FTI Consulting, Inc. FCN [NYSE] | ★★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Stewardship	Morningstar Credit Rating	Industry
38.67 USD	52.00 USD	36.40 USD	72.80 USD	Medium	Narrow	C	—	Management Services

Cyclical businesses should help FTI make up for lower revenue from its restructuring business.

by Swami Shanmugasundaram
Stock Analyst
Analysts covering this company do not own its stock.

Pricing data through March 15, 2010.
Rating updated as of March 15, 2010.

Currency amounts expressed with "$" are in U.S. dollars (USD) unless otherwise denoted.

Thesis Mar. 08, 2010
FTI Consulting is known for its market-leading position in bankruptcy, restructuring, and litigation-related consulting services. Its international footprint, highly credentialed consultants, and long-standing customer relationships are its key selling points and create an economic moat around its business. We believe diversified service offerings, which include a mix of cyclical, countercyclical, and noncyclical business practices, make the firm fairly resilient across economic cycles.

Founded in 1982 with a focus on forensic consulting and litigation, FTI grew over the years, internally and through acquisitions, to become a leading provider of high-end professional services. The company has one of the most respected global practices in restructuring and bankruptcy, and offers its clients a broad and deep range of services and knowledge. It has developed many long-term relationships with its customers, which can hardly be overemphasized in the consulting industry. FTI derives more than 85% of its revenue from existing customers or referrals from existing clients. Sticky client relationships act as a significant barrier that protects FTI's territory in consulting.

Consulting companies typically take the acquisition route to expand their service offerings, as it requires quite a bit of time to build a practice from scratch. FTI's management is known for its strong record of identifying and integrating multiple acquisitions, which greatly complement the firm's internal growth profile. FTI recently announced its intent to expand beyond North America, and we believe that its recent acquisition of London-based Financial Dynamics, a public relations and financial communications consulting firm, was a first step in that direction. In addition to expanding FTI's service offerings and geographic reach, this acquisition opened up tremendous cross-selling opportunities with multinational companies. FTI plans to derive 25%-30% of revenue from international operations by 2012.

FTI operates in a knowledge-intensive industry; its primary revenue-generating assets are its people. The company relies on the expertise and reputation of its consultants to drive its business; reputation, in particular, plays a critical role when clients evaluate FTI relative to its peer group. FTI had first-hand experience in recognizing the need to retain its top talent and maintain its reputation when a group of consultants, who had joined the company through an acquisition, left in 2004, significantly affecting results. Subsequently, FTI rolled out a long-term retention plan that locks in top performers with long-term contracts that include noncompete and nonsolicitation clauses, enhancing its positioning in the market as well as its long-term viability.

FTI's business offerings include a balanced portfolio of services that we believe should help the company perform well regardless of the economic environment. In addition, FTI should be able to exploit the current industry trends in its favor; the subprime crisis, tighter credit markets, and challenging macroeconomic environment should create solid demand for its corporate finance/restructurings and litigation consulting businesses. We believe FTI is on solid footing, and its long-term prospects look good.

Valuation
We are lowering our fair value estimate to $52 per share from $55. Given the recent improvements in the global economic environment, we expect the pace of restructuring to slow in 2010. With restructuring accounting for almost one fourth of FTI's total revenue, we expect the slowdown to hurt the company's growth prospects. However, the improved economic climate should work in favor of the company's cyclical businesses, which we expect to regain some of the lost momentum and thus make up for the decline in demand for the restructuring business. Overall, we estimate the company's revenue to grow at a compound annual rate of 8% during the next five years, excluding any acquisitions. In terms of profitability, we don't expect to see much

FTI Consulting, Inc. FCN [NYSE] | ★★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Stewardship	Morningstar Credit Rating	Industry
38.67 USD	52.00 USD	36.40 USD	72.80 USD	Medium	Narrow	C	—	Management Services

Close Competitors	Currency(Mil)	Market Cap	TTM Sales	Oper Income	Net Income
FTI Consulting, Inc.	USD	1,797	1,400	264	143
Navigant Consulting	USD	602	707	52	22

Morningstar data as of March 15, 2010.

volatility in the company's margins. We expect FTI to maintain its operating margin in the high teens (18%-19%) during our forecast horizon, in line with its historical range. Our fair value estimate would drop to our Consider Buying price if we were to assume a compound annual growth rate of 5% and average operating margins of 16% during our forecast period.

