Morningstar 2020 Shareholders' Meeting

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Opening Comments by Kunal Kapoor

Kunal Kapoor, CEO, Morningstar: Good morning, everybody, and welcome to our Annual Shareholder Meeting. Like Joe, I'm thrilled to welcome you and I am so glad that you are joining us. Of course, I would have loved to have seen all of you in person, but the circumstances being what they are, we're still very, very glad that you could take the time to be with us today.

Mission and Strategy

As is the case with the broader world, it's been a different time at Morningstar. But the thing that has kept us together is our mission. And I want to start today by just playing a short video that will give you a small sense of the spirit of Morningstar.

[Video]

Kunal Kapoor: I hope you enjoyed that video. And what it comes down to at the end of the day is that even amidst these tough times, Morningstar is focused on empowering investor success. We know there is so much insecurity out there in the world today, and we are focused on helping individuals feel financially secure. We want to help them make the right decisions at this unprecedented time and we're doing that in a way that empowers their long-term success.

We continue to operate in an independent manner, in a very transparent manner, and with long-term thinking because we know the decisions made today have very significant impacts on the goals and the financial outcomes that individuals will experience 3, 4, 5, maybe even 10 years from now. So, we've kept our true north the notion of our mission and how it empowers investor success at the center and continued to bring it through life through independent opinions, transparent actions and long-term thinking.

COVID Response, Enabled By Our People

You've seen this manifest most meaningfully in the amazing amount of research that our analysts have put together these past few months. Whether you're a credit analyst in the United Kingdom, an equity researcher in Australia, an individual investor here in the U.S. – you name it, and we have had calm, reasonable and thoughtful coverage available in this unprecedented time.

I'm particularly proud of the fact that we stepped up and really tried to help individuals through pieces, webinars and other meaningful actions. And where we work with advisors, we have enabled their success, so that they can engage with individuals that they are serving in a way that helps those individuals stay on course for their goals. So, Morningstar is shining, and I'm proud of the work that our teams have been doing at this time.

Morningstar's Market Fair Value vs. the Broader Market

One terrific example of the work we've been doing can be viewed through the lens of our equity research. Our analysts publish a fair value estimate for each of the companies that they cover. We then roll up those fair value estimates and compare them to the actual stock prices of the companies that we're covering.

On March 23, it turns out, our analysts said that the market was 30% undervalued based on our coverage list relative to the actual stock prices. Now, it turns out that our low point is also the low point so far this year for the markets and I'm not bringing that up to toot our horn, but rather to point to you that we have a process in place, and that process is repeatable, thoughtful and long-term and can help investors who are staying the course and following our advice.

In fact, on that day, March 23rd, we had almost 650 stocks, just over 40% of our entire coverage universe, rated 5-Stars. That's meaningful, and shows that even amidst all the noise, our researchers were providing thoughtful and valuable insights to individuals, advisors and institutions that rely on us.

Our People

As I think about sharing with you what Morningstar looks like going forward, I think it's fair to say that it should start though with an examination of what Morningstar looks like today.

Here's a snapshot of Morningstar across the world. We are now close to 7,000 employees, a number we will go over once the Sustainalytics acquisition closes. But most importantly, we continue to invest in our core areas – core strengths of research, technology and design. We highlighted for you on this slide our investments in those areas, and this doesn't even include all the data analysts who cover all the securities that underpin all the work that's done across Morningstar.

I'm actually also very, very pleased that I'm able to share with you today that one of the high points of our internal surveys is the fact that when we ask folks the question about acting ethically, and with the integrity of our teams taking priority over anything else, we score as high as just about any organization based on data that we've received from the Great Places institute. So, we really are living our values in a meaningful way here at Morningstar.

2019 Reported Performance

When you live your values, we think it also shows up in great business performance. And if you've been a long-term shareholder of Morningstar, we're really glad that we've been able to deliver the results for you that we have over time.

2019 itself was a terrific year for Morningstar. We continued to grow nicely and find ways to take cash flow and put it into growth opportunities that will deliver value for shareholders and other stakeholders year-in and year-out.

Jason Dubinsky, my partner, and our CFO, will follow me and spend some more time going into the details around our financial performance. But you should feel really good about the fact that Morningstar is a strong enterprise with a strong balance sheet, and that we're making investments even in this environment that secure the future of our firm for many years to come.

Recent Highlights

There are many highlights and I always have trouble when I look back on the past year at highlighting just a few things. As I shared in my Shareholder Letter though, 2019 will be marked by our acquisition of DBRS. I'm really excited about the way we've been able to scale our Credit Ratings operation as a result of that acquisition and even more excited that later today you're going to hear from my friend and colleague, Detlef Scholz, who is the leader of DBRS-Morningstar.

We're also making investments in Financial Planning, Managed Accounts, PitchBook and ESG. These are all meaningful areas of growth for Morningstar.

With Financial Planning, we're trying to link it to our core capabilities in investment planning. Many firms say it's one or the other. We believe it's both and we're enabling wealth managers to offer a broader spectrum of services to the individuals that they service.

In Managed Accounts, we're reaching out to advisors like never before to help them navigate the retirement landscape, as they too think about outsourcing part of the work that they've done in this space.

And with PitchBook, we just keep investing in that platform and the data that underpins it, so that every user can just keep enjoying it more and more. The NPS scores for PitchBook are off the charts, and I know that if you've been a user, you've been pleased. We have more than 40,000 users, in fact, now on PitchBook, which is an amazing statistic, and just shows the power of that platform.

Integrated ESG Data and Research for All Investors

And there is ESG, which is moving to the center of everything that we do here at Morningstar. Just a few weeks ago, we announced that in the third quarter, we hope to complete the acquisition of Sustainalytics and that's just the latest step in the journey that we're on to ensure that ESG moves to the center of all things that we do to empower investor success.

When you think about the fact that many investors aren't always fully engaged with their investments, or they feel like they're a few steps away from them, ESG is a way that will draw more investors in. It will allow us to personalize the investment experience, and really make portfolios be more meaningful for investors, whether they are small investors, whether they are financial advisors, or whether they are institutional investors. Technology will enable personalization, and ESG will be at the center of it, and will become available across all of Morningstar solutions throughout the years to come.

We Participate in Large and Growing Markets

So, what does the future of Morningstar look like? I've talked to you already about ESG and the importance of ESG and it certainly will be a core part of our future. But what really excites me about our future is also the fact that Morningstar participates in large and growing markets.

We're putting a lot of statistics in front of you on this slide. But the key takeaway here is that relative to our size, the opportunities that we're pursuing to drive impact to investors are very, very meaningful. Whether you look at the size of the financial data market, or even just the private equity data market that's a part of it, we have so much room to run. You look at the size of Managed Accounts, the opportunity in global credit ratings, or what's happening with ESG, the runway for growth at Morningstar is very significant. And Indexes is another opportunity that we think is exciting because it meets at the crossroads of ESG and how indexing may become more personalized in the future.

Investor Trends

So, I hope you're as excited about our growth opportunities and what I want to do now is talk a little bit about how we're going to try to execute against some of them.

For those of you who have been Morningstar shareholders for a while, or have come to this meeting in prior years, you'll be familiar with these trends, which we think are critical in evaluating the landscape that we're competing in.

Investor Trend One

The first is that the modern investor is empowered with new data, research and analytics. We're all awash in it and need help making sense of it. And so, investors are also demanding more value from the advice that they're receiving. And as they look at their portfolios, one of the ways that that advice is being really shown to add value is through the addition of public and private market capabilities at many of our clients and the investors that they serve.

Everything at Morningstar begins with how we invest in our databases and the core data that we have. This is how we start thinking about playing Trend Number One. Each year, we add more data to the pot that we have, and then we add our IP – our research IP – on top of it. Most recently, we were pleased to announce the acquisition of Hueler Analytics, which brings with it a whole suite of stable value data, which is very important in the U.S. retirement marketplace.

We're also investing in a way that allows the IP to come to life, and most recently that's happened through the launch of our Factor Profiles. Each year, we try to add new IP on top of what we're delivering to our clients. And slowly and surely, it all gets worked into their workflows. We have the pipes set up to our clients, and we just think sending them more things through those pipes every year, and that shows up in the wonderful performance – the steady performance of our data business year-in and year-out.

We also continue to get great reception to Direct. We've kept the model for Direct very simple, right from when we launched it. For one price, you get access to all our data, all our capabilities. It's something that our clients really appreciate and enjoy, and we continue to find great growth. And last year, in particular, we saw very good growth outside the U.S.

Finally, on Trend number One, I want to highlight that we expect that we will be doing more and more in fixed income in the years to come. The most natural way that that is manifesting itself today at Morningstar is through DBRS-Morningstar. But beyond that, we are making investments in fixed income data in meaningful ways, in fixed income data that is not only applicable to the public markets, but also to the private markets, where debt is an increasingly crucial part of the overall equation.

Investor Trend Two

On Trend Number Two, we believe that the move towards outsourcing is going to remain in place for a long time. When we look at Investment Management and what we want to do there, we are focusing more and more on working with like-minded advisors, who share our investment philosophy. We want to be more significant partners to them and help them manage more of their clients' money as opposed to working with many advisors, who give us just a small amount of the overall book that they are managing.

It's important here to note that our Investment Management business has continued to go under some big changes. It used to be what I largely think about as a consulting business. And today, it's a higher-quality business, I think, in that it's focused on the advisor and the clients that the advisor serves and is focused on Managed Portfolios, primarily.

We're also making good headway in Workplace Solutions, both here and in Investment Management, the growth in assets under management has been impressive, while the growth in revenue maybe looks a little bit lighter. And the reason for that is clearly the fee pressure that's been sweeping across the industry. We felt it too in these lines, where we've continued to invest. And what's exciting about Workplace Solutions is that our advisor managed accounts, where we're beginning to work with advisors who are in the 401(k) business, is really starting to take shape wonderfully. You won't see the results of these show up in meaningful ways in our revenue for a couple of years, but we are doing all the things to get the pipes, the plumbing and the customers in place, so that we think we're establishing our meaningful moat, perhaps the first-mover advantage, in this space well before others are really thinking about how to partner with advisors in a meaningful way.

As for Indexes, I alluded earlier to the fact that there are many opportunities to us, and there certainly are. Just late last year, we hired Ron Bundy, the former CEO of Russell Indexes, USA, to come on-board and become the head of our Indexes business. Ron is a very thoughtful person, and he's already charging ahead, focused on areas where Morningstar can provide some unique capabilities; that could be in ESG, it could be in the private markets, and it could be in other areas around asset allocation where Morningstar has some unique IP to offer. We're growing fast in the Indexes space, and we think this business continues to provide us with great optionality as we look to the future.

Investor Trend Three

On Trend Number Three, PitchBook is the way we think about playing the convergence of public and private markets. We were certainly early to this trend, and it's the case now that I think everybody believes that it's here to stay. That's certainly the truth, but what I will say is that the data and capabilities within PitchBook are almost unrivaled. And as we take our public market capabilities and marry them with the core private market capabilities that PitchBook had, and slowly start thinking about adding things like fixed income into this toolkit, the use cases for PitchBook only continue to grow. We're very excited about the future of PitchBook in this context.

Concluding Remarks

So, with that said, I'll conclude my presentation by thanking you again for being here and for partnering with all of us at Morningstar. We're leaning into our mission during these uncertain times. And by doing so, we think we're earning the trust of the individuals, the advisors, and the institutions who we work with.

