



# AGNC Investment Corporation (AGNC)

Updated November 9<sup>th</sup>, 2020 by Samuel Smith

## Key Metrics

<b>Current Price:</b>	\$14	<b>5 Year CAGR Estimate:</b>	8.8%	<b>Market Cap:</b>	\$7.7B
<b>Fair Value Price:</b>	\$20	<b>5 Year Growth Estimate:</b>	-7.3%	<b>Ex-Dividend Date:</b>	11/29/20
<b>% Fair Value:</b>	69%	<b>5 Year Valuation Multiple Estimate:</b>	7.8%	<b>Dividend Payment Date:</b>	12/10/20
<b>Dividend Yield:</b>	10.3%	<b>5 Year Price Target</b>	\$14.0	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	D	<b>Retirement Suitability Score:</b>	B	<b>Last Dividend Increase:</b>	NA

## Overview & Current Events

American Capital Agency Corp was founded in 2008, and is a mortgage real estate investment trust that invests primarily in agency mortgage-backed securities (or MBS) on a leveraged basis. The firm's asset portfolio is comprised of residential mortgage pass-through securities, collateralized mortgage obligations (or CMO), and non-agency MBS. Many of these are guaranteed by government-sponsored enterprises. The majority of American Capital's investments are fixed-rate agency MBS. Most of these are MBS with a 30-year maturity period. The counterparties to most of American Capital's assets are located in North America. Counterparties in Europe also represent a significant percentage of the trust's total portfolio. American Capital derives nearly all its revenue in the form of interest income. It currently generates about \$1.1 billion in annual net interest income and trades at a market capitalization of \$7.7 billion.

AGNC reported its Q3 2020 results on October 26<sup>th</sup>. Relative to consensus estimates for net spread and dollar roll income per share of 57 cents and 58 cents, respectively in Q2, the company outperformed at 81 cents for each in Q3. Partially responsible for this success was AGNC's forward purchase and sales of agency MBS in the TBA market that brought the average net long position to \$27.8 billion. The company's net book value per common share also showed an increase from \$14.92 on June 30, 2020 to \$15.88 as of Sept 30, 2020. 36 cents in dividends per common share and the 96-cent increase in TNBV per common share generated an 8.8% economic return on tangible common equity for Q3.

The lower coupon, new production pools, and higher coupon specified pools are the reasons AGNC's portfolio outperformed their hedge portfolio this quarter.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>EPS</b>	\$7.89	\$5.02	\$4.17	\$3.28	(\$0.72)	\$0.54	\$1.79	\$2.04	\$0.21	\$2.26	<b>\$2.55</b>	<b>\$1.75</b>
<b>DPS</b>	\$5.60	\$5.60	\$5.00	\$3.75	\$2.61	\$2.48	\$2.30	\$2.16	\$2.16	\$2.16	<b>\$1.44</b>	<b>\$1.50</b>
<b>Shares<sup>1</sup></b>	37	153	303	379	353	349	331	358	441	546	<b>546</b>	<b>800</b>

Due to AGNC's heavily leveraged business model and its high sensitivity to interest rates, its results have been very choppy over the years. Furthermore, the current coronavirus disruption to the economy will likely cause a steep drop off in earnings per share and book value. That being said, we believe that the current lower interest rate environment stemming from slowing global growth and the Federal Reserve's renewed dovish stance should enable it to have a strong bounce-back in the years to come, given it will keep spreads attractive and the mortgage market on somewhat solid footing.

Over the long-term we think they will grow earnings, but its high payout ratio and the volatile nature of the business model will prevent it from growing quickly after an initial snap-back after this year's disruption. We also believe that dividend growth will be anemic for the foreseeable future as the trust strives to grow its way back towards adequate coverage of its payout.

<sup>1</sup> Share count in millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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## Valuation Analysis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Now	2025
Avg. P/E	3.6	5.6	7.1	5.9	-30.4	31.8	10.1	9.9	83.6	7.5	5.5	8.0
Avg. Yld.	19.5%	19.8%	16.9%	19.4%	11.9%	14.4%	12.7%	10.7%	12.3%	12.7%	10.3%	10.7%

AGNC is currently trading at 5.5 times its projected 2020 earnings, and we see this as undervalued based on its longer-term P/E averages. As a result, we see valuation multiple expansion over the next half decade. The dividend yield is uncertain moving forward as the company has a history of cutting its dividend during times of uncertainty. However, our current estimate implies a yield that is significantly below historical averages.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	71.0%	112%	120%	114%	-363%	459%	129%	106%	1029%	96%	56%	86%