Risk

The biggest risk facing FTI is losing its senior employees to competitors. The war for talent is intense in the consulting industry, given the highly specialized nature of services and the fact that a large portion of new business is generated through the relationship channel. Further, as FTI focuses on expanding its global footprint to drive its growth, it is faced with several risks arising from international exposure such as foreign currency volatility, lack of skilled professionals in local markets, and unstable political and economic environments. Consulting is an event-driven business, and results can be lumpy.

Bulls Say

- FTI's focus on event-driven consulting assignments reduces its exposure to economic swings.
- FTI, through its restructuring operations, is well positioned to benefit in a countercyclical environment, where defaults and bankruptcies were prevalent.
- FTI has improved the retention of its senior managing directors, providing the company with a stable group of senior managers. Also client/manager revenue concentration is minimal.

Bears Say

- FTI's contract terms generally allow clients to terminate the engagement with little notice and without penalty. Unexpected changes in the demand environment could affect FTI's pipeline, leading to lumpiness in revenue streams.
- The consulting industry suffers from high employee turnover, and this poses execution challenges to FTI.
- FTI's expansion into international markets exposes the firm to considerable foreign exchange rate risk.
- Although FTI has a successful history of acquisitions, there is no guarantee that future acquisitions will be implemented successfully, and integrating new companies can be a challenge.

Financial Overview

Growth: FTI's revenue has grown at a compound annual rate of 27% from 2005 to 2009, largely with the help of acquisitions. We expect revenue growth to average 8% during the next five years, excluding any acquisitions.

Profitability: FTI's margins have been fairly stable during the past five years, averaging about 18%. We expect the company to maintain its margin around its historical levels during our forecast horizon.

Financial Health: FTI used financial leverage to pursue its acquisition strategy and carries more than $550 million in debt on its balance sheet. However, its debt load remains manageable; the company generates steady cash inflows and should be able to service its debt obligations.

Company Overview

Profile: Founded in 1982 and based in Baltimore, FTI

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

FTI Consulting, Inc. FCN [NYSE] | ★★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Stewardship	Morningstar Credit Rating	Industry
38.67 USD	52.00 USD	36.40 USD	72.80 USD	Medium	Narrow	C	—	Management Services

Consulting is a global advisory firm with expertise in litigation consulting, financial restructuring, and forensic investigation. The company provides its services through five distinct consulting practices focused on litigation, corporate finance and restructuring, strategic communications, technology, and economic consulting. It has more than 2,600 consultants and has offices in 32 U.S. cities and 26 foreign countries.

Strategy: Acquisition-based growth has been a key component of FTI's business strategy, and we believe acquisitions will play a major role in the future. Management has used targeted acquisitions to ramp up its service offerings and increase its density in the market to enhance its competitive position. FTI also plans to lower its dependence on the North American market and hopes to derive 25%-30% of revenue from its international operations. The company has made significant investments in its international operations to support its expansion strategy.

Management: FTI's stewardship has been fair. President and CEO Jack Dunn has been with the company since 1992 and became CEO in 1995 and president in 2004. Given that operating performance of the company has been solid during his tenure, we think this continuity has been a positive. Dunn also was chairman from 1998 to 2004 but relinquished the title to Dennis Shaughnessy in 2004 to separate the chairman and CEO titles. We like that the chairman and CEO roles are held by different people. A majority of the 10-member board is composed of independent directors. Executives and directors collectively own 4% of FTI's outstanding common shares, which bodes well for shareholder value creation. Annual salary compensation for top management includes base salary, performance-based bonus, and equity awards. Although this variable compensation benefits shareholders, we would like to see a better metric used to measure performance instead of earnings per share, which can be easily manipulated. FTI could improve its stewardship grade by eliminating its staggered board structure.

