

The McGraw-Hill Companies
1st Quarter 2012 Earnings Conference Call

Prepared Remarks
April 24, 2012

Chip Merritt

Vice President, Investor Relations
The McGraw-Hill Companies

Good morning and thank you for joining us this morning at The McGraw-Hill Companies' first quarter 2012 earnings call.

I'm Chip Merritt, vice president of Investor Relations at The McGraw-Hill Companies. This morning we issued a news release with our results. We hope you have all had a chance to read the release. If you need a copy of the release and financial schedules, they can be downloaded at www.mcgraw-hill.com.

In today's earnings release and during the conference call, we are 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 differences between the non-GAAP measures and comparable financial measures calculated in accordance with U.S. GAAP. The results for the prior-year quarter also reflect the reclassification of the Broadcasting Group as a discontinued operation.

Before we begin, I need to provide certain cautionary remarks about forward-looking statements. Except for historical information, the matters discussed in 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-Ks, 10-Qs, and other periodic reports filed with the U.S. Securities and Exchange Commission.

We're aware that we do have some media representatives with us on the call. However, this call is for investors and we would ask that questions from the media be directed to Patti Rockenwagner in our New York office at (212) 512-3533 subsequent to this call.

Now, I would like to turn the call over to Harold McGraw III, chairman, president and CEO of The McGraw-Hill Companies. Terry.

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Harold McGraw III

Chairman, President and CEO

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Thank you, Chip. Good morning everyone and welcome to today's conference call. You just heard from Chip Merritt. He is our new vice president of Investor Relations. Chip joined us about a month ago and we are certainly glad to have him aboard.

For the last 73 quarters, Don Rubin introduced our earnings conference calls. On February 20, 2012, our senior vice president for Investor Relations, Don Rubin, passed away after only recently announcing his retirement from McGraw-Hill. His distinguished career was 52 years long. He was a manager; a thought leader; a mentor, and a beloved friend to all and his legacy is one of growth, purpose, passion, trust, and relevance.

I had the distinct honor of working closely with Don for many, many of those 52 years. With Don's passing, McGraw-Hill has lost a leader, and personally, we have lost a very close and dear friend. And I know this is true for many of you on the earnings call today.

Don began his career as a sports writer and was a journalist at heart. To honor Don's rich legacy at McGraw-Hill, the Corporation has established a scholarship at the CUNY Graduate School of Journalism. And I can think of no better way to say good bye to our dear friend than to say hello to future "Rubin" scholars in the lifetime ahead.

Joining me on today's conference call is Jack Callahan, our chief financial officer. This morning, Jack and I will review first quarter results, provide an update on our Growth and Value Plan progress, and give the outlook for the balance of the year.

There are a couple of themes that permeate today's discussion and are at the core of our focus here at the Company:

- Number one is delivering top- and bottom-line growth; and
- The other is executing upon our Growth and Value Plan.

These are at the forefront of our strategy to transform McGraw-Hill into two powerful new companies and we are pleased with the progress made thus far in 2012. We see incredible opportunity ahead as we create McGraw-Hill Financial and McGraw-Hill Education. Both companies share a common promise and a common purpose: We're about helping our customers find new ways to succeed and to prosper in a rapidly changing world where information is often conflicting, confounding, and sometimes confusing. The bottom line is that we help make sense of it all. To be clear, our mission is never – nor ever will be – about us. It will always be about our customers. And if we remain focused on them, solid business results will follow.

Therefore, we are very pleased to begin the year with a record first quarter. \$1.3 billion is a record for first quarter revenue and \$0.51 is a record for first quarter adjusted diluted earnings per share. What makes these results all the more impressive is that they occurred during a quarter in which so many of our employees were focused on the work streams necessary for the separation of the Company.

The McGraw-Hill Companies

As you will see momentarily, the three segments that will comprise McGraw-Hill Financial delivered strong, top-line growth. This performance, coupled with successful cost reduction efforts associated with our restructuring and the recent substantial share repurchases, led to record first-quarter profitability. What is also notable is that, on a pro forma basis, McGraw-Hill Financial and McGraw-Hill Education both delivered increased year-over-year adjusted operating profit.

Steady progress has been made on the Growth and Value Plan during the first quarter.