I thank you for your partnership. And I'm very pleased now to turn to my colleague, Jason Dubinsky, over at his home, to take the next steps and share our financial results with you. I'll be back on later on for the Q&A.

Jason, over to you.

Financial Highlights – Jason Dubinsky

Jason Dubinsky, CFO, Morningstar: Thanks, Kunal, and hello, everyone. It's great to be here again with all of you and hope you and your families are doing well. While we can't be here in person with you, we really appreciate the opportunity to spend time with you each year and thank you for your support and your affiliation with Morningstar. We truly value your partnership, and importantly, your feedback, your input and your engagement in our success.

I'd also like to take time to thank all of our team members globally, not only for the work you did last year, but for all of your efforts over the past several months. Our team has continued to support each other, our customers and our business while staying true to our mission and it really speaks to the culture and core values of this organization, which I'm proud to be part of.

So, I'll cover a few things with you today. First, I'll walk through our 2019 performance with some emphasis on margins; then I'll cover the first quarter and how the current environment is impacting us; then I'll take you through our performance through the last downturn using 2008 and 2009 as a reference point; and finally, we'll close with some discussion on our balance sheet, liquidity and capital allocation.

Financial Success in 2019

So, let's start with 2019, which seems like a long time ago at this point, but really important in the context of what we accomplished and helping to set the stage for 2020. We had a good year, and from my perspective continued to embody the core Morningstar value of financial success. We acquired DBRS for over $600 million, the largest transaction in our history. We continue to report strong top line growth, driven by important investments across the business. And we reported our highest level of free cash flow in our history, probably the most important health metric of the business on this page.

2019 Reported Performance

So, Kunal shared the 2019 headline numbers, and I'll provide a little bit more context here. We had strong top line performance last year supported by the inclusion of DBRS in the back half of the year. So, we now report adjusted operating income. And hopefully, most of you now are starting to get more familiar with that metric, which we think is a better measure of comparable performance as it excludes deal-related amortization and transaction and integration costs. And you can see here the big difference relative to the GAAP number. And amortization related to the DBRS acquisition is the big component of that difference. But you can see that adjusted operating income did decline last year, and I'll get into some of those margin drivers shortly. And importantly, free cash flow increased year-over-year, and it stood at $250 million at the end of 2019.

2019 Revenue Growth

So, here is that walk from reported revenue to organic revenue, which excludes M&A and FX impacts. DBRS-Morningstar was the biggest driver of the difference between the two. And recall that organic revenue last year was 8.4%, but we had a one-time license amendment, which increased 2018 revenue, and that impacted the growth rates. So, it's important to show that impact again this year, just like it was in 2018. And that had a negative 110 basis point impact on growth. So, I think about the 9.5% growth rate as the more representative organic growth number last year, which is strong underlying performance, and we saw it across all revenue types and geography, with particularly strong performance in our licensed-based products.

Operating Margin

So, I'll turn to margin and we get a fair amount of questions about our margin components and trends. So, I'll try to address some of this for better perspective, and we'll dedicate a bit of time here. So, first, you can see that on an adjusted basis margins declined about 340 basis points from 2018 to 2019. But I want to deconstruct that a bit for you.

First, there were two large non-comparable items, the accelerated license amendment in 2018, which artificially increased margin for one year, and a large increase in stock-based compensation in 2019 related to the final year of the initial PitchBook incentive plan, so here there was a large step-up in the incentive target and PitchBook actually outperformed the target, which is a good thing. So, these things were called out in our earnings releases, but if you neutralize the impact of both of these, the margin decline year-over-year was closer to 150 basis points, but that was still down.

So, we have small margin benefit from the inclusion of DBRS, and while revenue for the rest of Morningstar was up, there were other offsets last year, excluding the impact of DBRS. So, compensation costs increased in key areas of the business, notably in PitchBook to continue to accelerate growth, and other data collection and software development efforts with much of that headcount growth outside the U.S., particularly in Mumbai. And we increased other sales and support roles too. Our production costs were higher primarily due to sub-advisory fees and other costs related to the launch of our mutual funds and we continue to scale and transfer assets here.

And other company-wide production costs were up too, as we transitioned from our on-prem data centers and products to the cloud with Amazon Web Services. So, this is an important infrastructure investment and here we're trading CapEx for OpEx going forward over the long-term. And finally, our real estate cost increased due to planned expansions and renewals and we're focused on our footprint and I'll touch on that a bit later.

Business Mix

So, our business composition has also changed over the years, which has an impact on margin. On the left-hand side of the page, you can see that revenue composition by type in 2019, with 18% of the business classified as asset-based, which includes Investment Management, Workplace and Index products and about 13% transaction-based, which now includes Credit Ratings. So, this picture doesn't fully reflect the full year of DBRS Morningstar in 2019. And if you use the first quarter as a representation, transaction-based revenue will be closer to about 16%. So, we're a bit more weighted to these categories today versus where we were in the past. And if you go back two years, our asset-based and transaction-based revenue was lower compared to today pro forma for a full year of DBRS and that has some implications as you see on the right.

So, we thought it would be helpful to share estimated margins for our product groupings relative to the Morningstar total. And for reference, we did estimates of EBITDA margin, making some higher-level assumptions to fully allocate corporate costs and shared service costs. So, please use this as a directional representation.

First, our licensed-based margins are higher in aggregate than the total of Morningstar and the highest in the portfolio. And that shouldn't be too surprising to you given that we have larger and leverageable areas here. And across the licensed-based portfolio, we are still investing in areas like PitchBook to support growth, with more in sales, in client service and product development resources and in migrating Morningstar software products like Direct from desktop to web-based solutions and building out more robust data sets like public equity data and fixed income data.

Our asset-based margins in aggregate are below the corporate average and next in order of licensed-based. So, although lower, our margins are really healthy here and we're confident in our growth opportunities. And recent investments reflect our launch of the mutual funds within Investment Management and infrastructure to better support technology in our advisor clients.

In Workplace, we've added resources and development for our recent product launches of Morningstar Plan Advantage, and advisor managed accounts, which are gaining real traction in the marketplace, but there are lags between our investment and asset accumulation. And Indexes is also an area where we have significant future opportunity and we just hired some great industry talent to help accelerate our growth strategy.

And finally, our transaction-based margins fall below asset-based and are also below the Company average. Within this category, we have ad sales on Morningstar.com, which have high margins, although sales were down last year, which had a direct impact on the bottom line. And DBRS Morningstar is included in here and that's currently below the corporate average. But remember here that we combined our legacy MCR business with DBRS and MCR had much lower margin profile, given its smaller size, which is also having an impact on the combined business as we continue to integrate.

Comparisons to Peers

And while absolute margins are important, we thought it would be helpful to compare our financial metrics against some of our peers. This slide gives some comparisons across key measurements with a peer group that includes Envestnet, FactSet, Moody's, MSCI, SEI and S&P. While our business is not a perfect comparison in size or product lines or geographies, these are still useful comparisons and we show ranges here across four metrics and where we fit on the scale. Everything here is derived from public data with definitions footnoted for you to take a look at later.

So, first, if you look at the third row, our 2019 EBITDA margins are in the middle of the range and frankly, below several of our peers. But our business mix is different and as we've said before, we match up well in margin in several comparable product areas. But if you look across other metrics, namely top line growth on a three-year basis and a one-year organic basis, we're close to the top with only one peer above us in each category. And this should give you confidence that growth is coming from successful investments.

And finally, last year, we had one of the highest free cash flow conversion metrics across this group, which highlights our strong capital efficiency and cash returns. So, I feel good about where we are and we have opportunity to increase margin over time, but our goal is to grow, but grow smartly, and make sure we continue to balance the short-term and long-term as long as we see the right returns.

Cash Flow Generation

So, I'll close out 2019 with our cash flow progression. 2019 was a record year, supported by the incremental strong cash flow generation of DBRS. Our historically steady cash flow is an important characteristic of the business and gives us flexibility. And while not on the page, our conversion metrics have also progressed well over time.

Q1 2020 Reported Performance

I'll now turn to 2020 and start with our first quarter financial performance. As you know, we released earnings and filed the 10-Q a couple weeks ago. So, hopefully, you've all had a chance to take a look at that. And we had a good start to the year, revenue was up 25% and that includes the contribution from DBRS. And while not on the page, organic growth was 11.6%. That was the highest level of growth we've seen since the first quarter of 2018. Adjusted operating income was up over 12% and that's important. And although that's below the rate of revenue growth, it was the highest growth rate over the past few quarters, and we did see a sequential improvement in margin. And cash flow is down, but that was expected to start the year due to the inclusion of 2019 DBRS bonus payments in the first quarter.

Key Products and Investment Area Growth: Q1 2020 vs Q1 2019

Here's a quick snapshot of our product revenue in the first quarter, which gives a picture of where organic growth came from. This group represents about 80% of our total revenue. You can see that we had continued demand for software and data products, some of that from good carryforward from our Q4 sales performance, which helped drive our licensed-based products. In Investment Management and Workplace, you can see double digit growth. Revenue was up in both, from increases in managed portfolios and managed retirement accounts. And while the market declined sharply in March and investor behavior changed, our revenue here is tied to how our variable fee contracts work, which can include advance billing or based on average daily AUM levels. And for other areas, particularly in Workplace, we rely on client reporting, which comes in after the end of the quarter. So, that means we tend to see lags between movements in asset levels and how that resulting revenue flows through to the P&L.

And in Credit Ratings, we added about $37 million in revenue year-over-year and that's the big driver of the 25% growth number we saw earlier. And we don't have the year-over-year organic comparisons yet. That will happen in Q3 as we lap the deal. And I can say that in January and February, we started off pretty positively and then started to see some of the impact of the tightening credit markets in March on billings and revenue for new issue ratings. It's important to know that close to 40% of the revenue in Credit Ratings for the quarter was more recurring in nature. And that's tied to credit surveillance, research, other services, which helped support the underlying performance. But overall, we're really pleased with the progress of the acquisition and integration work so far.

Business Impacts in Current Environment

I thought it would be helpful to highlight our revenue categories and things we have seen and are watching, as we progress into the second quarter, given the market and economic environment that we're facing. Our licensed-based revenue tends to be more recurring with annual subscription revenue. We did not see much of an impact in Q1 and are watching the sales pipeline, new business opportunities and client renewals closely. Our second quarter sales performance will be an important indicator as we look forward.

Our asset-based areas are heavily dependent on asset levels, as most of our fees are basis point driven. And as I mentioned, there are lags here and we'll start to see the impacts of market volatility from Q1 impacts on revenue in the second quarter. And as always, future quarters will also be dependent on market performance and investment flows. And our transactional revenue is now tied more closely to credit ratings and the new issue environment, particularly, for us in structured finance. The good news here is that the pipeline remains strong and as things stabilized and return, we'll be ready to actively work with issuers.

Looking Back at Last Downturn: Revenue Composition

So, given the current environment, we thought it would be helpful to take a look at how the business performed during the last downturn. Realize that this is not a perfect comparison or a future indicator of performance. So, to start, the size of our business and the mix of our business is a bit different today than it was back in 2008 at the start of the financial crisis. We're larger and more diverse today and that's a good thing. And about two-thirds of our revenue today is licensed-based versus about three-quarters in 2008. And while those percentages are down, revenue here was over $800 million in 2019, which is significant given that this is more recurring.