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

FTI Consulting, Inc. FCN [NYSE] | ★★★★

Last Price	Fair Value	Consider Buy	Consider Sell	Uncertainty	Economic Moat™	Stewardship	Morningstar Credit Rating	Industry
38.67 USD	52.00 USD	36.40 USD	72.80 USD	Medium	Narrow	C	—	Management Services

Analyst Notes

Feb. 26, 2010

FTI Consulting Under Review After Weak Guidance

FTI Consulting's diversified revenue base helped it to close fiscal 2009 on a strong note. The company's counter-cyclical businesses delivered a solid set of numbers, which more than offset weak performance from its cyclical businesses. The net result was an 8.3% increase in revenue and 30 basis points expansion in operating margins when compared to fiscal 2008. While the company's 2009 results were mostly in line with our assumptions, management guidance for 2010 came in below our estimates. We are placing our fair value estimate under review while we reassess our forecast in light of management's commentary, and expect to reduce it modestly.

The Corporate Finance and Restructuring practice maintained its growth momentum and registered a 37% increase in revenue compared to last year, primarily driven by increased restructuring activity in several industries including healthcare, financial services, utility/energy, and media. This segment also benefited from its recent international expansions as it derived solid contributions from European, Canadian, and Latin American activities. The next best performance in terms of revenue growth came from the Economic Consulting business, where revenue increased 7% compared to last year. Increased activity in strategic M&A and financial dispute matters helped this segment post solid numbers.

Forensic and Litigation consulting had a relatively stable year with a 2% increase in revenue. Participation in a few large fraud investigations including the Madoff and Stanford cases helped the company offset lower demand from generic commercial litigation. The Strategic Communications and the Technology Consulting businesses reported weak results, as expected. These segments were hurt by the economic slowdown as clients cut their investments in discretionary projects. Strategic communications, which relies heavily on capital markets for its business, fared the worst with a 20% plunge in revenue, while technology consulting saw its revenue decline 4%.

Operating margins increased marginally by 30 basis points to 18.8%. Solid demand for the more profitable Corporate Finance/Restructuring and Economic Consulting businesses led to higher billing rates and chargeable hours, which boosted overall margins.

Feb. 12, 2010

FTI Consulting Earnings Preview

FTI Consulting will report its fourth-quarter results in a few weeks. The company posted solid results during the first nine months, mostly driven by a healthy demand for its services in the bankruptcy / restructuring arena. Given the strong backlog and new restructuring assignments it had won since the beginning of the fourth quarter, we expect the company's restructuring practice to close out the year on a strong note.

However, the momentum in the restructuring business could partially be offset by the deceleration of growth in two of its other segments: Technology and Strategic Communications. We expect these segments to witness a slowdown in demand due to economic distractions, a slowdown in discretionary spending by companies, and lower activity in the capital markets.

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

Analyst Notes (continued)

Nov. 05, 2009

FTI Consulting Reports 3Q Results

FTI Consulting reported fiscal third-quarter results that were in line with our expectations, and we are maintaining our fair value estimate.

FTI's third-quarter revenue increased 7% year over year (9% in constant currency) to $349 million, primarily driven by strong performance from the Corporate Finance/Restructuring and Economic Consulting business segments. The Corporate Finance/Restructuring business continued its momentum with 40% growth in revenue compared to last year and management cited particular strength in financial services, automotive, utility/energy, and media sectors. Given the underlying demand trends for corporate restructuring, we believe revenue growth in this segment will remain very strong over the next few quarters. Revenue from the Economic Consulting business, which advises clients on issues related to M&A, antitrust, and public policy, rose 6% year over year, driven by increased M&A activity during the quarter. Strong performance from these two business segments were offset by weak results from the Strategic Communications and Technology Consulting businesses. Strategic Communications fared the worst with a 15% decline in revenue compared to the year-ago period. This segment was hit hard by softer capital market activities and a negative foreign currency impact. Technology consulting revenue dipped 12% due to pricing pressure and a decline in revenue from a large product liability engagement. The demand for the company's Forensic & Litigation Consulting remained mostly stable--revenue declined a modest 1% compared to the year-ago period.