- We remain on track for separation into two industry-leading companies by year-end.
- We have filed a request with the Internal Revenue Service for a ruling that the spin-off of McGraw-Hill Education is tax-free to the Corporation and its shareholders. And I am very pleased to inform you that, as of late last night, we have received a favorable ruling from the IRS agreeing to the tax-free status for the spin-off of McGraw-Hill Education.
- The Corporation also plans to file the Form 10 in the coming weeks.
- We remain on track to deliver in excess of \$100 million, on a run-rate basis, in cost savings by year-end.
- These cost savings are also seen across the Corporation with first quarter expense growth, on an adjusted basis, of only 3%, which expanded the consolidated margin by approximately 200 basis points.
- Implementation is well underway on the Growth and Value Plan. Globally, there are more than 100 people supporting more than 15 work streams to drive separation and reduce costs.
- And we will continue to invest in McGraw-Hill Financial through targeted acquisitions.

So far this year we have acquired two companies, both adding capability to the S&P Capital IQ platform. The first was R² Financial Technologies. With this addition, S&P Capital IQ will now be able to offer clients an integrated view of market and credit risks across asset classes in a unique solution. This is increasingly important for financial institutions that are looking to manage complex and diverse portfolios across the globe. By combining R², ClariFI, and Risk Solutions' development teams, we have the foundation to build a powerful and innovative new offering for professional investors.

The second acquisition was QuantHouse. QuantHouse provides S&P Capital IQ clients with a global, integrated, low-latency distribution network. They will develop a new generation of desktop monitoring and display applications, alpha-generation tools, and integrated low-latency data feeds moving S&P Capital IQ closer to becoming a one-stop shop for all financial industry professionals.

With that, let me now turn to the business results.

McGraw-Hill Financial

McGraw-Hill Financial, on a pro forma basis, delivered a very solid quarter with revenue up 8% and operating profit up 10%. While all three segments delivered revenue growth, it was clearly Commodities & Commercial that led the operating profit growth.

McGraw-Hill Financial derives 40% of its revenues from outside the United States and during the first quarter international business growth of 12% outpaced domestic growth of 5%. The Standard & Poor's Ratings segment led the way as the most influential on the international side with 47% of its first quarter revenue coming from sales outside the United States.

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Standard and Poor's Ratings is the largest business segment within McGraw-Hill Financial. Revenue for the segment grew 5% driven predominately by transaction revenue which increased 10%. The key drivers to the increase in transaction revenue were:

- U.S. public finance issuance, which increased 61%. But recall now that the muni market was adversely impacted back in the first quarter of 2011 by weak municipal economies and the perceived risk of a wave of muni defaults which did not come to fruition.
- U.S. corporate issuance increased 8%, driven by record speculative-grade issuance which increased 14%.
- During the quarter, risk aversion waned due to European Central Bank liquidity flooding the global capital markets and a temporary resolution of the European sovereign situation. This resulted in a quest for yield by investors.
- And European non-financial corporate issuance, which increased 31%.

Non-transaction revenue, which represents 58% of first quarter revenue, increased 2%. The macro themes that we have shared with you in the past related to the ratings market remain in place, namely:

- A large pipeline of maturing global corporate debt that will need to be refinanced.
- Another would be the shift in Europe from bank loans to public debt markets. In fact, during the first quarter European companies borrowed more from the bond market than they did from banks. This trend was highlighted in a *Wall Street Journal* article written earlier this month entitled "*Bonds With Banks Fraying – European Companies' Move Into Debt Markets Bucks Direct-Lending Tradition.*"
- And finally, the structured finance market recovery remains beholden to improved activity in the residential and commercial real estate markets.

Operating profit was down slightly in the quarter as we made targeted investments in new employees to reinforce the growth of Corporate and Government ratings as well as growth in emerging markets. In addition, legal expenses were up versus a year ago, but were modestly down on a sequential basis versus the fourth quarter of 2011.

While certainly expensive, our success on the litigation front has been encouraging. Three additional cases were dismissed in the first quarter bringing the total to-date to 27. Seven dismissals by lower courts have been affirmed by higher courts, and ten cases have been voluntarily withdrawn.

One very important case was the Reese case. Earlier this month, the judge granted our motion to dismiss all claims against the Corporation. This was important because it was one of four purported class-action stock-drop cases filed against the Corporation associated with the financial crisis. And now all four have been dismissed.

