



# Harvest Capital Credit Corp. (HCAP)

Updated December 9<sup>th</sup>, 2020 by Nikolaos Sismanis

## Key Metrics

<b>Current Price:</b>	\$6.85	<b>5 Year CAGR Estimate:</b>	-0.3%	<b>Market Cap:</b>	\$40 M
<b>Fair Value Price:</b>	\$4.50	<b>5 Year Growth Estimate:</b>	0.0%	<b>Ex-Dividend Date:</b>	12/14/2020
<b>% Fair Value:</b>	152%	<b>5 Year Valuation Multiple Estimate:</b>	-8.1%	<b>Dividend Payment Date:</b>	12/29/2020
<b>Dividend Yield:</b>	6.6%	<b>5 Year Price Target</b>	\$4.50	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	D	<b>Last Dividend Increase:</b>	N/A

## Overview & Current Events

Harvest Capital Credit Corporation is a publicly-traded Business Development Company (BDC) that provides customized financing to small and mid-sized businesses located throughout North America. Its services include senior secured debt, uni-tranche term loans, junior secured term loans, subordinated debt investments, and minority equity co-investments. Despite its tiny portfolio value of just around \$97 million, the company has stakes in 22 companies through various debt and equity structures.

On November 6<sup>th</sup>, 2020, Harvest Capital reported its Q3-2020 results for the period ending September 30<sup>th</sup>, 2020. Harvest Capital recorded a loss of -\$0.4 million vs. a net loss of -\$1.0 million in Q3-2019, primarily due to the company not realizing positive investment results from its underlying portfolio. Gross investment income from its investments came in at \$3.0 million, -6.3% lower than Q3-2019, primarily attributable to a smaller income-earning portfolio, a lower weighted-average effective yield on its income-earning portfolio, and an increase in interest expenses between periods. Net investment income (NII) per share for the quarter was \$0.14, a -22% decline YoY. Based on its most recent results, we expect the company to end its financial year with an NII/share of around \$0.45 (Q1-Q3 = \$0.34.) However, amid higher expenses due to COVID-19, we have utilized NII/share of \$0.50 in our estimates. Due to unsustainable distribution levels, the company had suspended its dividend since May. Management announced that it will pay investors two additional deferred monthly dividends for FY2020 (\$0.16 total) but has not announced a future DPS resumption rate going forward. To match our NII/share forecasts, we have assumed a reduced DPS post FY2020 in our estimates.

## Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
<b>NII/Share</b>	---	---	\$1.97	\$1.32	\$1.34	\$1.54	\$1.34	\$1.28	\$0.93	\$0.63	<b>\$0.45</b>	<b>\$0.50</b>
<b>DPS</b>	---	---	\$1.66	\$0.88	\$1.35	\$1.35	\$1.35	\$1.35	\$1.13	\$0.96	<b>\$0.45</b>	<b>\$0.45</b>
<b>Shares<sup>1</sup></b>	---	---	0.9	4.4	6.2	6.2	6.3	6.4	6.4	6.1	<b>6.0</b>	<b>7.0</b>

The company has chosen to be treated as business development company (BDC). Since its income is only derived by its underlying investments, net income per share (NII/share) is a more useful metric than earnings per share (EPS)

Over the past few years, Harvest Capital's NII/share has been continuously declining as a result of its tiny portfolio failing to attract higher-yielding investments, which in turn has caused Harvest Capital to have above-average financing costs. The weighted average effective yield of its debt and other income-producing investments, as of September 30<sup>th</sup>, 2020, and December 31<sup>st</sup>, 2019, was 12.6% and 14.0%, respectively. On the entire portfolio basis, these figures reduce to 8.6% and 11.3%, respectively. The company's performance is, therefore, deteriorating very rapidly.

Adding its deferred dividends soon to be paid out, Harvest Capital's FY2020 DPS should close at \$0.56. However, we have assumed an annualized rate of \$0.45 upon management's potential resumption. Along with our net investment income forecast, these figures remain quite speculative. We anticipate 0% growth ahead due to a lack of such catalysts.

<sup>1</sup> Share count is 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
P/NII	---	---	---	11.3	10.2	7.9	9.6	10.4	11.2	16.3	<b>13.7</b>	<b>9.0</b>
Avg. Yld.	---	---	---	5.9%	9.9%	11.0%	10.4%	10.1%	10.8%	9.3%	<b>6.6%</b>	<b>10.0%</b>

Despite Harvest Capital's weak historical performance, the stock has retained a valuation multiple similar to its peers. Based on our current estimate, shares are trading around 13.7 times net income. Considering that every relevant metric has performed significantly weaker than last year, combined with the lack of future growth catalysts, we believe that the stock's valuation multiple should not exceed 9. At this point, a double-digit yield would better reflect the company's underlying risks.