We also have larger asset-based areas today in terms of dollar size and that gives us more exposure to market fluctuations, as revenue in these areas are tied to total assets and we didn't have a Credit Ratings business back in 2008. And while this is a larger piece of the puzzle today, recognize that with DBRS, we have greater product and geographic diversity in Credit Ratings with certain components of recurring revenue. So, overall, we have some more exposure to market conditions today. But we have a much larger business with more scale and product diversity, which is really important.

Looking Back at Last Downturn: Business Performance

With that context, I also thought it was helpful to take a look back at how our business performed in that period. And here we show revenue and reported operating income along with organic growth rates and margins. So, let's focus on the 2009 shaded columns where we saw most of the impact.

So, that year our reported revenue declined about 5% from 2008 and organic revenue declined about 9%. If you breakdown the composition of that organic number, our asset-based revenue, which was primarily Investment Management back then, declined about 20%, while licensed-based areas declined about 4%. That highlights the correlations of Investment Management and the markets. But importantly, that highlights some of the resiliency for more of our recurring data and software revenue during that period, which held up particularly well. We saw the revenue trajectory recover in 2010 and 2011, which was supported by new business and renewal rates increasing and eventual flow through with some of the acquisitions that we did.

And then, if you turn to margins here, you can see that they declined in 2009 by about 160 basis points. So, we were able to mitigate much of the revenue impact that year and that's because we took some very deliberate and important actions to hold on to margin and protect near term profitability. Those actions were around restrictions in hiring, pulling back on discretionary spend, reducing certain compensation and benefits, and you had some variable components there like bonus and commissions being lower. Margins didn't fully recover over the next couple of years and as economic conditions started to improve, we did increase hiring and spend areas to grow the business. But the more important factor there was the level of M&A activity and that was the larger driver because of the some of the dilution that those deals added to margins in the ensuing years.

Looking Back at Last Downturn: Capital Deployment

In the last downturn, we were able to retain our people, we were able to invest in organic opportunities and importantly, use our balance sheet and cash flow to still make good long-term capital allocation decisions. And you can see back in 2008 through 2010, we were opportunistic and primarily used our steady excess cash flow to do acquisitions. And over that period, we did over 15 deals, which really helped position the business for future growth and value creation.

Actions in Current Environment

So, we're at this period now proceeding with caution and first and foremost, we're supporting our people, we're supporting our clients and our business and making sure that our team members are taken care of and our infrastructure is holding up. We want to be prudent as we continue to monitor the business and external environment and we're already taking some action to mitigate potential business impacts. We've slowed hiring meaningfully and are taking a role-by-role approach to make sure we're still supporting critical needs of the business. We've reduced discretionary spend like travel and certain professional fees and marketing and events. And we're reviewing compensation related alternatives as we continue to evaluate business performance.

So, protecting the P&L in the short-term is really important. But also, the long-term perspective is critical and we're working to ensure that key projects and programs remain on track to deliver desired results and support our organic growth opportunities.

We're also looking at our real estate portfolio in the context of future needs and recent acquisitions to assess what the future work requirements would be. We have some upcoming projects getting focus, including our office relocation in Mumbai. And part of our real estate and workforce strategy is looking at technology and data and development teams to make sure we've got the right Centers of Excellence in certain geographies and leveraging outside resources for certain activities.

And finally, we'll continue to be thoughtful around M&A and use our balance sheet wisely to create value. And as you know, we closed our acquisition of PlanPlus Global in Canada in early April and we're excited to announce Sustainalytics acquisition last month as well.

Balance Sheet and Liquidity as of March 31, 2020

So, if we turn to the balance sheet, at the end of the quarter, we're in a strong liquidity position. That's important to allow us to operate in this environment, maintain flexibility and importantly be opportunistic. At the end of March, we had over $320 million in cash and $210 million in capacity under our $300 million revolver. We're also putting a new $50 million short-term facility in place in conjunction with the Sustainalytics acquisition. So, although we have over $500 million of debt on the balance sheet, we have no near-term maturities. And our overall leverage is very manageable. Our gross leverage was less than 1.5x at the end of March based on the definition in our credit facility. So, we feel really good about our position and capacity and have a real cash mindset here as we approach the rest of the year.

ROIC: Return On Invested Capital

Let's turn to returns. Our return on invested capital dropped at the end of 2019. But that was really due to the significant size and backend timing of the DBRS acquisition, but still remains above our cost of capital.

MORN Total Return

And importantly, our shareholder returns have been positive relative to the market, given our stock price performance. So, we're now ahead of the market across all time periods, even the longer-term horizons, which was not necessarily the case at this time last year.

Concluding Remarks

So, as I said last year and I'll say it again, this is a nice chart, but it's not a victory lap. Our job is to continue to work for our team, our clients and all of our stakeholders to make sure we're making the right decisions, particularly, in times like this to come out even stronger. And with that focus and staying true to our mission to empower investor success, I'm confident in our ability to continue to capitalize on opportunities ahead of us and drive long-term value creation. So, thanks again for the time and appreciate the partnership.

Now, I'm going to introduce my colleague Detlef to you. And I'd like to acknowledge the great addition that he's been to the organization and the entire DBRS team for that matter. Things are progressing really well, and the team deserves a lot of credit. Detlef has brought great leadership, critical thinking, compassion and focus to Morningstar and not just for the Credit Ratings business, but beyond. I really value his partnership and insight and I'm glad that you're all getting a chance to see that firsthand.

So, Detlef, over to you.

DBRS Morningstar Credit Ratings – Detlef Scholz

Detlef Scholz, President, DBRS Morningstar: Welcome to the session on Credit Ratings. My name is Detlef Scholz, I am heading the global business for DBRS Morningstar. I have been in the credit rating industry now for 25 years, 20-plus years, working for one of the leading competitors, pretty much in all analytical functions, but also last years in ratings management before more importantly, I accepted the invitation to join DBRS five years ago with a focus on building out the European footprint. And then last August, I accepted the invitation to head the combined business at DBRS Morningstar.

Credit Ratings Business Model

Before we go into any details, let me recap a little bit the business model of credit rating agencies. It's such a powerful product that most of you are familiar with. It's a global language starting with AAA ratings as being the lowest credit risk going all the way down to a D standing for default. Now, the business model itself has very high barriers to entry when you like to operate on a global basis. That's because of the required regulatory conditions, but even more important because you require a long track record to acceptance and credibility with institutional investors.

Now, there are different ways to operate and the leading rating agencies in all markets have turned to an issuer-pay model. The alternative is an investor-pay. However, the ratings under an investor-pay would only be available to the subscribers, while the issuer-pay model offers a benefit that the ratings are universally available to everyone and allow the comparability of credits across sectors and regions.

Now, any of the business models has a potential inherent conflict of interest that needs to be well managed. On the investor side, the conflict of interest would be that as an existing investor, you don't want to have your portfolio being downgraded. As a future investor, you'd rather like to have a low rating in order to gain relative on the price. And on the issuer side, the inherent conflicts are quite obvious. So, the important one is and that's why the industry is so regulated that the rating agencies assign their opinions free of whoever is paying it and that's a separation of the analytical work and the business area.

History of Credit Ratings at Morningstar

Now, with that, let me actually move to the history of Credit Ratings at Morningstar. Morningstar already had, pre-acquisition of DBRS, a full-service rating, which means that all relevant areas such as corporate ratings, financial ratings and many segments listed in structured finance were already covered through methodologies. Then building up over a 10-year period, step-by-step, the required recognitions, regulations, methodologies, up until last year when the opportunity came to purchase DBRS. And by doing that, it's accelerated this organic growth over the last decade by gaining international recognitions, but also much broader footprint. Now, the initial decision, very important to highlight, was on the back of the last financial crisis and the opportunity to have a different view, an alternative, to legacy rating agencies available to the marketplace.

DBRS History

Now, let me turn to the history at DBRS. It goes back to 45 years with a Canadian business, for many years a domestic business, but then at the turn of the century took the step to move into the U.S. and then, by 2006 had gained the 6th position on a global basis and then further with the re-launch after the financial crisis, a hub in London to cover Europe. And then, by 2014, it was already the number four on a global basis. And then, well ahead of Brexit, also the move to continental Europe. And you see actually by the different colors that the European business did grow as the U.S. business on top of the Canadian operation.

2018 DBRS and Morningstar

Now, when you put Morningstar Credit Ratings and DBRS together, you're getting a nice portfolio with a stronger presence in the U.S. market, but also the well-balanced and existing and robust business in Canada, plus the increasing opportunity through the European footprint.

Diversification in Asset Classes

And at the same time when you look at the underlying segments in each region that are being covered, you see a tremendous amount of diversity by asset classes, looking at the different sub-segments. It ultimately helps the different parts of the business, responding to issuance, trends, opportunities differently. So, there's much more diversity than what you would have assumed at the first look at just at the regional level.

Competitive Landscape

Now, with that, let me move on, on how we service a market with our focus on investor success, which is our mission across all businesses at Morningstar, and equally, highly relevant for our Credit Ratings business on the fixed income side.

In order to understand the competitive landscape, I think there's an easy picture you can draw where you look at your local footprint versus global capabilities on the left hand side, and then you also look at how much coverage you have and ultimately how many sub-segments that are being able to service and cover through your credit ratings.

And you really see a bifurcation here. You have a whole number of rating agencies and there are many more that would fall into this lower left. Some of them are on the lower left-hand side because they only focus on one industry, such as they invest on the insurance side, or others like HR Ratings in Mexico or Scope in Continental Europe, they are domestic or regional players.

And then, on the other side, you have some of the leading global rating agencies that you all have heard about. They're both the global capability is well established, but also the rating coverage in each market segment is good. And I believe we are the only player that is positioned both to oversee global capability side with the ability to move the coverage step-by-step by looking at adjacencies of our existing business. And that makes this combination of Morningstar Credit Ratings and DBRS so unique.

Moat, Strategy, Opportunity

With that, let me actually tell you a little bit how I look at our positioning in our core regions and where you also see easily our next steps and how we like to further develop our footprint. So, on the left-hand side, you see some of the segments I discussed before, corporate ratings, financial institutions ratings. Sovereign rating stands for government debt ratings. And then, the various segments in structured finance, securitizations, but then also data products. And in Canada, given our 45 years history, we are a leading player and I define a leading player that is really a market coverage that is the best, leading and ultimately, given that many fixed income instruments sold to market have two ratings, we are one of the two ratings on the vast majority of the issuance in those particular subjects. And defending this is our ambition for Canada. We have a high moat. Our franchise is well known, and others would rather look at our market segment and see us as the leading player.

Now, in Europe, you see in some segments, in structured finance, we already are viewed as a leading player, while in others we have established our ratings capabilities. And then, on structured credits and on the data side, these are investment opportunities to further develop off of it. And the way we have developed the European business over the last five years was always looking at a segment where we had a value-add or a differentiating opinion. And once the market was convinced about our views, we then looked at next adjacency and ultimately executed there in the same way. And that actually helped in combination with structured finance and bank ratings that many markets have some protection. But then also more recently, since 2016, on the corporate rating side, we invested that our analysts, our methodologies, and then ultimately, the market is starting to use us more and more.

And in the U.S., through the combination of both Morningstar and DBRS we have very good and leading coverage in some of the segments of structured finance. We have established capabilities on the financial institutions side and our focus, clearly, given the tremendous size of the U.S. corporate rating market is doing all the steps needed in order to execute there. And the way we will enter, as we did in Europe, the corporate rating market is looking first of those segments, which are typically private ratings and private placements, where in the middle market segment where we are less exposed to some of the index products that are certainly driving some of the key investments. And once we have established our foothold there, we can then look at the next segments, that is, infrastructure, project finance, and step-by-step develop also our footprint in those areas, where we are not viewed as a leading player yet. And over time, our ambition is to be the alternative to the legacy three rating agencies also for the U.S. market.