The ratings business remains an area of focus for regulators. While I recognize that the suggested regulations in Europe continue to evolve, I am increasingly encouraged by some of the more pragmatic views that have been expressed more recently. All-in-all, I am encouraged by Ratings' start to the year. I believe that we are investing appropriately in the business to enable continued growth, and as credit markets continue to normalize, we are well positioned for success.

Let me now turn to S&P Capital IQ/S&P Indices, the second-largest segment within McGraw-Hill Financial. It delivered solid top- and bottom-line results with revenue and operating profit increasing 9%

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and 11%, respectively. Both S&P Capital IQ and S&P Indices delivered year-over-year revenue growth with 75% of revenue coming from subscriptions, up from 74% a year ago.

Looking at S&P Capital IQ alone, revenue increased 10%. A key driver of this growth was the 11% increase in Capital IQ clients year-over-year, however both RatingsXpress and Ratings Direct also contributed to the double-digit revenue growth. This was in part due to cross-selling opportunities that are being realized as both the Global Credit Portal and TheMarkets.com are migrating onto the S&P Capital IQ platform.

Another driver of subscriber growth is the continuous enhancements to the platform. A few examples include the iPhone and BlackBerry® apps that are now available and an Enterprise Solutions Software Development Kit that was launched in January that will allow our clients' IT personnel to pull just the data they need when they need it.

With the acquisitions of R² and QuantHouse, along with internal capabilities, S&P Capital IQ is well poised now to deliver further competitive capabilities to offer our clients the most comprehensive market data and risk analytics platform in the industry.

S&P Indices revenue increased 5%. The key contributor to this was an 11% increase in assets under management in exchange-traded funds linked to S&P indices. During the quarter, 10 brand new indices and 23 variants to existing indices were launched. Also during the quarter, 41 new ETFs linked to S&P indices were launched bringing the total to 419 ETFs. These new additions bode well for continued growth of S&P Indices. Another area of excitement within S&P Indices is the pending joint venture with CME Group. We continue to anticipate completing this transaction mid-year.

Clearly the highlight of the quarter was the performance of the Commodities & Commercial segment. While the smallest segment within McGraw-Hill Financial, it delivered year-over-year operating profit gains that led all the other segments. Revenue growth was 13%, with international revenue up 23%. Not only was there strong top-line growth, but the expense control was outstanding – resulting in impressive segment operating profit margin expansion to over 27%.

Within Commodities, subscriptions for petroleum and natural gas products drove the 22% increase in revenue. Since the acquisition of BENTEK Energy we have been leveraging our Platts sales force to drive increases in our natural gas business. Because of the growth in our Commodities business, I thought it would be instructive to spend a few minutes discussing our hidden gem—Platts.

Platts is a leading provider of oil, natural gas, electric power, coal, shipping, petrochemicals, and metals information. Importantly, more than 90% of revenue is derived from subscriptions. That results in a business with very little volatility.

Market Data is Platts' largest product. It is a subscription service that provides access to the latest price data, including end-of-day assessments, third-party data, and access to a complete historical database. Platts' price data is highly valuable to traders, risk managers, analysts, and others who seek unbiased price assessments. Because of the importance that the market participants place on Platts' price assessments, they are frequently utilized as reference points in long-term contracts between two parties. As such, Platts has become integral to the functioning of the industries in which it serves. We believe

The McGraw-Hill Companies

that Platts can continue to deliver meaningful growth by focusing on extending capabilities within markets it already serves, and expanding into new market areas.

Within Commercial, J.D. Power delivered significant year-over-year revenue growth. While all industry sectors delivered growth, automotive led the way both domestically and internationally.

With that, let me move over to McGraw-Hill Education.

McGraw-Hill Education

McGraw-Hill Education reported a 2% decline in revenue yet delivered a 13% increase in segment operating profit. By now, everyone is quite familiar with the weakness in the el-hi markets. In contrast, both Higher Education and Professional delivered nice revenue growth. Also quite encouraging were the cost reductions that the segment delivered, most notably as a result of the restructuring actions taken in the fourth quarter of 2011. We want to ensure that our cost structure is optimal for the new market realities and that we make the appropriate investments in the digital products that our customers demand.

Because the first quarter is such a seasonally light quarter, I'm not going to get into a detailed discussion regarding adoption and open territory progress, but we will be doing that as we go forward. Instead I would like to focus on digital progress.