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

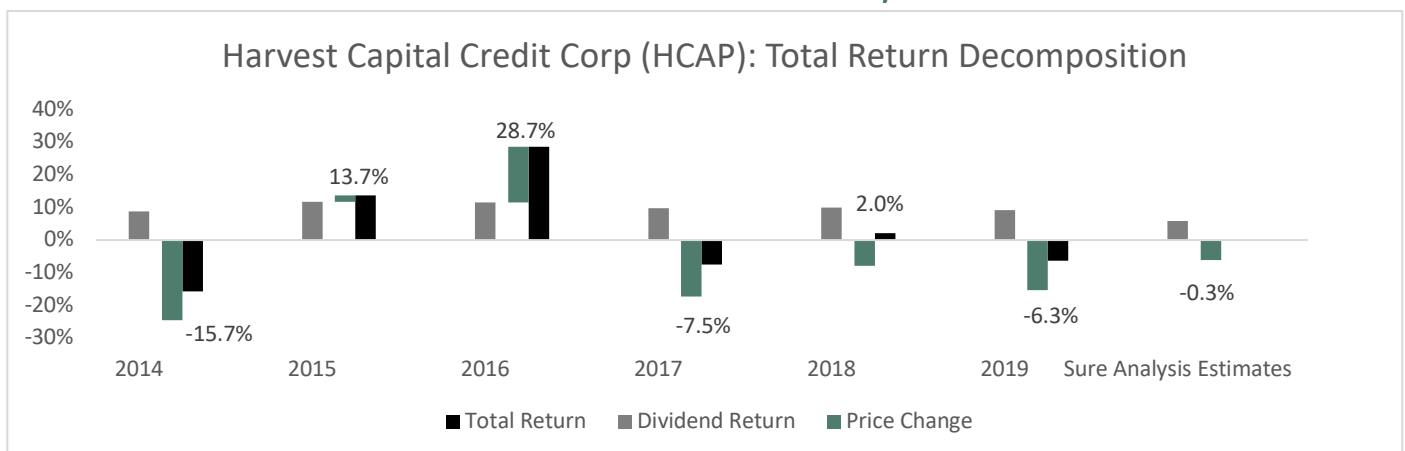
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	84%	67%	101%	88%	101%	105%	122%	152%	<b>90%</b>	<b>90%</b>

Harvest Capital's expected distribution levels should remain covered in the short term, backed by management's encouraging deferred dividend payments. However, the company's future financial performance remains incredibly risky. The company's small portfolio cannot be leveraged for management to achieve higher portfolio yields. It's a shame because management seems to be otherwise quite skilled. For example, on September 28th, 2020, the company received a \$7.1 million repayment, at par, on its senior secured debt investment in Kleen-Tech Acquisition, LLC and sold its warrants and received proceeds of \$0.6 million. Harvest Capital recorded \$0.3 million in exit and prepayment fees related to this transaction and retained its equity investment. Consequently, it generated an internal rate of return (IRR) of 27.5% on this investment. At its current position, however, such returns on new loans in the future are incredibly improbable. A future recession is likely to adversely affect Harvest Capital.

## Final Thoughts & Recommendation

Harvest Capital has been underperforming for years, featuring declining financials and poor portfolio characteristics. Its historical distributions have also failed to compensate for the stockholders' equity losses. Despite management's intention to return a couple of the previously deferred dividends to shareholders, the stock earn a sell rating. Even amid constant performance expectations, the stock's dividend may not compensate investors for the possibility of valuation compression.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	---	---	4	5	11	9	9	6	9	3
SG&A Exp.	---	---	---	1	2	2	3	4	4	3
Net Profit	---	---	4	4	9	6	6	2	5	(1)
Net Margin	---	---	91.4%	76.1%	84.1%	69.8%	64.6%	25.4%	53.8%	-44.7%
Free Cash Flow	---	---	(29)	(24)	(35)	(21)	16	21	26	(23)

## Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	---	---	50	91	120	149	143	128	125	140
Cash & Equivalents	---	---	8	19	0	1	4	4	27	11
Total Liabilities	---	---	30	2	29	60	56	46	47	73
Accounts Payable	---	---	2	1	1	1	1	1	1	1
Long-Term Debt	---	---	28	---	26	57	54	44	45	72
Shareholder's Equity	---	---	20	89	91	89	87	82	78	67
D/E Ratio	---	---	1.41	---	0.29	0.64	0.62	0.54	0.57	1.08

## Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	---	---	---	5.8%	8.9%	4.8%	4.1%	1.2%	4.0%	-0.9%
Return on Equity	---	---	---	7.6%	10.5%	7.1%	6.8%	1.9%	6.3%	-1.7%
ROIC	---	---	---	6.0%	9.1%	4.9%	4.2%	1.2%	4.1%	-0.9%
Shares Out.	---	---	0.9	4.4	6.2	6.2	6.3	6.4	6.4	6.1
Revenue/Share	---	---	0.66	1.22	1.81	1.47	1.48	1.00	1.47	0.44
FCF/Share	---	---	(4.79)	(5.40)	(5.72)	(3.41)	2.48	3.31	4.01	(3.79)

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

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