The operating margin was 18.4%, up 210 basis points from the comparable quarter last year. Solid demand for Corporate Finance/Restructuring and Economic Consulting businesses led to higher billing rates and chargeable hours, which boosted the overall operating margin.

Disclaimers & Disclosures

No Morningstar employees are officers or directors of this company. Morningstar Inc. does not own more than 1% of the shares of this company. Analysts covering this company do not own its stock. The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

FTI Consulting, Inc. FCN

Sales USD Mil	Mkt Cap USD Mil	Industry	Sector
1,400	1,797	Management Services	Business Services

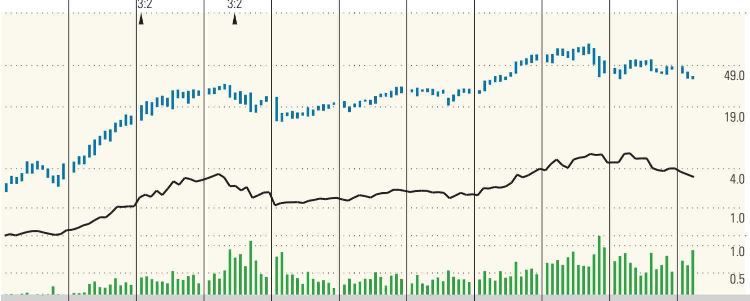
Founded in 1982 and based in Baltimore, FTI Consulting is a global advisory firm with expertise in litigation consulting, financial restructuring, and forensic investigation. The company provides its services through five distinct consulting practices focused on litigation, corporate finance and restructuring, strategic communications, technology, and economic consulting. It has more than 2,600 consultants and has offices in 32 U.S. cities and 26 foreign countries.

500 East Pratt Street Suite 1400
Baltimore, MD 21202
Phone: 1 410 224-8770Website: http://www.fticonsulting.com

Morningstar Rating	Last Price	Fair Value	Uncertainty	Economic Moat™	Stewardship Grade
★★★★	38.67	52.00	Medium	Narrow	C

per share prices in USD

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	YTD	
5.17	16.09	28.62	32.45	24.14	30.54	29.77	63.00	80.00	56.41	48.33	Annual Price High
2.11	3.78	13.93	16.79	13.55	17.01	19.82	25.95	37.80	36.14	36.10	Low
		3:2	3:2								Recent Splits



Price Volatility
Monthly High/Low
Rel Strength to S&P 500

52 week High/Low
56.41 - 36.10

10 Year High/Low
80.00 - 2.11

Bear-Market Rank
1 (10=worst)

Trading Volume Million

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	YTD	**Stock Performance**
105.0	220.0	83.6	-12.7	-9.8	30.2	1.6	121.0	-27.5	5.5	-18.0	Total Return %
115.1	233.0	107.0	-39.1	-18.8	27.2	-12.0	117.5	11.0	-17.9	-21.2	+/- Market
149.2	148.1	109.1	-49.5	-18.6	24.7	-19.5	128.2	-6.8	-16.5	-22.1	+/- Industry
—	—	—	—	—	—	—	—	—	—	0.0	Dividend Yield %
65	423	955	980	893	1071	1160	2962	2271	2216	1797	Market Cap USD Mil

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	TTM	**Financials**
135	166	224	376	427	540	708	1001	1293	1400	1400	Revenue USD Mil
51.1	49.8	51.8	53.1	45.0	46.0	45.0	45.2	45.4	45.2	45.2	Gross Margin %
25	32	63	114	78	114	106	187	239	264	264	Oper Income USD Mil
18.3	19.4	28.3	30.3	18.4	21.1	15.0	18.7	18.5	18.8	18.8	Operating Margin %
3	16	37	59	43	56	42	92	125	143	143	Net Income USD Mil
0.14	0.56	1.09	1.41	1.01	1.35	1.04	2.00	2.34	2.70	2.70	Earnings Per Share USD
—	—	—	—	—	—	—	—	—	—	—	Dividends USD
18	29	34	42	42	41	40	46	53	53	53	Shares Mil
4.78	3.62	7.51	10.85	11.70	11.64	13.59	20.23	22.12	23.50	23.76	Book Value Per Share USD
16	27	78	96	58	99	64	78	200	251	251	Oper Cash Flow USD Mil
-7	-4	-9	-11	-12	-18	-30	-36	-36	-29	-29	Cap Spending USD Mil
9	23	69	86	47	82	34	42	164	222	222	Free Cash Flow USD Mil