As I've said before, I believe that the digitization of education represents the opportunity of the century. As McGraw-Hill Education is formally launched later this year as an independent company, it will be one of the market's commanding leaders with a brand name that's already universally recognized and respected for past accomplishments. We are targeting new achievements in a changing educational landscape that's limited only by our imagination.

Currently Professional and Higher Education are leading our efforts in delivering digital solutions to address customer needs in the marketplace. Nearly 40% of Professional revenue came from digital products during the quarter. This shift is also happening in our larger Higher Education arena which realized a roughly 50% increase in digital revenue year-over-year.

Since digital products are often subscription based, another way to measure the traction that these products are making to our product portfolio is to look at deferred revenue. Deferred revenue grew 63%, compared to the end of the first quarter of 2011, to \$106 million. This gain was largely driven by the sales of CINCH Science, an all-digital curriculum for the school market, and McGraw-Hill Connect, a homework management and study system for the higher education market.

The Higher Education, Professional and International Group reported a 2% increase in revenues. We were excited to see a continuation of recent strength in Higher Education and Professional with revenues up from the prior year by mid-single digits. These increases were partially offset by a decline in international results.

The School Education Group reported a 10% decline in revenue from the prior year, with decreases occurring in both the instructional materials and testing businesses. The first quarter is the smallest in

The McGraw-Hill Companies

the el-hi market, representing approximately 11% of annual sales. These results are not predictive of full-year trends. Those trends are being determined now as school districts across the country decide which materials they will order later in the year for use beginning next fall. So far, the spring selling season appears to be progressing well for McGraw-Hill and for the industry in terms of district-level activity. However, funding concerns remain acute in many areas. We will have a better view of the full-year el-hi market at the end of the second quarter.

We are setting up the Education business to thrive as a stand-alone company. We are putting in place the cost structure and digital capabilities necessary for McGraw-Hill Education to lead the transformation of the industry.

And, therefore, in summary:

- The McGraw-Hill Companies is off to a record start to the year.
- McGraw-Hill Financial should continue to deliver solid growth. With bolt-on acquisitions and our in-house capabilities, we plan to continue to deliver increased capabilities to our customers.
- McGraw-Hill Education will focus on capitalizing on the opportunity of the century by driving unique new digital product offerings to satisfy a changing education landscape while simultaneously creating a cost structure that is right-sized to serve the market.
- The Corporation will remain focused on delivering on our Growth and Value Plan and continue to work toward the completion of the spin-off of McGraw-Hill Education by year-end.

That completes our review of operations. I will now ask Jack Callahan, our chief financial officer, to update you on some key financials.

Jack Callahan

Executive Vice President and Chief Financial Officer
The McGraw-Hill Companies

Thank you Terry.

Let me begin this morning by discussing our consolidated results. Terry has just discussed the record first quarter revenue that we delivered, which represented 6% growth versus 2011. The solid revenue performance was leveraged by limiting our adjusted expense growth to just 3% — essentially half of our revenue growth. As a result, we were able to realize adjusted operating profit growth of 18% and deliver a consolidated adjusted operating margin of 19%. This resulted in margin improvement of approximately 200 basis points versus last year.

We are beginning to see benefits from the multiple initiatives underway across the organization to improve expense productivity as we separate the company and prepare for the spin-off of Education. In addition, we were able to leverage this strong growth with substantial share repurchases. The result was to turn the 18% growth in adjusted operating profit into a 30% increase in adjusted diluted earnings per share.

Our share repurchase program is an important part of the Growth and Value Plan. Since the beginning of 2011, the Corporation has repurchased nearly 36 million shares at a weighted average price of \$42.05. This is a reduction of approximately 12% of the shares outstanding at that time.

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Apart from the completion of the accelerated share repurchase program, no other shares were repurchased so far in 2012. As we get closer to separation, and accumulate additional cash, we will consider when to resume share repurchases.

We have a very strong balance sheet with cash and short-term investments of \$932 million. Year-over-year, our adjusted free cash flow was down \$44 million. The first quarter is the seasonally weakest cash flow quarter. This was exaggerated this year by the timing of some working capital and tax payment items. We fully expect to deliver another year of solid adjusted free cash flow growth with guidance of approximately \$750 million.