Target Market and Our Opportunities

Let me move on now to describing a little bit the overall market, but also then our opportunities, and then, give you an example of how we like to differentiate through technology but also the way we work and have a value proposition that is attractive to the investors that we like to serve.

Total Addressable Market Opportunity

So, as I mentioned, let me focus on the addressable market first. Overall, the size of the market relative to what we currently cover allows a lot of headroom. Now, these are our estimates, but then, if you look at our turnover versus the market, there's for the time being no limit to grow into the existing market. And the market continues overall to develop further, and it's primarily driven through the increasing an additional disintermediation of the credit markets where institutional investors tap, from an investment perspective the market directly while issuers are not necessarily going through bank funding but ultimately seek the institutional money directly and this applies both to the private, but also to the public market.

Now, there is also more opportunity through to the, what I call, componentizing of credit book, embedding our components of analysis, our views in the workflow of investors and other intermediaries. But there's also work on the data and analytics product side where rating agencies can contribute. And then, with more and more sustainable investment, there are also opportunities in order to provide a full range of products in order to make the modern investor fully informed regarding their investment decisions.

Periods of Market Volatility Highlight Opportunities

So, now, turning to the opportunities that I see ahead of us. So, first of all, this is the time because of the crisis where I don't need to explain to you how important credit is. The last three months and the time to come shows that there's much more focus on credit analysis in order to look at the impact. And at the same time, we see volatility in the market where credit spreads are moving and obviously, some transactions are being delayed or substituted through other issuance in the market. Very important also to point out that some of the government emergency programs offer new opportunities to us, whether it's our ratings done on a routine basis where the collateral is being used to seek liquidity from the central banks, or alternatively, some credit assessments also being used by governing bodies, including central banks in Europe, but also in North America for their own assessment of the risk of some of the emergency corporates.

Now, equally, it's very important to show that our opportunity is in the way we operate, how we use technology, how our operations are different and let me go back to my own experience working for a company that has more modern technology stacks and is more nimble and more agile is one of the key benefits compared to my own experience at one of the previous opportunities that I had.

Now, very important for me is also the way that a crisis offers opportunity. And DBRS came out of the last financial crisis on a stronger basis as we did have a different view on credit, more a look-through rating philosophy applied to credit. And the one example I'd like to give to you is the way we look at government debt during the euro crisis where to take Portugal as an example, we had been criticized as being the lowest rating agency at the beginning of our own rating coverage of Portugal. And then we were criticized through the crisis that we had the highest rating. And then, at the end of all that the rating agencies aligned at similar levels again, with the one observation that we had the most stable rating through the crisis and never dropped Portugal to the below investment grade level. That's one of the examples where a different view, diversity of opinion, is helping everyone in the marketplace so that the investor side can read through the rationale of the ratings and decide which component they like to use for their own analysis.

Now, when I talked about technology and differentiation, and before I wrap up, let me give you an example, in order to show how we combine analytics and transparency, and this particular platform I show you is what we call Viewpoint, which is a map-based platform to dive into all the CMBS and commercial real estate transactions going back to late 1990s. And you can look at it at a portfolio level, you can then dive into a transaction level, you can then look at a loan level to the underlying real estate markets by going into the combination of market data on cap rates or rental levels, combining that with the loan exposures we have. You can then, as you would expect in the crisis, look at our research and rating actions that may impact only your defined portfolio and equally, you can then overlay exposures to tenants or certain regional exposure and figure out how much you are concerned or not about your portfolio. And combined with all that you can do a deep dive also in our own commentary, pictures from our site inspections all the analytical rationale supporting our rating analysis.

And before I summarize here, for me, sitting in Europe important to say that this is not only working for the U.S. and Canada but also for Europe, and there's even a sister product we have available on residential mortgage securitizations in Europe.

The Next Generation of Credit Ratings

So, with that, let me summarize what I try to highlight and why I call our business the next generation of credit ratings. It's very important to me to provide transparency on the analysis to offer investors diversity of opinion, given that different views, make it easier for the investor side to understand the different components of credit and then draw their own conclusions, and combined with our more nimble and agile approach to be responsive and more customer-focused in the marketplace.

With that, thank you very much.

Question-And-Answer

Kunal Kapoor: Great. Well, thank you everyone, Jason and Detlef, for those terrific presentations. We're now going to be moving to the Q&A portion of this meeting. It's always, I think, my favorite part of the meeting. But hopefully, you enjoyed the presentations and they set the stage for some good conversation here in the next hour.

I wanted to point out that Detlef was showcasing Viewpoint. And in the shareholder packet that we sent around, you have a login to Viewpoint included. So, we hope you'll take advantage of it and also take advantage of some of the additional Morningstar goodies that we tried to put in there, unlike in the past, where we've tried to have demos in our offices, that was obviously challenging, but we're hopeful that you will be able to take advantage of what we sent over to you.

I'm going to be joined in this Q&A by Detlef who you just heard from, Jason and Bevin Desmond, our Head of Talent & Culture as well. So, four of us will be taking questions from you.

But before I jump in, it's taken a lot, obviously to run this presentation or set of presentations remotely. And I want to recognize the Morningstar team that's done such a nice job in bringing this to life. So, Barb Noverini, who heads up our Investor Relations; Scott Halver, who is doing all the video here today and he does an amazing job for us; Kristin Nehls; Regina Comito; Evangelina Ramirez; and Teresa Jessee. Thank you to all of you for enabling this and making it work as seamlessly as it is working.

Now, for everyone on the webinar, I know you're itching to start asking questions and so let me share with you what we're going to do so it's easy for everyone. So, if you look at your Zoom screen, the easiest way to ask a question is to click the Raise Your Hand button at the bottom of your Zoom window. This will allow you to ask questions live, either using your camera and microphone, or just your mic. The camera is our preferred way to take questions. We think it's important to see each other face to face just as we would at a live meeting, and we think it just enriches the experience for everyone. So, we'd like to hear from you in that fashion.

When we select you to ask your questions, Barb will move you to the main meeting room and you'll experience a slight pause as you're admitted into the webinar to ask your questions. So, don't worry. You won't be dropped; you're just being moved. And we'll then prompt you to ask that question. If for some reason you're unable to ask a question live, you can indeed type in a question in the Q&A box and we will take questions that way as well, although we're going to prioritize the live questions first and foremost, but we'll try to get to everything here in the next hour and try to answer your questions as clearly as possible. And if we don't get to a couple, we'll do what we've done in the past, which is that we will answer them in an 8-K after the event. So, we've practiced all of this, as you can imagine, with Q&A technology, and Morningstar has been a longtime user of Zoom. So, I think this should work fairly seamlessly. But we appreciate your patience as we get going here. And I'll turn it over now to Barb and all of you. So, you can go ahead and pick a question if you'd like Barb and we can get rolling.

Barbara Noverini, Director of Investor Relations, Morningstar: Thanks. Once again, if you'd like to ask your question live, please click on the Raise Hand feature and just wait for us to call you because you'll be placed into a queue. And the first question comes from Arthur Baptist. Arthur, go ahead and ask your question.

Arthur Baptist, Golden Gate Capital: Great. Thank you, guys. Good to see you this way. Sorry for not making it to Chicago. I did just want to ask one on the asset-based businesses. So, if I go back – we've been attending this meeting since 2016 and since we became shareholders, and if I go back, the Workplace Solutions and Managed Portfolios, those were identified as growth areas at the time kind of businesses that could add $100 million plus of revenue. If you look at the performance of those, the revenue hasn't tracked, and you made some comments around that in the opening remarks. I was just curious, kind of, do you think now we've gotten through and some of that has stabilized and we can start to see the revenue accelerating or just kind of going forward, how should we think about the revenue growth of those business areas within asset-based?

Kunal Kapoor: Yeah, thanks. It's a fair question. And Jason, I'll start and if you want to weigh in as well, that's great. We continue to think that those are large opportunities and I'll take them both slightly separately. In Investment Management, Arthur, if you recall, we've been on a trajectory to move away from what used to be largely a consulting business to focus on our Managed Portfolios business. And for the most part, we have made that transition. But there continue to be some areas where that transition will be made. Now, if I look at the opportunity for that business, it is significant. And we're doing a lot of things right as we sort of set up this business in a few key markets around the world.

So, we've concentrated the Investment Management business in the U.S., in the UK, Australia and South Africa today, with some potential growth opportunities in India longer term, but that's the areas of focus. And I think it can certainly grow meaningfully from here. Obviously, with the recent crisis that we're having, that does impede the trajectory that the business was on and I think it's fair to say that the team has gone from focusing on growth to really focusing on servicing the heck out of clients in the near term. And I do think the pace at which we return to a more normalized environment will have an impact on the trajectory of that business.

With Workplace Solutions, the core part of the business, which is Managed Accounts, continues to do well. The partnerships that we have continue to do well, and one of the reasons actually, that perhaps revenues have not grown as quickly as assets is because we've hit breakpoints because we've been so successful with certain partners. We are also seeing really good traction, as I was saying earlier, with our offering for advisors, and it's obviously a service that takes a little while, while you get all the record keepers set up and connected, and we are in the process of doing that this year. We have a lot of people who are interested, signed up. And if you talk to Brock Johnson who runs that part of the business, I think we view it as a very significant growth opportunity that will power that business. So, we're very bullish on that part of the business.

Arthur Baptist: And maybe just as a quick follow-up on the asset-based business model more broadly as we think about this environment. Any kind of metrics you can try to give us as we think about modeling through the downturn, like what percent is equity-linked, how much kind of booked in advance versus bills in arrears, just any of those metrics that we could think about modeling the business through the downturn.

Kunal Kapoor: Yeah, it's a good question. Jason, why don't you take it?

Jason Dubinsky: Yeah. So, maybe without getting – maybe a couple of factors you can take a look at is just – just around the average AUM over the periods. But I think that's where we tried to give you a bit of a look back to '08 and '09 and how the business performed, I think, particularly Investment Management, when it was the predominant asset-based revenue back in '08-'09. So, it's not absolute, but I think you can kind of look at that as a guide of the revenue performance then relative to the market performance as a good indicator today.

Arthur Baptist: Thank you. I'll get back in line.

Barbara Noverini: Thanks. And as a reminder, if you'd like to ask a question, please raise your hand and we'll get you into the queue. We do have a question in the Q&A box. And this is from Daniel Lee, from OMD Ventures. How do you measure your return on investment in talent? And would you please expand on what unique systems Morningstar has implemented to develop talent bottom-up?

Kunal Kapoor: Bevin, why don't you take this one?

Bevin Desmond: Sure. Thanks for the question. I'll start with the building talent up for Morningstar, which is a really important part of our business success, being able to build our subject matter experts, our innovators, our people who are ensuring we have quality data. So, that investment knowledge and product leadership and thought leadership is only built over time. So, we have found it very successful to build a lot of our own talent from scratch. We have a practice of hiring a large amount of our workforce right out of school around the world. And we have a rotation program that allows them to experience many different parts of Morningstar and then tracks in the most important parts of our business to us. For example, we have an investment management track, a research track. And this allows people to really build expertise. In fact, many of our leaders across Morningstar are experts we built ourselves including Kunal Kapoor, our CEO. So, those practices are very important to our business around the world and are in place – any place where we're growing our talent and building our business.

