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ANALYST QUICK NOTES
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CME Group Inc. (NGS: CME: BUY)
Target Price: $134
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Investment Thesis

- February volumes (announced Mar. 2) averaged 18.4 million contracts, down 1% from 18.7 million in Feb. 2016:
  - Monthly volumes in 2016 generally in 14-16 million range.
  - 1Q volume so far averaging 17.2 million for Jan./Feb., ahead of all quarters last year except 1Q.
- Volume trends likely running ahead of most Street estimates:
  - Potential for 1Q EPS beat and higher 2017 consensus.
  - Argus is at $1.25 for 1Q, versus consensus of $1.17.
  - CME has exceeded consensus by $0.01 to $0.05 the past four quarters.
- Expect trading volumes to remain elevated:
  - Running well above second-half 2016 average despite a complacent, one-directional market over the past few months.
  - Repositioning around sooner-than-expected rate hikes.
  - Political uncertainties leading to speculation and hedging.
  - Some volume has moved from underlying equity trades to derivative options and futures trading.
- Mix shift expected to have favorable impact, with volume growth strong for higher-priced contracts:
  - Agricultural contracts average $1.34/contract, volumes up 12% year-over-year in February.
  - Metals contracts average $1.46/contract, up 7% in February.
  - Interest rate contracts average $0.49/contract, up 9% in February.
  - Lower-priced equities, energy and FX volumes down in February.

- Open interest has remained elevated:
  - 120.3 million contracts at March 5, up from 105.0 million in mid-2016 and 91.3 million at 2015 year end.
  - High open interest is generally a good indication of volume trends continuing.
- In early February, CME increased the quarterly dividend by 10% to $0.66, for a 2.1% yield.
- With an effective tax rate average of 34.6% the past two years, CME would be a strong beneficiary of lower corporate tax rates.
- The operating margin expansion story continues as 8% revenue growth is leveraged by low single-digit growth in operating expenses.
  - We see operating margins improving to 64% in 2017 and 65% in 2018, from 61% in 2016.
- Our target price of $134 implies 28-times our 2017 EPS estimate of $4.82:
  - The high end of the five-year P/E range is justified by record operating margins.