Now let me provide some additional details around the execution of the Growth and Value Plan. During the quarter, we continued to make progress on our target of at least \$100 million in run-rate cost savings by the end of 2012. The margin expansion that we delivered in the first quarter was in part due to these efforts. We have already taken some actions that will deliver cost saving and, as the year progresses, we plan to take more. Therefore, the cost savings from these initiatives should step up throughout the year. However, we are not solely focused on reducing costs. We continue to make targeted investments in the business to support global growth and enhanced capability.

We do want to give you our current outlook with regard to the one-time costs in support of the separation and the cost reduction plan. Please keep in mind that these are estimates and timing have not been finalized. We will update you as we progress through the year.

During the first quarter, we incurred \$33 million of one-time Growth and Value Plan costs that we noted in this morning's press release. We anticipate that for the remainder of the year we will incur an additional \$100 million of one-time separation expenses necessary to implement the Growth and Value Plan. These one-time expenses are largely professional fees, as we need the support of various consultants, business process and information technology firms, and financial advisors. Please keep in mind this is a working estimate.

In addition, we anticipate that during 2012 we will continue to incur restructuring costs as part of our ongoing cost reduction initiatives, as we did during the fourth quarter of 2011. While the timing of these actions are still fluid, restructuring expense for 2012 could be approximately up to \$75 million.

As we prepare to file the Form 10 necessary for a tax-free spin-off of the Education business, I want to update you with some high-level thoughts with regard to the capital structures of the two new companies:

- We expect that McGraw-Hill Financial will carry a strong investment-grade rating and continue to be committed to a strong dividend.
- With McGraw-Hill Education, we are targeting a more flexible investment-grade rating and a modest dividend. We will ensure that at the time of the spin-off that there is adequate liquidity to meet business needs and to manage the seasonal fluctuations in working capital.
- And as Terry mentioned, we have received a ruling from the Internal Revenue Service agreeing to the tax-free status for the spin-off of McGraw-Hill Education.

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All-in-all, we are off to a terrific start with a record first quarter:

- Our guidance remains unchanged
- Separation activities are accelerating
- Our cost reduction programs are on track
- We are focused on the mission to establish two powerful industry leaders by year-end

Thank you.

To access the accompanying slides online, go to:

<http://investor.mcgraw-hill.com/phoenix.zhtml?c=96562&p=irol-EventDetails&EventId=4746923>

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

This presentation contains forward-looking statements, including without limitation statements relating to our businesses and our prospects, new products, sales, expenses, tax rates, cash flows, prepublication investments and operating and capital requirements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are intended to provide management’s current expectations or plans for our future operating and financial performance and are based on assumptions management believes are reasonable at the time they are made.

Forward-looking statements can be identified by the use of words such as “believe,” “expect,” “plan,” “estimate,” “project,” “target,” “anticipate,” “intend,” “may,” “will,” “continue” and other words of similar meaning in connection with a discussion of future operating or financial performance. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict; therefore, actual outcomes and results could differ materially from what is expected or forecasted. These risks and uncertainties include, among others:

- worldwide economic, financial, political and regulatory conditions;
- currency and foreign exchange volatility;
- the effect of competitive products and pricing;
- the level of success of new product development and global expansion;
- the level of future cash flows;
- the levels of capital and prepublication investments;
- income tax rates;
- restructuring charges;
- 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 capital markets in the U.S. and abroad;
- the demand and market for debt ratings, including collateralized debt obligations, residential and commercial mortgage and asset-backed securities and related asset classes;
- enrollment and demographic trends;
- the level of merger and acquisition activity in the U.S. and abroad;
- the level of funding in the education market;
- School Education Group’s level of success in adoptions and open territories;
- the state of the credit markets and their impact on Standard & Poor’s Ratings and the economy in general;
- the regulatory environment affecting Standard & Poor’s Ratings;
- the strength of School Education Group’s testing market, Higher Education, Professional and International’s publishing markets and the impact of technology on them;
- continued investment by the construction, automotive, computer and aviation industries;
- the strength and performance of the domestic and international automotive markets;
- the volatility of the energy marketplace;
- and the contract value of public works, manufacturing and single-family unit construction.



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In addition, there are certain risks and uncertainties relating to our previously announced Growth and Value Plan which contemplates a tax-free spin-off of our education business, including, but not limited to, the impact and possible disruption to our operations, the timing and certainty of completing the transaction, unanticipated developments that may delay or negatively impact the spin-off, and the ability of each business to operate as an independent entity upon completion of the spin-off. We caution readers not to place undue reliance on forward-looking statements.