42nd year of sustained dividend increases.

As we look forward, we will remain disciplined in our capital allocation strategy. But now that we have addressed the most significant legal/regulatory matters facing the Company, we can put more focus on driving shareholder value.

Just to remind you on our priorities on the allocation of capital:

- First, we will invest in organic growth;
- Second, continue to pursue attractive acquisitions to expand the portfolio;
- Third, sustain growth in our dividend as today's announcement demonstrates; and
- Finally, continue to selectively repurchase shares. We currently expect to be resuming the share repurchase program, subject to market conditions. As a reminder, we have 45.6 million shares remaining under our existing share repurchase authorization.

Furthermore, we will also consider additional leverage in the balance sheet as appropriate to both create growth and drive shareholder value.

Finally, I would like to provide more detail on our outlook for 2015. Guidance is as follows:

- Mid single-digit revenue growth — we are mindful that the strong U.S. dollar will likely negatively impact our revenue a bit;
- We are targeting more than 125 basis points of adjusted profit margin improvement;
- A tax rate on an adjusted basis of approximately 33%;
- Adjusted diluted earnings per share of \$4.35 to \$4.45;
- Assume approximately \$100 million of capital expenditures; and
- We are targeting free cash flow of greater than \$1.1 billion, excluding the payments related to the legal/regulatory settlements.

In closing, our businesses are performing very well, as clearly demonstrated in our 2014 adjusted operating results and this 2015 guidance, in line with our longer term financial goals. Overall, we remain focused on creating growth and driving performance.

To access the accompanying slides online, go to:

<http://investor.mhfi.com/phoenix.zhtml?c=96562&p=irol-EventDetails&EventId=5184265>

“Safe Harbor” Statement Under the Private Securities Litigation Reform Act of 1995

This presentation contains “forward-looking statements,” as defined in the Private Securities Litigation Reform Act of 1995. These statements, which express management’s current views concerning future events, trends, contingencies or results, appear at various places throughout this report and use words like “anticipate,” “assume,” “believe,” “continue,” “estimate,” “expect,” “forecast,” “future,” “intend,” “plan,” “potential,” “predict,” “project,” “strategy,” “target” and similar terms, and future or conditional tense verbs like “could,” “may,” “might,” “should,” “will” and “would.” For example, we may use forward-looking statements when addressing topics such as: the outcome of contingencies; future actions by regulators; changes in our business strategies and methods of generating revenue; the development and performance of our services and products; the expected impact of acquisitions and dispositions; our effective tax rates; and our cost structure, dividend policy, cash flows or liquidity.

Forward-looking statements are subject to inherent risks and uncertainties. Factors that could cause actual results to differ materially from those expressed or implied in our forward-looking statements include, among other things:

- the rapidly evolving regulatory environment, in the United States and abroad, affecting Standard & Poor’s Ratings Services, Platts, S&P Dow Jones Indices, S&P Capital IQ and our other businesses, including new and amended regulations and our compliance therewith;
- the outcome of litigation, government and regulatory proceedings, investigations and inquiries;
- worldwide economic, financial, political and regulatory conditions;
- the health of debt and equity markets, including credit quality and spreads, the level of liquidity and future debt issuances;
- the level of interest rates and the strength of the credit and capital markets in the U.S. and abroad;
- the demand and market for credit ratings in and across the sectors and geographies where we operate;
- concerns in the marketplace affecting our credibility or otherwise affecting market perceptions of the integrity or utility of independent credit agency ratings;
- our ability to maintain adequate physical, technical and administrative safeguards to protect the security of confidential information and data, and the potential of a system or network disruption that results in regulatory penalties, remedial costs and/or improper disclosure of confidential information or data;
- the effect of competitive products and pricing;
- consolidation in our end customer market;
- the impact of cost-cutting pressures across the financial services industry;
- a decline in the demand for credit risk management tools by financial institutions;
- the level of success of new product development and global expansion;
- the level of merger and acquisition activity in the U.S. and abroad;
- the volatility of the energy marketplace;
- the health of the commodities markets;
- the impact of cost-cutting pressures and reduced trading in oil and other commodities markets;
- the level of our future cash flows;

- our ability to make acquisitions and dispositions and to integrate, and realize expected synergies, savings or benefits from, the businesses we acquire;
- the level of our capital investments;
- the level of restructuring charges we incur;
- the strength and performance of the domestic and international automotive markets;
- our ability to successfully recover should we experience a disaster or other business continuity problem, such as a hurricane, flood, earthquake, terrorist attack, pandemic, security breach, cyber attack, power loss, telecommunications failure or other natural or man-made disaster;
- changes in applicable tax or accounting requirements;
- the impact on our net income caused by fluctuations in foreign currency exchange issues; and
- our exposure to potential criminal sanctions or civil remedies if we fail to comply with foreign and U.S. laws and regulations that are applicable in the domestic and international jurisdictions in which we operate, including sanctions laws relating to countries such as Iran, Russia, Cuba, Sudan and Syria, anti-corruption laws such as the U.S. Foreign Corrupt Practices Act and the U.K. Bribery Act of 2010, local laws prohibiting corrupt payments to government officials, as well as import and export restrictions.

The factors above are not exhaustive. The Company and its subsidiaries operate in a dynamic business environment in which new risks may emerge frequently. Accordingly, we caution readers not to place undue reliance on the above forward-looking statements, which speak only as of the dates on which they are made. The Company undertakes no obligation to update or revise any forward-looking statement to reflect events or circumstances arising after the date on which it is made. Further information about our businesses, including information about factors that could materially affect our results of operations and financial condition, is contained in the Company's filings with the SEC, including Item 1a, Risk Factors, in our most recently filed Annual Report on Form 10-K.