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	TTM	**Profitability**
2.2	11.0	12.7	10.9	6.3	6.8	3.6	5.7	6.4	6.9	6.9	Return on Assets %
5.2	19.0	19.9	16.4	9.0	11.9	8.3	12.0	12.0	12.8	12.8	Return on Equity %
1.9	9.9	16.6	15.8	10.0	10.4	5.9	9.2	9.7	10.2	10.2	Net Margin %
1.17	1.11	0.77	0.69	0.62	0.65	0.60	0.62	0.66	0.67	0.67	Asset Turnover
2.1	1.5	1.6	1.5	1.4	2.1	2.5	1.9	1.9	1.9	1.9	Financial Leverage

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	12-09	**Financial Health**
20	29	14	15	60	193	116	280	129	94	94	Working Capital USD Mil
56	24	78	105	84	348	563	416	—	—	—	Long-Term Debt USD Mil
69	105	268	455	496	454	565	972	1124	1104	1104	Total Equity USD Mil
0.82	0.23	0.29	0.23	0.19	0.77	1.00	0.43	0.37	0.38	0.38	Debt/Equity

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	TTM	**Valuation**
32.0	26.0	26.3	15.2	20.9	20.3	26.8	30.9	19.1	17.4	14.3	Price/Earnings
—	1.1	1.3	0.7	1.1	1.2	1.6	1.9	1.8	0.9	0.7	P/E vs. Market
0.5	2.6	4.1	2.6	2.1	2.1	1.6	2.8	1.9	1.8	1.5	Price/Sales
0.9	4.0	3.6	2.1	1.8	2.4	2.0	3.0	2.0	2.0	1.6	Price/Book
4.5	15.7	11.8	10.3	15.3	11.7	17.6	36.4	12.0	10.0	8.2	Price/Cash Flow

Growth Rates Compound Annual

Grade: B	1 Yr	3 Yr	5 Yr	10 Yr
Revenue %	8.3	25.5	26.8	32.4
Operating Income %	10.4	35.4	27.4	39.7
Earnings/Share %	15.4	37.4	21.7	26.3
Dividends %	—	—	—	—
Book Value/Share %	-3.6	16.2	12.7	22.6
Stock Total Return %	-18.5	4.3	14.0	27.6
+/- Industry	-59.9	6.1	8.3	25.9
+/- Market	-70.6	10.5	14.8	29.7

Profitability Analysis

Grade: C	Current	5 Yr Avg	Ind	Mkt
Return on Equity %	12.8	11.4	26.3	19.1
Return on Assets %	6.9	5.8	8.8	7.3
Fixed Asset Turns	17.6	18.0	18.9	6.8
Inventory Turns	—	—	912.4	12.1
Revenue/Employee USD K	403.2	392.9*	—	669.8
Gross Margin %	45.2	45.4	40.3	41.1
Operating Margin %	18.8	18.4	10.2	12.2
Net Margin %	10.2	9.1	6.0	8.2
Free Cash Flow/Rev %	15.9	10.5	10.8	0.1
R&D/Rev %	—	—	—	10.7

Financial Position

Grade: B	12-08 USD Mil	12-09 USD Mil
Cash	192	119
Inventories	—	—
Receivables	305	308
Current Assets	552	500
Fixed Assets	79	81
Intangibles	1341	1372
Total Assets	2088	2077
Payables	—	8
Short-Term Debt	—	—
Current Liabilities	424	406
Long-Term Debt	—	—
Total Liabilities	964	973
Total Equity	1124	1104

Valuation Analysis

	Current	5 Yr Avg	Ind	Mkt
Price/Earnings	14.3	22.9	20.4	19.2
Forward P/E	9.9	—	—	14.2
Price/Cash Flow	8.2	17.5	10.5	7.0
Price/Free Cash Flow	9.2	28.4	12.3	17.5
Dividend Yield %	—	—	1.2	1.8
Price/Book	1.6	2.3	5.0	2.2
Price/Sales	1.5	2.0	1.3	1.3
PEG Ratio	0.6	—	—	1.7