On the second part of the question, I'll see if Jason wants to answer that one on how we measure our return on talent.

Jason Dubinsky: I'd say the return on talent is probably directly correlated to where we're investing across the business. I think if you look at the – in fact the expense profile of the Company, it's heavily weighted towards compensation costs, which is heavily weighted towards headcount. So, I think if you look at where we've been adding headcount over the past few years, it's primarily in those key investment areas that we keep talking about that Kunal mentioned, where we're seeing more outsized revenue growth for the company and disproportionate cash flow contribution. So, I think our measurement in talent is just how our teams are adding into supporting to growth in the areas that we're focused.

Barbara Noverini: Okay. Thank you. Then our next question will come from Jordan McNamee. Jordan, please ask your question. Jordan, you may be muted, but go ahead and ask your question. Jordan, you look like you're unmuted now. There we see you, Jordan. Jordan, we're still having trouble hearing you. All right, what we can do is, Jordan, I will place you on hold and come back to you and we'll give you a chance to answer your question. The next question comes from Mindee Wasserman. Mindee, go ahead and ask your question please.

Mindee Wasserman: Can you hear me now?

Barbara Noverini: Sure, I can.

Mindee Wasserman: What are the outflows or inflows of equity funds, debt funds, and also money market funds? You recently had an April report, but could you elaborate on that? And do you also have data on the percentage of small business, sole proprietors or is it general population that are investing in mutual funds or the stock market?

Jason Dubinsky: Go ahead, Kunal.

Kunal Kapoor: Mindee, I'm happy to take your question. I think you were asking largely about flows into different asset classes during the recent times. If that's accurate, if you look at our data and some of the reports that we've put out based on some of the data we collect and published in Direct, we saw some historic outflows in assets, particularly from equities during the month of March. We saw some stabilization in April, but it has been a little bit of an up and down period. If you're asking about May flows, those will be reported later on at the end of this month. But our impression and some of the work that we've been doing too shows that investors who have used managed accounts, for example, have tended to stay put.

So, one of the interesting pieces of research that our Workplace team was able to do is look at folks who are using managed accounts, for example, and it's interesting that they've stayed the course even though there's been a lot more volatility in assets. But Mindee, we're happy to sort of send you our full report on asset flows that we publish.

And so, we'll be sure to do that after the meeting as well. If anyone else is interested, let us know. We can send that over.

Mindee Wasserman: There was information on debt outflows also, but I don't think you included money market flows.

Kunal Kapoor: Correct. Correct.

Barbara Noverini: Okay. Thank you very much for your question, Mindee. We're going to try Jordan one more time. Yeah, we can hear you now.

Jordan McNamee, Cambridge Global Asset Management: I appreciate all the incremental conversations around the DBRS acquisition, but I just about – if we look out five years from now, how should we think about what success looks like for that acquisition?

Kunal Kapoor: Yeah, good question. Detlef, seems like this is a good one for you to weigh in on first and foremost.

Detlef Scholz: Leading example of what our ambitions are going forward. But before I talk about building business, keep in mind that we equally have experience and need to focus on defending our leading positions in some segments as I tried to say earlier, and in particular, Canada is an excellent example where we already are and like to stay the market leader.

Now, when it comes to building segment by segment, I think we are well positioned clearly on the structured finance asset classes that I mentioned. And when you look at my chart previously, there's more green than blue and the blue was saying we have potential to develop based on already existing capabilities.

Now, obviously, the key measure of success over such a five, maybe seven-year, maybe even 10-year period is to grow in corporate ratings in the regions we operate. And there is a lot for us to do certainly as we already started in Europe, but in America to have more diversity of opinion, and having a strong fourth player is clearly an ambition in front of us. But I'd like to manage your expectation that this is really a very thoughtful step-by-step approach that you effectively create the value, the understanding for our opinions, and execute segment by segment. And as I tried to say earlier, in the U.S., but the same applies elsewhere, I think the first segments are clearly private placements. The middle market segment, the middle lending market, is very important to us, but also those areas which are closer to our already existing coverage on the transaction-based side, in infrastructure as well as in project finance, are very good segments where you should be able to see over the next few years our success, hopefully, segment by segment, region by region.

Jordan McNamee: Can I ask a follow-up?

Barbara Noverini: Sure. Go ahead.

Jordan McNamee: Just looking at the advisor market, clearly there's a mix shift to the RIA channel, which presumably is a positive for you. But then also just looking at within like the investment management market where I look at our own firm, we're using a lot more like alternative research tools like GLG or other expert networks and different data providers instead of just like the typical equity research approach. So, I'm just curious when you look at investment management versus wealth management, where do you think there's the most opportunity for disruption and opportunity for different types of data providers or software providers like yourself?

Kunal Kapoor: Yeah, I'm happy to take that question. So, Jordan, I think your question is largely around sort of the evolving landscape of financial advice probably in the U.S. in particular, and what that means. And so, first of all, just to take a step back, we have really great penetration across the board in the financial advisor landscape, both here in the U.S. and across the world, and we serve advisors in multiple ways. Some advisors we serve with essentially what we like to say is a solution where they can build portfolios themselves or build a financial plan themselves. So, what they're doing in that instance is using our data using our software and working with the client more directly. Or there are some advisors who simply want to outsource the work that they're doing. And so, in those instances, we're often going to them with our managed portfolios offering and working with them in that type of capacity.

Now, I think what you're pointing to is that increasingly the challenge for advisors is really to prove that they are delivering value to the end client. And so, different advisors are choosing to do that in different ways. The subset of advisors who are truly starting to go and focus on alternatives, as you are pointing to, is still relatively small but growing. And our ways of playing that are largely in a couple of ways. One is, we are building up our data capabilities in areas not only that we've had a presence in, i.e., equities, but expanding beyond that. Similarly, we're doing that with research as well.

So, simple example is that more and more advisors are using a separate account of some kind and building portfolios using those separate accounts. Or they're buying managed portfolios. Historically, there hasn't been data or research around those types of things, and we want to be there and start to provide that type of data and research. Or for advisors who are moving into private equity and kind of into sort of more esoteric spaces, we are positioning PitchBook as a use case for them, although I will caution that at this stage there are very few who have kind of started to use it in that fashion. But I expect as more start to that that will start to become the case.

But the most important thing and this is critical – as we think of our data capabilities really being born out of the investor portfolio. And as the investor portfolio evolves in the way that you're talking about it, we want to have the data to help basically demystify that portfolio and then provide IP and research on top of it. So, the steps we've taken in the past few years, whether that is adding more to fixed income, doing more with alternatives, recently adding a stable value funds, buying PitchBook, all these things are our steps that ultimately allow us to demystify a portfolio in a more meaningful manner.

Jordan McNamee: Is the managed funds portion, could that – like the PitchBook assets seem really interesting. And I understand where your managed funds is today. But I'm thinking more about like, even like companies like Hamilton Lane and different types of asset allocation solutions to the private market, which seems to be growing rapidly, I'm curious on your thoughts on that as an opportunity for Morningstar down the road.

Kunal Kapoor: Yeah, I think, certainly, we evaluate all those types of opportunities and think about them. If Daniel Needham, who heads up that part of our business was here today, he would probably say too that – one thing of caution from his perspective right now in terms of getting too excited about launching something in that space is that the returns have been so strong up to this point, you risk sort of bringing in investors at exactly the wrong time and essentially burning them. So, we're having those conversations and one of the things we've been able to do in our Investment Management unit as well is we've experimented outside the U.S. a little bit particularly in Australia and done a few things there, and then tried to bring that over to the U.S. But candidly, we have not gone to the extent to sort of thinking about managing money in the way that you are suggesting, at least as of today.

Jordan McNamee: I'll jump in the queue. Thanks.

Barbara Noverini: Thank you, Jordon. Our next question comes from Will Slocum from Golden Gate Capital.

Will Slocum, Golden Gate Capital: Barbara, nice to see you, Bevin as well. Just a question – again, we've been really impressed by the growth and appreciate as shareholders, you've done a great job. Would there be – it's more sort of prospectively, but would you be able to provide a little bit more context on your operating investment in growth? And so, in cases where you've taken down margins or margins have come down naturally through growth spend, if you can quantify that either on a go-forward basis or in your quarters to say, you know, we've invested 300 basis points in growth and that's how we've gotten up to this 11% growth rate and really help us think through that balance between margins and growth going forward. Maybe you could even talk about it in the 2019 context on a go-forward basis, particularly as growth we expect to slow down. So, how does that how does that impact margins?

Kunal Kapoor: Absolutely. Jason, why don't you take the first crack at this one?

Jason Dubinsky: Yeah. So, I think first the question for Will, so appreciate it, is potentially going forward to provide a bit more clarity in terms of how the investments in growth are translating specifically to the top line and margin. So, noted. So, we can think about that. I'd say before I maybe give a little commentary on, I think what we've been trying to do is continue to provide as much disclosure as we can to enhance that, to make sure you get a good understanding of how a lot of the key investment areas are contributing to the top line performance, trying to break out DBRS Morningstar, just given some of the anomalies of the comparison. So, we're doing our best in the context of what we've got to continue to provide that transparency. So, appreciate the feedback, and we can look to do that.

So, I think how I would answer that more is how I'd looked at the – in kind of the prepared remarks, as you looked at the margin walk from 2018 to 2019, where if you kind of stripped out some of those anomalies, adjusted operating margin was down about 150 basis points. So, I think you could think about that as what I would characterize as the investment in growth. And I think we're paying very careful attention to that. And it's good to look at that over a one-year period but a longer term horizon. And I think if you looked over the past few years, it's those key areas that have had a disproportionate share of growth relative to the rest of Morningstar, where we feel really good. And as I said before, that's really driving a lot of the excess cash flow in these areas. So, we continue to look at that. We'll think about providing a lot more – some of that more disclosure.

But I'll continue to reinforce that we are trying to balance the short-term and the long-term. So, while margin is important, and we know we've got leverage in the business, we do want to make the right trade-offs to drive the top line as well as cash flow in a responsible way. But we're $1.2 billion business today. And we've got ambitions to grow significantly and we have a growth mindset. So, that balance is really important in the context of managing the short-term and the long-term. But please be confident that we're managing that and monitoring it to make sure that the incremental investments are providing the right near-term and long-term returns.

Will Slocum: That's great. And some of those investments that you were talking about in terms of real estate, realignment, and also the shift towards AWS in the cloud. When will we be complete with those programs? I'm sure some are multi-year, but will they start to show up in the financial statements or is that more just operational excellence, like, will you see some step-downs in cost or changes in cost as a result of this?

Jason Dubinsky: Yes. That's a good question. So, the question was around – maybe more around our infrastructure cost as we look at migration to the cloud and Amazon Web Services as well as our real estate portfolio. So, a couple things, too, I think we continue to, let's say, invest in growth opportunities in our product and business lines. But a lot of what we're doing too is making sure that we're shoring up how the core infrastructure of the Company as we as we continue to develop and mature as a business. Those are important infrastructure investments.

So, take the investment in the cloud. And that's really the public cloud. So, I want to differentiate the public cloud between migrating from, let's say, desktop to web-based versions of a lot of our products and applications. So, the public cloud investment where we're trying to get out of the data center business over the long-term, and Amazon is a great way to do that to shore up infrastructure, have better availability, have more flexible models of demand. So, there's a good example where you'll see – we've seen some increase in expense to do that, but you'll see CapEx come down over time, because we're not investing in data centers and hardware to do that.

