



Solar Senior Capital Ltd. (SUNS)

Updated December 2nd, 2020 by Nikolaos Sismanis

Key Metrics

Current Price:	\$15	5 Year CAGR Estimate:	5.3%	Market Cap:	\$236 M
Fair Value Price:	\$13	5 Year Growth Estimate:	0.0%	Ex-Dividend Date¹:	12/21/2020
% Fair Value:	113%	5 Year Valuation Multiple Estimate:	-2.4%	Dividend Payment Date:	12/30/2020
Dividend Yield:	8.2%	5 Year Price Target	\$13	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

Solar Senior Capital is a Business Development Company (BDC) which is externally managed by Solar Capital Partners. It invests primarily in senior first lien secured loans of private, middle-market companies. Its investment criteria include companies that generate revenues between \$50 million and \$1 billion, EBITDA of \$15 million to \$100 million, and resilient cash flows through economic cycles. Hence management avoids speculative investments as much as possible. Solar Senior Capital was founded in 2010 and is based in New York, New York.

On November 5th, 2020, Solar Senior Capital reported its Q3-2020 results for the quarter ending September 30th, 2020. Net investment income (NII) was \$4.8 million, a -15.7% decline year-over-year, as the company's portfolio yield was heavily reduced due to its exposure to LIBOR (London Interbank Offer Rate,) as well as an overall smaller portfolio due to exiting some of its investments. Gains made on these exits boosted EPS by 68% to \$0.54 despite the lower NII. However, amid a reduced asset base and paying out more in dividends than income received, net asset value (NAV) per share fell by -3.2%, to \$15.79. Solar Senior's current investment portfolio is diversified across approximately 206 unique borrowers in over 120 industries with an average issuer exposure at \$2.5 million, or <0.5% of its total loans.

Growth on a Per-Share Basis

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
IIPS²	---	(\$0.03)	\$1.46	\$1.10	\$1.01	\$0.09	\$1.88	\$1.46	\$0.86	\$1.43	\$1.30	\$1.30
DPS	---	\$0.60	\$1.29	\$1.41	\$1.41	\$1.41	\$1.41	\$1.41	\$1.41	\$1.41	\$1.20	\$1.20
Shares³	---	8.6	9.5	11.4	11.5	11.5	12.9	16.0	16.0	16.0	16.0	16.0

Solar Senior's conservative investment strategy has been a doubled-edged sword. The company's avoidance of higher risk investments has failed to deliver stable returns, as originally intended. At the current ultra-low rate environment, such companies can easily access financing, not allowing Solar to get high-enough portfolio yields. Financial services, insurance, and other traditional companies account for the majority of its investments. Industries that could potentially attract higher yields are almost completely absent, such as software, which makes up only 6.6% of its investments.

Hence, investment income per share (IIS) has struggled to sustain distributions. With the ongoing pandemic further increasing global credit availability, and with higher credit yields only found in tech at the moment, management was forced to cut its distributions this year, to an annualized rate of \$1.20. This was a move that was necessary considering the lackluster results as of late. The company pays its dividends on a monthly basis.

The company's recent exits should hopefully reallocate capital towards more fruitful returns. However, we don't expect any IIPS or DPS growth going forward. It's quite common for BDCs to issue equity in order to fund their future expansion, since they have to distribute at least 90% of their net income. As table depicts, the company has not issued any shares lately, indicating the lack of available investments that meet both the company's conservative criteria and adequate yields.

¹ Estimated dividend dates based on SUNS historical record.

² Investment Income per Share.

³ 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
Avg. P/I	---	---	12.3	16.7	16.9	---	11.4	11.8	19.3	11.7	11.3	10.0
Avg. Yld.	---	3.5%	7.6%	7.6%	9.1%	9.9%	8.8%	8.7%	8.7%	8.1%	8.2%	9.2%

Solar Senior Capital's valuation has been slightly higher than its peers, despite the company's relatively weak performance. We believe that the company will continue to struggle due to its strict and limited industry investment criteria. Hence, we believe that a more suitable valuation multiple would be around 10 times its underlying net income, which is closer to the industry average. This implies the possibility of a small valuation headwind.