Quarterly Results

Revenue USD Mil	Mar 09	Jun 09	Sep 09	Dec 09
Most Recent Period	347.9	360.5	348.6	342.9
Prior Year Period	307.1	337.7	325.5	322.9

Rev Growth %	Mar 09	Jun 09	Sep 09	Dec 09
Most Recent Period	13.3	6.8	7.1	6.2
Prior Year Period	34.9	40.9	28.5	15.1

Earnings Per Share USD	Mar 09	Jun 09	Sep 09	Dec 09
Most Recent Period	0.60	0.69	0.70	0.71
Prior Year Period	0.59	0.66	0.51	0.58

Industry Peers by Market Cap

	Mkt Cap USD Mil	Rev USD Mil	P/E	ROE%
FTI Consulting, Inc.	1797	1400	14.3	12.8
Navigant Consulting	602	707	27.3	5.6

Major Fund Holders

	% of shares
T. Rowe Price Small-Cap Value	2.49
Rainier Small/Mid Cap Equity	1.92
Fidelity Advisor Small Cap T	1.87

*3Yr Avg data is displayed in place of 5Yr Avg

TTM data based on rolling quarterly data if available; otherwise most recent annual data shown.

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

Morningstar's Approach to Rating Stocks

Our Key Investing Concepts

- Economic Moat™ Rating
- Discounted Cash Flow
- Discount Rate
- Fair Value
- Uncertainty
- Margin of Safety
- Consider Buying/Consider Selling
- Stewardship Grades

At Morningstar, we evaluate stocks as pieces of a business, not as pieces of paper. We think that purchasing shares of superior businesses at discounts to their intrinsic value and allowing them to compound their value over long periods of time is the surest way to create wealth in the stock market.

We rate stocks 1 through 5 stars, with 5 the best and 1 the worst. Our star rating is based on our analyst's estimate of how much a company's business is worth per share. Our analysts arrive at this "fair value estimate" by forecasting how much excess cash--or "free cash flow"--the firm will generate in the future, and then adjusting the total for timing and risk. Cash generated next year is worth more than cash generated several years down the road, and cash from a stable and consistently profitable business is worth more than cash from a cyclical or unsteady business.

Stocks trading at meaningful discounts to our fair value estimates will receive high star ratings. For high-quality businesses, we require a smaller discount than for mediocre ones, for a simple reason: We have more confidence in our cash-flow forecasts for strong companies, and thus in our value estimates. If a stock's market price is significantly above our fair value estimate, it will receive a low star rating, no matter how wonderful we think the business is. Even the best company is a bad deal if an investor overpays for its shares.

Our fair value estimates don't change very often, but market prices do. So, a stock may gain or lose stars based just on movement in the share price. If we think a stock's fair value is $50, and the shares decline to $40 without much change in the value of the business, the star rating will go up. Our estimate of what the business is worth hasn't changed, but the shares are more attractive as an investment at $40 than they were at $50.

Because we focus on the long-term value of businesses, rather than short-term movements in stock prices, at times we may appear out of step with the overall stock market. When stocks are high, relatively few will receive our highest rating of 5 stars. But when the market tumbles, many more will likely garner 5 stars. Although you might expect to see more 5-star stocks as the market rises, we find assets more attractive when they're cheap.

We calculate our star ratings nightly after the markets close, and issue them the following business day, which is why the rating date on our reports will always be the previous business day. We update the text of our reports as new information becomes available, usually about once or twice per quarter. That is why you'll see two dates on every Morningstar stock report. Of course, we monitor market events and all of our stocks every business day, so our ratings always reflect our analyst's current opinion.