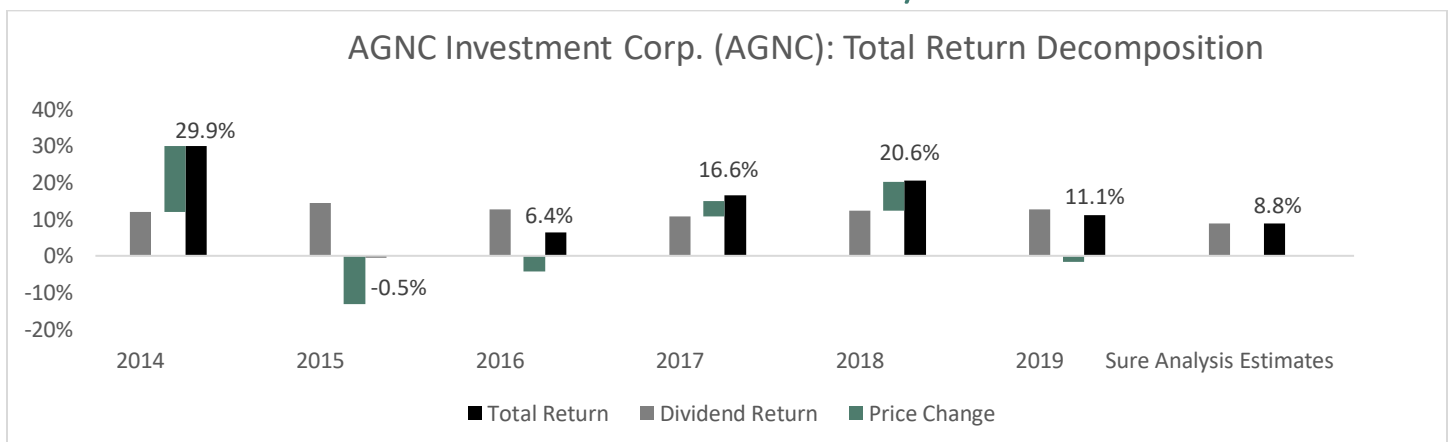
Given that it had its IPO in 2008 – in the midst of the financial crisis – it is hard to get an accurate picture of exactly how it can be expected to perform during this recession. However, the mortgage backed security industry – given its leverage and interest rate sensitivity – is very prone to underperform when the housing market experiences a downturn and mortgage foreclosures rise. As a result, it should not be viewed as a safe, defensive stock. That being said, its record thus far has been fairly strong, with industry-leading total economic return (NAV-based) and total stock return (share price-based).

This outperformance has been driven by its highly efficient operating cost structure of approximately 0.8% of total equity capital, and the competitive advantage that it enjoys through economies of scale as one of only three residential mortgage REITs with a market capitalization of above \$5 billion. The trust also strives to guard against downside and enhance shareholder total returns by utilizing a comprehensive risk management framework that is predicated on careful asset selection, disciplined hedging, and diversified funding.

## Final Thoughts & Recommendation

AGNC offers investors an attractive current dividend yield of 10.3% and a discount to fair value in its earnings multiple. That said, the earnings stream is unpredictable and highly leveraged. As a result, we view shares as fairly valued at present with annualized total return potential of 8.8% over the next half decade. We rate shares a hold as a result and advise conservative dividend growth investors to look elsewhere.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Revenue</b>	307	850	1440	1440	-92	354	728	844	229	771
<b>SG&amp;A Exp.</b>	19	74	144	168	119	116	71	42	45	47
<b>D&amp;A Exp.</b>	N/A	N/A	N/A	N/A	0	0	2	3	25	-
<b>Net Profit</b>	288	770	1277	1259	-233	215	623	771	129	688
<b>Net Margin</b>	93.8%	90.6%	88.7%	87.4%	253%	60.7%	85.6%	91.4%	56.3%	89.2%
<b>Free Cash Flow</b>	233	1070	2321	2501	1622	1428	1352	1260	1113	1,180

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Total Assets</b>	14476	57972	100B	76255	67766	57021	56880	70376	109241	113082
<b>Cash &amp; Equivalents</b>	173	1367	2430	2143	1720	1110	1208	1046	921	831
<b>Goodwill &amp; Int.</b>						0	554	551	526	526
<b>Total Liabilities</b>	12904	51760	89557	67558	58338	49050	49524	61622	99335	102041
<b>Accounts Payable</b>	727	40	132	492	100	61	211	299	518	424
<b>Long-Term Debt</b>	73	54	937	910	761	4348	3497	357	275	228
<b>Total Equity</b>	1572	6212	10729	8530	9092	7635	7020	8270	9422	10109
<b>D/E Ratio</b>	0.05	0.01	0.09	0.10	0.08	0.55	0.48	0.04	0.03	0.02

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Return on Assets</b>	3.0%	2.1%	1.6%	1.4%	-0.3%	0.3%	1.1%	1.2%	0.1%	0.6%
<b>Return on Equity</b>	27.2%	19.8%	15.1%	13.1%	-2.6%	2.6%	8.5%	10.1%	1.5%	7.0%
<b>ROIC</b>	26.3%	19.5%	14.1%	11.7%	-2.4%	1.9%	5.4%	7.7%	1.3%	6.4%
<b>Shares Out.</b>	37.0	153.0	303.0	379.0	353.0	349.0	331.0	358.0	441.0	546
<b>Revenue/Share</b>	8.41	5.54	4.74	3.80	-0.26	1.02	2.19	2.35	0.52	1.42
<b>FCF/Share</b>	6.38	6.98	7.64	6.60	4.59	4.10	4.07	3.51	2.52	2.18

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

### Disclaimer

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