On the real estate front, we continue to look at our footprint, especially in the context of a lot of the acquisitions where we've got offices now in different locations. So, how we look at that going forward, consolidating space, things that we're looking at, I'm sure as you and your firms and all looking at is what is the future workforce requirement look like post-COVID. So, Real Estate is important, but our people are important too and are our most important assets. We want to make sure that we have the right footprint to accommodate our people. But we continue to evaluate that in the long term to make sure that we've got the right footprint to support our people and support our business.

Barbara Noverini: Our next question comes from the Q&A box. This is from Sid Arora from Brown Brothers Harriman. How are you thinking about additional data monetization opportunities at DBRS? And separately, what opportunities exist to increase the recurring component of DBRS' revenue stream?

Kunal Kapoor: It's a good one for you Detlef. And maybe you could just start by reminding everyone a little bit of what we disclosed in our Q1 earnings in terms of the recurring nature of the current business as a base.

Detlef Scholz: So, DBRS had been what I call a pure-play rating agency, where all the focus was on the repeat nature of some of the, let's call it, existing relationship business, but also then the connection-based environment. And as part of our analysis we are sitting on some great data, and I believe one of the great benefits of now being part of the overall Morningstar family is to make more use of all the treasures that we are sitting on. And as part of that, you see – and that was one of the reasons why my earlier comments I included one of the showcasing platforms – we had approached historically all that in order to get our opinions across and our diversity in terms of how we approach the analysis of our credit. But as one of the obvious steps, and that's why your question I believe is so targeted, there's certainly the opportunity to embed our components of analysis in the workflow of the investor side. And as part of that, you can either directly on the credit rating agency side, but also as part of being the Morningstar family member, certainly monetize some of those opportunities. I think data is certainly the obvious target there. And then, step-by-step, you can also look at some of the products we have and then figure out how you monetize that.

But let me really say, this is step-by-step. And at the moment, I believe we'd like to grow the presence and the thought leadership of our opinion, and all these other opportunities are clearly on our mind. But really, as I said, in developing the rating coverage and the capabilities, that's the first step. I believe we have a lot of runway there. So, some of the data and product opportunities are going to be realized. But I would look at them more as a byproduct of our primary focus in developing our ratings footprint. Maybe Kunal, with that, over to you more from a broader Morningstar perspective.

Kunal Kapoor: No, I think I think you answered the question fully, Detlef. Thank you. I'm not sure I have much to add on that one, Barb. But it's true that ultimately any rewards that flow to tangential parts of the rating business will come from our ability to establish ourselves as an alternative in Europe and the U.S. and kind of get to a leading position as we have in Canada. So, that's exactly right.

Barbara Noverini: Great. Then the next question we have is from Alex Braid from Artisan Partners. Alex, please go ahead and ask your question.

Alex Braid, Artisan Partners: Great. Thanks very much for organizing today. I just want to dig into PitchBook. Looks like you increase the TAM there to $2.3 billion. Firstly, are you able to kind of walk through how you come to that TAM and what's driving the increase? And then, maybe just spend a little bit time on the growth of PitchBook over the last couple of years in terms of the licenses, is that coming from new accounts, increased seats within the new accounts, and how much of that is coming from, say, participants outside kind of the alternatives, corporate M&A, et cetera?

Kunal Kapoor: Sure, Alex. Thanks for asking the question. I'm happy to answer it. So, I think, I think it was a two-part question. The first just broadly on the increase in sort of the total market size available to PitchBook and the second more specifically focused on where PitchBook is growing and how PitchBook is growing. And I'll try to also just, as a part of this answer, answer some of the questions that are in the Q&A around revenue growth versus licensed growth at PitchBook and hopefully, try to answer that as well.

So, Alex, the total addressable market, we are pulling public sources and essentially using those sources, and so they're widely available. We've cited them. It's not an internal estimate. We're basically using the sources that we cited, because we think that they're the right ones and historically have, I think, provided a good idea. And the truth is that that market is growing even just anecdotally, when you look at people entering the market and you look at the pools of assets, there, it's certainly been the case that more and more money is being allocated there.

In terms of PitchBook itself, when we think about the growth of PitchBook, what has become evident to us is that the use cases are multiplying. And when we bought PitchBook about four years ago, the use cases were fairly singular. But now, when you look at what's happened in the markets that PitchBook serves, even the rise of private debt is meaningful, the rise of ESG, you have big private equity firms in the last month or so coming out with meaningful ESG reports. And in Europe, you're having sovereigns basically being very clear that even private equity investments need to be done with an ESG lens. So, you start looking at all these different use cases, and they're pretty meaningful. It's not just sort of the traditional PE fund that might be interested in using PitchBook.

One area of growth, and we've talked about this in the past as well, has been corporates. Clearly, our strategy teams that in the past might just have bought, let's say, a product that looked at public equities now are looking across the board. Because when they're thinking of strategy and M&A, they are looking not just at the competitive set that's public, but the private set as well, as well as startups. And so, we've seen some really steady growth in that part of the market as well. And we think we will continue to have traction there because we're adding more and more on the public side. And our belief is that as PitchBook gets richer, that more folks from the buy side will have an interest in it, and that we will continue to move up market in that regard.

In terms of the way PitchBook has been growing, and perhaps the difference in rate of growth between revenue and license growth, a simple way to think about that is that when we bring people in, we often start them with a fairly base version of PitchBook and base set of capabilities. And then, at the renewal, we see some fairly significant bumps. And this is a strategy that we've seen play out multiple times that once PitchBook is being used within a firm, a couple of things happen, either the user wants to add even more to what they're doing, or they want to add more people around them. And we've seen this with Direct historically as well; you just get embedded into the workflow. And that's sort of what started to happen with PitchBook and it's self-fulfilling. And one of the things that I found really interesting was that in this last downturn here in the past two months, if you look at the coverage at the private markets and look at the media, PitchBook had a disproportionate amount of mindshare in terms of being quoted about the private equity markets. And so, we think we've really just built a great product there. And the use cases will keep growing. And we find that once people are using them, the time of renewal is often the time where we see a significant bump up both in terms of seats getting added and in terms of what people are willing to pay.

Alex Braid: Do you mind if I ask one more question?

Kunal Kapoor: Please go ahead.

Alex Braid: So, recently, – you've owned a stake in Sustainalytics for quite some time but have decided to acquire the entire company recently. What can you do now with Sustainalytics coming on board fully at Morningstar that you couldn't have done in the past? And where do you plan to invest within Sustainalytics moving forward?

Kunal Kapoor: Sure, Alex, and I think Artisan asked a question last year too about Sustainalytics. So, staying consistent, I think, in that regard. So, yes, the question again is what's different now that we potentially will be the owner or full owner of Sustainalytics in the third quarter.

I think the easy answer is, most likely, the thing that we think will start to happen is just speed to market. It removes friction of two firms operating separately. I think we've been well aligned. In general, we have a great partnership, Michael Jantzi and the team at Sustainalytics, are just fantastic people. We work well with them. But there's always a little bit of a mismatch in priorities when you have different things going on. So, you look at something like our Indexes business, driving some focus – we spent some time – our team spent some time this week just thinking about Indexes and ESG and how we accelerate there. It just removes the friction because all teams are on the same page and thinking of moving ahead. And across our portfolio, you just see benefits. An area that Sustainalytics has been growing is in terms of the validation of green bonds and now you sort of link it up with DBRS and some of the things going on at DBRS and you can sort of see the benefits flowing both ways not just to DBRS Morningstar but also to Sustainalytics in terms of how to think about fixed income in a different way. We've never really had Sustainalytics linked up to PitchBook. That's going to be something we look at as well. So, the ability to go deep is significant.

And the other thing that I'll just say is Michael and his team have a lot of ideas. There's no shortage of ideas of how you grow right now. And even just in the past couple of weeks, the increase in demand for labor issue related data or supply chain data, and you think about the investments that could be made to sort of drive that – you know, we've been a good partner to Sustainalytics and our goal here is to fund their growth even further, because the opportunities are significant, and we think we have an opportunity here in the third quarter to take ownership with the leading player in the ESG space. So, we're super excited.

Alex Braid: Great. Thanks very much.

Barbara Noverini: Thank you, Alex. So, to stay on this ESG topic, Kunal will take a question from the Q&A box from Jennifer Fo from Fidelity. Can you talk about what makes you bullish on ESG in the long-term and what you think ESG looks like within investment management five years from now? Is ESG still a niche, albeit a high growth one? Or will it become a broader overlay? And there's also a fair bit of criticism about the quality of ESG data today. What needs to get better and how will it be better five years from now?

Kunal Kapoor: Yeah. A bunch of good questions. And I'll try to take them both separately, but you may have to remind me, Barb, once I answer the first one. Actually, let me take the one on data first and foremost. And if Michael was here, Michael Jantzi was here answering this question for me, and he was talking about standardization, Michael's answer is that, sure, standardization will be helpful, but oftentimes, the criticism around standardization comes from those who are maybe not being rated favorably by the way the data is being presented today. And Michael's point is that there will be standardization in a few years. But the level at which we will standardize the data will be much higher than what people think it's going to be at. And you're already seeing in Europe that there are regulatory moves to think about how that data is standardized. So, I think standardization is a good thing longer term. And I do think it's going to happen. But I agree with Michael's view here that it's going to happen at a much higher level than it is today.

In terms of just the future of ESG, I think it's moving to the center of investing. And what I mean by that is, if you think about it, ESG has been thought of sort of to the side and an additional capability that perhaps you tack on when you're building a portfolio. But really what ESG is about, it's about engaging the end investor in a way that the investor has not been engaged with their investments. Many of us on this call are probably investing geeks, and we'd love to spend time thinking about it, but many of my colleagues at Morningstar remind me that the people we're serving are often not, and the reason that they have so much trouble sticking with their investments, engaging with their investments is because they don't feel like they're personally invested in them. And we think ESG changes that. And you combine that with the ability to use technology to start delivering personalized portfolios to people and allow them to build personalized benchmarks, allow them to express a view of the future in their portfolios, we think that's the way the world is going to go. And having that data not only allows us to provide a richer experience within Morningstar offerings, but we think with many of the clients that we work with who need that ESG data, we have the pipes built now to make that data available to them. So, we're very bullish not only on the financial opportunity here, but simply because we think when you think about our mission of empowering investor success, and Sustainalytics' mission of creating a just and sustainable economy, in the context of today's world, I think that intersection is certainly a very meaningful one and one we can help prioritize.

Barbara Noverini: To stay on that theme, Kunal, we'll take question from Jinesh Patel from Pelham Global. How should we think about competitive market development given MSCI, S&P, Moody's and LSE are also allocating high investment into the ESG space? How confident are you being one of the largest benchmark and data providers within the ESG space?

Kunal Kapoor: Yeah, it's certainly getting a lot of attention. And many firms, as you noted, are in fact rushing to build capabilities. I believe today that the two leading players are Sustainalytics and MSCI. It's clear that others are taking some steps to build some capabilities but some of the firms that you named actually rely on Sustainalytics as well for some pieces of their data. And it's true just in financial services in general that we have some interdependencies. But if the question is, am I comfortable being in that leadership spot and building the capabilities, I think we certainly feel that way and we have a clear vision for what we want to do here.