Economic Moat™ Rating

The Economic Moat™ Rating is our assessment of a firm's ability to earn returns consistently above its cost of capital in the future, usually by virtue of some competitive advantage. Competition tends to drive down such

Morningstar Research Methodology for Valuing Companies

Competitive Analysis → **Economic Moat™ Rating** → Company Valuation → **Fair Value Estimate** → Uncertainty Assessment → ★★★★★

Competitive Analysis: Analyst conducts company and industry research:

- Management interviews
- Conference calls
- Trade-show visits
- Competitor, supplier, distributor, and customer interviews

Economic Moat™ Rating: The depth of the firm's competitive advantage is rated:

- None
- Narrow
- Wide

Company Valuation: Analyst considers company financial statements and competitive position to forecast future cash flows.

Assumptions are input into a discounted cash-flow model.

Fair Value Estimate: DCF model leads to the firm's Fair Value Estimate, which anchors the rating framework.

Uncertainty Assessment: An uncertainty assessment establishes the margin of safety required for the stock rating.

★ / ★★ / ★★★ / ★★★★ / ★★★★★: The current stock price relative to fair value, adjusted for uncertainty, determines the rating.

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.

economic profits, but companies that can earn them for an extended time by creating a competitive advantage possess an Economic Moat. We see these companies as superior investments.

Discounted Cash Flow
This is a method for valuing companies that involves projecting the amount of cash a business will generate in the future, subtracting the amount of cash that the company will need to reinvest in its business, and using the result to calculate the worth of the firm. We use this technique to value nearly all of the companies we cover.

Discount Rate
We use this number to adjust the value of our forecasted cash flows for the risk that they may not materialize. For a profitable company in a steady line of business, we'll use a lower discount rate, also known as "cost of capital," than for a firm in a cyclical business with fierce competition, since there's less risk clouding the firm's future.

Fair Value
This is the output of our discounted cash-flow valuation models, and is our per-share estimate of a company's intrinsic worth. We adjust our fair values for off-balance sheet liabilities or assets that a firm might have--for example, we deduct from a company's fair value if it has issued a lot of stock options or has an under-funded pension plan. Our fair value estimate differs from a "target price" in two ways. First, it's an estimate of what the business is worth, whereas a price target typically reflects what other investors may pay for the stock. Second, it's a long-term estimate, whereas price targets generally focus on the next two to 12 months.

Uncertainty
To generate the Morningstar Uncertainty Rating, analysts consider factors such as sales predictability, operating leverage, and financial leverage. Analysts then classify their ability to bound the fair value estimate for the stock into one of several uncertainty levels: Low, Medium, High, Very High, or Extreme. The greater the level of uncertainty, the greater the discount to fair value required before a stock can earn 5 stars, and the greater the premium to fair value before a stock earns a 1-star rating.

Margin of Safety
This is the discount to fair value we would require before recommending a stock. We think it's always prudent to buy stocks for less than they're worth.The margin of safety is like an insurance policy that protects investors from bad news or overly optimistic fair value estimates. We require larger margins of safety for less predictable stocks, and smaller margins of safety for more predictable stocks.

Consider Buying/Consider Selling
The consider buying price is the price at which a stock would be rated 5 stars, and thus the point at which we would consider the stock an extremely attractive purchase. Conversely, consider selling is the price at which a stock would have a 1 star rating, at which point we'd consider the stock overvalued, with low expected returns relative to its risk.

Stewardship Grades
We evaluate the commitment to shareholders demonstrated by each firm's board and management team by assessing transparency, shareholder friendliness, incentives, and ownership. We aim to identify firms that provide investors with insufficient or potentially misleading financial information, seek to limit the power of minority shareholders, allow management to abuse its position, or which have management incentives that are not aligned with the interests of long-term shareholders. The grades are assigned on an absolute scale--not relative to peers--and can be interpreted as follows: A means "Excellent," B means "Good," C means "Fair," D means "Poor," and F means "Very Poor."

© 2010 Morningstar. All Rights Reserved. Unless otherwise provided in a separate agreement, you may use this report only in the country in which its original distributor is based. Data as originally reported.
The information contained herein is not represented or warranted to be accurate, correct, complete, or timely. This report is for information purposes only, and should not be considered a solicitation to buy or sell any security.
Redistribution is prohibited without written permission. To order reprints, call +1 312-696-6100. To license the research, call +1 312-696-6869.