I think the difference between some of the firms that are getting into it today versus what Sustainalytics can bring to the table is 25 years of experience doing this. When we bought PitchBook, one of the questions we often got is how easily replicable is the data and can others do it? And I think as PitchBook has demonstrated, it's hard to collect that data and put it in a format that people can really use and understand. And I think that's true of ESG data as well. The reason the topic is so controversial is potentially because many people don't know how to use the data, or the data is not good when it gets to them. With Sustainalytics, you have a firm that's been around for 25 years, got into ESG data well before others had even started to go down this path, slogged it out really candidly. And they know the space, they understand the space and candidly they're educating us even about how to take it into our capabilities.

So, I feel very good about it. And I think when we look back in five years, we will sort of just assume that ESG is integrated into portfolio in a more natural way than people think about it today. It's almost like people think of it as an added capability today, I think it'll just be a very natural part of an overall portfolio.

Barbara Noverini: Great. Then we have a follow-up question from Arthur Baptist. Arthur, go ahead and ask your question.

Arthur Baptist, Golden Gate Capital: Great. Can you hear me?

Barbara Noverini: Yes.

Arthur Baptist: Okay. I was just wondering if you could give a little more color just on the current environment we're going through and specifically around the licensed-based businesses. It was helpful to get that down 4% in '09. That was a good data point. But I guess just, what's great about your model maybe now versus then is more of it even more as kind of subscription and recurring. So, I guess, as you think about the current environment, kind of two areas of potential risk would be – one would just be new sales and customer demand and if you're seeing any pullback on your sales and bookings. And then the other would be, you have great retention rates, and you're kind of 120% plus in PitchBook, and 100% in some of those other areas, have you seen any declines or early signs of declines in those retention rates through this environment?

Kunal Kapoor: Jason, why don't you start and answer that. And maybe Detlef, if you want to weigh in a little bit from a credit perspective as well.

Jason Dubinsky: Yeah. Thanks, Arthur. It's a good question. So, I think you're primarily focused on the licensed-based model and how is it holding up? So, I don't really have much more to add than I shared before and the fact that we didn't see much of an impact in Q1 and we're really looking at things closely now in Q2, and this will be an important indicator of how the sales pipeline continues to build and conversion. I'll tell you that, so far, our renewal rates are holding up, which is a good thing. And that's what you want to see. But I can't suggest that's the best indicator going forward as we have to continue to work with our clients to make sure that we can retain the business. But so far, renewal rates are still looking pretty good. And this is going to be an important sales quarter in terms of conversion of the pipeline. But sales teams are working hard. I give them a lot of credit across the globe in a different environment. But pipelines are building, and I think the real key is our ability to convert those sales leads into revenue and we'll probably have more to share as we get through this quarter. But at least as the flow through from Q1 into now is – more to come as we continue to monitor the business, but we're on top of it and continue to work really closely with our clients to make sure we can keep them but convert the new business from the sales pipeline.

Detlef Scholz: Maybe just to add, certainly, the new transaction-based business on the Credit Ratings side is very much exposed to the market volatility and especially the spread development. But we have those two segments also that I already described earlier, the repeat relationship business where you have extremely high retention rates given that once you're rated and your bonds are outstanding, you typically repeat. And also, within the structured finance segment, we have the surveillance business until transactions are maturing. And those are in some sectors actually, not only two or three-year cycles, but actually five years or seven years or sometimes transactions even running for 10 years. But Arthur, back to you.

Arthur Baptist: Thank you. Maybe just one last follow-up on the licensed-based products would just be – just the strategy around unifying some of the products or moving into a common platform, just when you think about there's Workstation, there's Office, there's Office Cloud, there's Data, just can you talk about the progress on kind of, you know, maybe moving those to a common platform, moving those to the cloud and where we are today?

Kunal Kapoor: Yeah, good question, Arthur. It's one that we spend a lot of time on at Morningstar. So, the question is just around unification of our platforms and how we deliver our data, I think, to the clients. I think that was the gist of the question. So, we are making good progress. I think one thing that is maybe a little bit different than it was last year is, we often thought of the decision ahead of us as purely desktop or cloud. And I think we've come to the conclusion as have others that you can have a hybrid solution where certain capabilities live on the desktop and certain capabilities live on the cloud and need to be accessed at all times. And so, with Direct, in particular, we have continued to focus really on the back end and ensuring that our data is in one place. And we've actually made really good progress, particularly through the first quarter of this year. And I'm actually very pleased in terms of where we are on the data front and the things that we're doing to kind of unify the platform. On the advisor side, we are increasingly also just focusing on a couple of platforms and releasing even new capabilities, such as for Reg BI into Advisor Workstation as opposed to releasing new capabilities on a standalone basis as well. So, I'd say good progress on that front, Arthur, but the only thing is that we are maybe diverging a little bit from the either-or strategy to it can be both things.

Arthur Baptist: Thank you.

Barbara Noverini: Thanks, Arthur. And then the next question is a follow-up from Jordan McNamee from CI Financial Cambridge. Jordan, please ask your question. Hold on one second, you seem to be muted. There we go. We hear you.

Jordan McNamee, Cambridge Global Asset Management: Great. Historically, it seems like you guys have always run with a significant amount of cash on your balance sheet. And clearly, you've decided to lever up for the DBRS acquisition. I just want to have a better understanding of just your comfort with leverage and how we should think about like, is there a deal that could have taken you to two times leverage. Is that something you'd even consider? Or is there some sort of risk metric in place that limits the absolute leverage you are willing to take on?

Jason Dubinsky: Yeah, so good question, Jordan. Maybe I'll field that first and Kunal can chime in. So, I think the question was more around running with a significant amount of cash on the balance sheet, and then comfort with leverage, particularly related to acquisitions. So, maybe I'll take those in two components. I think, first, and I think what I tried to do at least the pie chart earlier and we disclosed in the financial statements – so, cash on the balance sheet could be a bit misleading depending on where it is. So, that's the first thing in that most of our cash right now is sitting offshore outside of the U.S. and we've been working through tax reform and other mechanisms to have the ability to repatriate that over time back to the U.S. and that really depends on where acquisitions ultimately occur and where those proceeds go and where we able to utilize it.

So, I think when you look at our cash on the balance sheet, how much is in the U.S. versus outside the U.S. you can think about how we deploy it, which is a good example in the Sustainalytics acquisition that's coming up where we've got an upfront payment of EUR55 million. We're going to look to utilize a lot of that and watch our cash to fund that acquisition, because it's in the right jurisdiction. So, we run with a significant amount of cash. It gives us flexibility, but where that cash is and how we deploy it is pretty important. But we do want to make sure we have some cash and liquidity in the business to make sure we're supported in times like these to make sure we can appropriately weather cycles as needed.

And then, with leverage, I think what you've seen over time is we haven't been afraid to use the balance sheet and the balance sheet is an asset to be able to deploy for M&A. I think DBRS is clearly the largest deal we did in our history, about $670 million; PitchBook was a couple of hundred million. But as I said before, 1.5 times, even 2 times, I mean, that's modest leverage for us. But leverage in and of itself isn't good unless we can make sure we're getting the right levered returns. But I would just answer the leverage point in that we're going to use the balance sheet when it makes sense when we have the right opportunities and acquisitions at a fair price that can drive the right return that are on strategy. But the balance sheet is there, and we've taken conservative approaches over time because in times like this, we can play offense and be opportunistic when others may not be able to.

Kunal Kapoor: That's right. I think Jason answered the question fully. I think the important thing to just emphasize is, we will continue to be thoughtful and conservative in the way we manage it. We want to be in a position that if you get environments like this, and you always do, that, as a firm, we have the flexibility to do the things we need to in this type of environment as well.

Jordan McNamee: Can I get a follow up? In terms of the Sustainalytics deal seems really interesting. I just wanted to better understand what the potential size of that business could actually be.

Kunal Kapoor: So, the question is really around the size of the business. And I think it's actually a little bit of a tricky question to answer because not only do I think we can – not only do I think we can do just a lot with the Sustainalytics data, but I think we can actually feed it into multiple parts of our business and make the other parts of our business stronger. So, earlier in the conversation, I cited, for example, the index area or what we might do with Credit Ratings. And so, as a standalone basis, I have no doubt that Sustainalytics could be multiples larger over time than it is today.

But I think for it to be really, really successful across Morningstar we would need to leverage it more fully and ensure that we build up those capabilities because if we do that, then we can do more in the Credit Ratings space, we can do more in the portfolio management space. So, there's lots of cool things. Even last year in our Managed Portfolios part of the business, we launched some ESG portfolios. And while they are still a small part of the overall pie there, the immediate take-up of those portfolios was much higher than what we anticipated. And so, when you think about the impact on parts of our business, that really makes us even more excited than just thinking of it on a standalone basis.

Barbara Noverini: Thank you, Jordan. Our next question is a follow up question from Alex Braid.

Alex Braid, Artisan Partners: You know, back in 2014, Morningstar bought the data aggregator ByAllAccounts. There's been some recent acquisitions like Visa with Plaid. I think on your investor Q&A, you said that this is an underappreciated asset within Morningstar. Are you able to use this as an opportunity to feather out why you think it's an underappreciated asset and how much maybe (technical difficulty) about how much it's contributed to revenue growth over the last couple of years?

Kunal Kapoor: Absolutely, I'm happy to take that. So, the question is around ByAllAccounts, which for those of you who are not familiar with ByAllAccounts, it is an aggregator. So, what we do is we take up assets that an individual might hold, or an advisor might hold in multiple locations, and we pool them together in one place every day, so that that portfolio can be looked at in a holistic manner. So, first of all, you're right, we bought it many years ago, and I do think it's an underappreciated asset that one might argue we got a value price in retrospect when you look at some of the subsequent transactions that have been done in the space. But I think also the most important thing to understand about ByAllAccounts relative to a Plaid or a Yodlee is that those firms really sort of served the consumer area and have focused particularly on banking whereas ByAllAccounts, we've focused it as the leading provider of aggregation services to financial advisors in the wealth management space.

So, even if you look at other firms in the space, including, let's say, like an Envestnet or Orion, they are using ByAllAccounts for some of the work that's sort of getting done because of the expertise that we have in that space. Having said that, when we look at our aggregate growth, I think – and think about whether it's been a significant contributor, it has not. It's been a valuable piece in the overall aspect of what we've done for financial advisors. But we do need to do some things differently there. And particularly what we found is that while we're really good at the wealth management space, even advisors want a little bit more on the individual side so that they can help some of their clients have a better interface kind of a more easy to sort of navigate experience on the individual side. And so, we've been building a portal that allows advisors to sort of send their individuals there. And I think that that will help a lot in terms of plugging what was that one hole.

But in terms of connections that it has, in terms of capabilities that it has, it's very solid, and it was interesting Plaid when they bought Quovo recently, they actually deemphasized the wealth management and advisor capabilities. And so, when you look at the landscape and what's going on there, we have the asset in the aggregation space that's focused on wealth management. And James Carney who founded and leads ByAllAccounts, he recently moved into a new role at Morningstar, where he's overseeing our offering for independent financial advisors in aggregate. And one of the reasons that we're excited about that is that James sort of plugging all these things together, including ByAllAccounts to have a more comprehensive package than perhaps we've had in that space. So, it's a really nice asset. We're going to do more with it in the individual investor space as well than what we've done.

Alex Braid: Great. Thank you.

Barbara Noverini: Thank you, Alex. Our next question comes from the Q&A box from David Chamberlain of Amundi Pioneer. Do you envision the ESG ratings space market share wise, eventually becoming a duopoly, like Sustainalytics and MSCI as it matures, which would be similar to the ratings business with its incumbents currently?

Kunal Kapoor: That's an interesting question. I think there's a lot of competition that's going to take place in that space. And I don't know exactly, what the future will hold and I'm not going to try to predict whether there's just a couple of firms that have a leading position or not. What I'm focused on really candidly here is to make sure that we build a really great solution and we take our ratings and not only make them available to institutional investors, but make sure that they are available in the wealth space and the individual investor space. And I bring that up because I think this is what makes Morningstar uniquely different is that we can work with Sustainalytics to solidify the progress it's made in the institutional space. But none of the other firms that have been cited as competitors have the ability to also do what we do in the wealth management and the individual investor space. And it's our goal to do that and differentiate in that manner, and we think that will lead to good results.

Barbara Noverini: Then the next question comes from Daniel Welden of Numerus LLC. Could you provide a little bit of context on the AUM in Morningstar Managed Portfolios that moved to a fixed fee arrangement in the first quarter of 2020? How did the economics differ and where are those fixed fees revenues recognized? Is it still an asset-based or now in licensing?

Kunal Kapoor: Jason, why don't you go ahead?

Jason Dubinsky: Yeah, it's a good question. So, the question was around – in the first quarter results, you saw that we had – we did have a drop in assets under management primarily because an institutional client went from a variable fee to a fixed fee arrangement. What I would say generally, maybe it goes on top of some of the remarks that Kunal made earlier. First, for some clients, we provide different level of advisory or some component into their business and we have institutional relationships where they sometimes are a bit larger and fixed fees over time make a bit of sense, but it differs from the relationship that we have with advisors and the Managed Portfolio business where effectively we're fully outsourced and have really a longer-term relationship and are sharing investment outcomes over time. So, over time, we've been transitioning away from those institutional relationships and more emphasis, as we've been talking about, in terms of managed portfolios. But when we have some of these institutional relationships, fixed fees sometimes tend to work better for both sides. And that's exactly what happened with this one. Those fixed fees still fall within Investment Management. It's not a licensed-based classification. But it's fixed versus basis point related.

Barbara Noverini: Great. Then the next question comes from David Chamberlain from Amundi Pioneer. Is DBRS looking at the China corporate market as an opportunity for rated issuance? If so, where are you in terms of progress and what are the lowest barriers to entry in the U.S. corporates to gain share from Moody's and S&P?

Kunal Kapoor: Detlef, why don't you answer that one?

Detlef Scholz: So, let me take the second one first. On the corporate rating side in the U.S., those segments that are not heavily influenced by index bias are the ones within the corporate space that are easier for us. And certainly, private placements fall into that category, some of the transaction-based business in the infrastructure project finance side, but also the much growing middle market lending space are the ones where we can show expertise, but also then, as I mentioned earlier, grow our business into the adjacencies step by step. And I would actually describe that as a very low-risk execution based on our already existing capabilities, based on our ability of having entered markets in Europe on the back of our flagship corporate team and operations in Canada.

Now, the earlier question you had on China, I would not describe in the same way as a low-risk execution. It's actually a much higher hurdle to navigate in the new market where on the credit rating agency side we are not present yet. Certainly, Morningstar broadly has significant operations in China. But on the rating agency side, we are not registered at this point in time. We are not licensed at this point in time. But we carefully certainly monitor the value-add we could provide in any of the Asian markets where we are currently not operating. But I would really to be balanced and thoughtful say this, it's something we currently monitor, but there's no decision, there's no rush to expand, given that we have opportunities in North America and in Europe, which are much closer and have a lower risk of execution as we develop our footprint.

Barbara Noverini: Thank you. We're going to go ahead and take questions till about 11:45 Central Time. So, please go ahead and get your questions in or raise your hand. The next question comes from Shane Connor from Huffman Prairie Holdings. There's been a divergence between PitchBook license growth and PitchBook revenue growth in recent quarters. Can you help me understand why that's occurring?

Kunal Kapoor: Yeah, I answered that question a little bit earlier, but I'll just reiterate that the difference primarily is that when we bring in new users, what we find is that as they become familiar with the platform and start to use it more heavily, at the time of renewal, we're able to add more things to their renewal, upsell them as well as add more seats. So, that's really what the phenomenon that you're seeing is that once PitchBook is being used, it tends to be that people love it and want to renew in a more meaningful way when that time comes along.

Barbara Noverini: Thank you. Then the next question comes from Daniel Lee, OMD Ventures We've seen how DBRS is positioned against the competition and where that leads in various markets in the presentation today. But how can we think about the market position and share for each of Morningstar Data, Direct and PitchBook?

Kunal Kapoor: Detlef, do you want to maybe start, and I can also fill in? You seem to be muted Detlef.

Detlef Scholz: I believe we got the question here where we were quite clear on our positioning relative to the other firms in the credit rating space. So, I think this is more targeted on the other segments and how you look at our positioning there.

Kunal Kapoor: Barb, do you mind read the question…

Barbara Noverini: Sure. Yeah, the rest of the question is, how do we think about the market position and share for each of Morningstar Data, Direct and PitchBook.

Kunal Kapoor: Okay. Jason, do you want to have a go at it?

Jason Dubinsky: Yeah. So, I think, first I would start with the point – if you look at Data, for example, right now, where it's a couple of hundred million in revenue, Direct is about 150 million and close to PitchBook, too. So, if you just look at the relative size of some of our position in these businesses and how we report them relative to the competitive set, relative to the market opportunity, we still have a lot of runway from our perspective, both here domestically and internationally to continue to grow. I think, from my perspective, it's really what we're adding in a lot of these areas to help enable that. So, Data is a good example where we're building more robust equity datasets, we're building more robust fixed income datasets, we've got annuity data, derivative data, analytics, you know, (indiscernible) values. So, the data is so core to Morningstar just from our direct selling, as well as how it shows up in rest of our software products. So, we believe we continue to have a lot of opportunity and runway there with all that we're adding.

Direct is another good example where you've continued to see high single digit growth. A lot of good Direct growth is still coming from outside of the U.S. But we continue to work to enhance the Direct platform not just to create the right web-based solutions, but adding things like ESG data and Mercer data, our recent risk model to continue to add value to the platform for the asset managers and advisors who use that. And I think we've spent a fair amount of time on PitchBook today. You look at a $2 billion plus addressable market against $150 million product line at the end of

2019. There's a lot of opportunity and runway for growth and where we continue to invest significantly to make sure we're capitalizing on that. So, I think we have a lot of confidence and that's why we're putting a lot of effort behind at least these three product areas because of the opportunity that we have.

Barbara Noverini: Great. Then the next question is from Sid Arora from Brown Brothers Harriman. Regarding PitchBook, can you discuss how you see pricing power at PitchBook? Or is that not the right metrics to focus on? Any help in understanding that would be great. Thanks very much.

Kunal Kapoor: Sure. So, Sid, your question is on pricing at PitchBook, and I would go back to my earlier comments around how we've been able to grow PitchBook at the time of renewal in particular. And from my perspective, that should be an indication to you that we do have pricing power. Now, it's interesting that there are other players in that space who have tried to find their way by underpricing relative to PitchBook and have not succeeded. And what we hear is, even when people do make the switch and they come back, what we always hear is that the data is just not as good, the content is not as good. And so, something might be shinier on the outside. But once people look into it and they find what's in it, the pricing doesn't really reflect anything other than maybe something that's not as good as PitchBook. And so, we found that we do have pricing power there and that people who are using PitchBook and have been customers and have integrated into their workflow, are happy to pay more over time, because we are doing so much to enhance that platform.

Barbara Noverini: Thanks. Then the next question comes from Mindee Wasserman. The real estate market has been stressed – CMBS with office buildings, malls, hotels; RMBS with the level of unemployment really high. Will new credit ratings in structured finance help avoid some of the systemic problems that occurred in the last crisis?

Detlef Scholz: So, I guess this is a question for me and I have to make the disclaimer that I'm not an analyst so I cannot really make any analytical comments given the clear separation that we have between the business management as well as the analytics. But that said, it's actually very straightforward. And I think even my focus in the earlier comments on looking at some of the tools and some of the data we have available, that we certainly in our analysis overall are differentiating heavily between an economic stress in the current crisis and companies that are just going to come out well afterwards versus those sectors that are impacted by true structural change. And I believe the crisis is still early to figure out how many of those sectors are actually impacted by true structural change.

So, if the entire business model is evaporating, then certainly there's exposure on the credit side. That's actually why credit rating agencies in this current environment are so important and the thought leadership we provide to our COVID-19 related coverage is I believe at the forefront of the investor mind. So, we created a micro hub on our website, have published segment-by-segment research pieces of how we look at the impact. And to focus here on the commercial real estate market, it has to be broken down into the sub-segment; it also has to be broken down by the various regions. So, I can just invite you to look at some of the sector pieces within commercial real estate to look at our current view of the impact, whether it's just an impact going through the crisis where some of the sub asset classes are just going to come out well, versus those areas where we are concerned and where you also see rating activity in response to that. So, a lot of reading available to you and I would be pleased if you have a look at it.

Barbara Noverini: Thanks, Detlef. Then our final question is from Gregory Dean at CI Financial - Cambridge. What are your long-term plans with Morningstar Japan and why keep it public?

Kunal Kapoor: Sure. I'm going to involve Bevin in this one since she is our representative on that board. But obviously, we're unable to comment on the nature of the company being public or non-public. But Bevin, maybe you could just shed some light on the nature of the relationship and why we have this… and tell us how we operate in Japan as well.

Bevin Desmond: Sure. Long ago when Morningstar was first building our non-U.S. operations, actually, Morningstar Japan was the very first relationship that we developed with SoftBank, who is a great partner to us in Japan. SoftBank engaged with Morningstar to develop Morningstar Japan, and not long after probably within 18 months, I think, we went public. And this was before Morningstar was a public company. And it's been a very successful operation for us. And as a result of that, we've had many interactions with SoftBank. In helping us build our business, we actually had a joint venture with them in the Greater China region, across Hong Kong, Taiwan and Singapore. Also, they were a partner of Morningstar Korea operation. As you probably know, early on, probably, almost 10 years ago, we made transactions to exit most of our joint ventures. Now, they're wholly owned. Obviously, Morningstar Japan is a public company, as Kunal said, and our goal would be to have a great outcome for all the shareholders there no matter the way we operate.

We also have a second business in Japan that we acquired through our Ibbotson transaction, I think in 2006. And that has given us another angle of operating in Japan. Those two businesses interact frequently. And between Morningstar Japan and Ibbotson we're able to really do our global business in Japan relatively seamlessly. We have kind of a mutual beneficial relationship in sharing data and services and meeting the needs of our clients.

Is there anything else you want to add, Kunal?

Kunal Kapoor: No, I think you've covered it. And Barb, I think that was the last question if I'm not mistaken.

Barbara Noverini: Yeah, that's correct. Thanks to everyone for your great questions.

Kunal Kapoor: Yeah, awesome. I know we ran a little bit long, but hopefully we were able to get to everyone's questions. And again, I just want to thank everyone for joining us today. And I want to thank all my colleagues at Morningstar. They continue to do a great job. We've got a great team and I hope all of you as shareholders recognize and see that in your interactions with us. So, thank you, everyone. Stay safe and hopefully look forward to seeing you in person next year.