The yield presently sits above 8% and will continue to drive investor returns.

Safety, Quality, Competitive Advantage, & Recession Resiliency

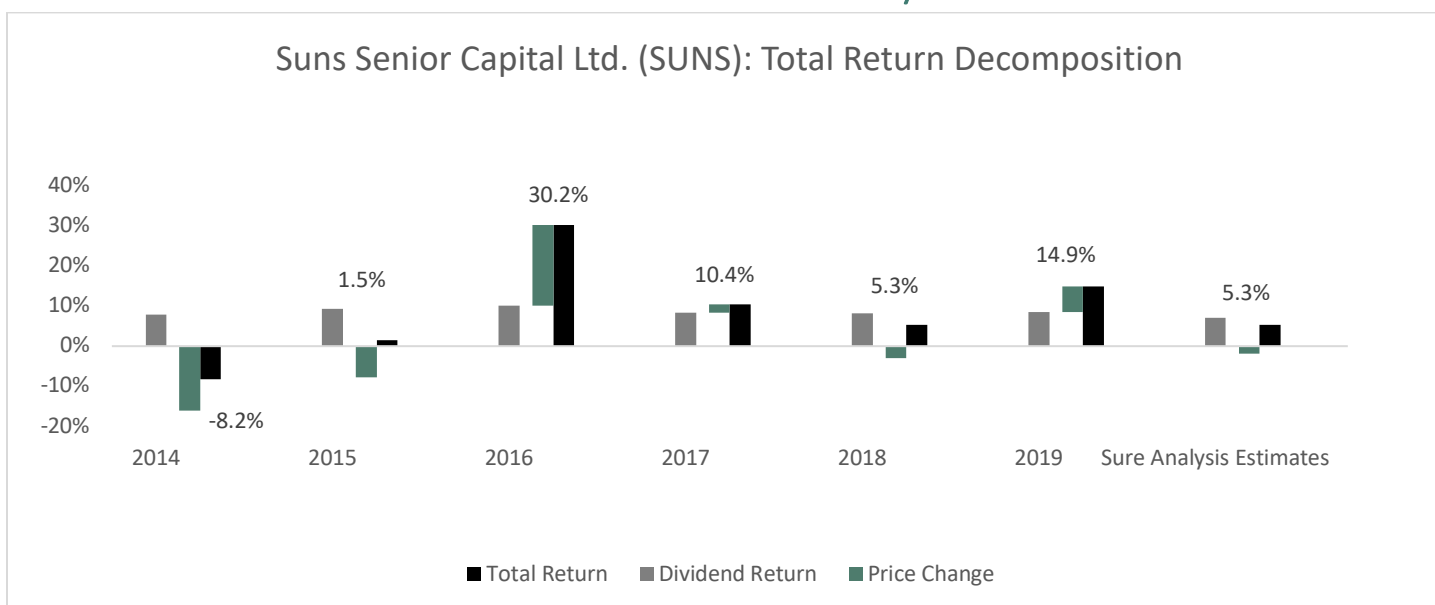
Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025
Payout	---	---	88%	128%	140%	---	75%	97%	164%	99%	92%	92%

The recent distribution cut should help the company sustain its current annualized dividend. However, considering the company's investment style, which limits portfolio growth, another cut is not impossible. While the company was not public during the last recession, its investment performance has been stable during the ongoing pandemic. The company's issues are mostly related to the available investments and refinancing rates, rather than its underlying portfolio. Finally, while there are some qualities to appreciate, such as the stable cash flows and the external management that reduces costs, the company doesn't showcase any competitive advantages whatsoever.

Final Thoughts & Recommendation

Solar Senior Capital has performed decently over the past few years, with a relatively stable distribution track record despite the recent cut. However, as financing has become cheaper, the company's portfolio has been performing weaker both due to LIBOR declining, and companies having cheaper capital options. Total return potential comes in at 5.3% per annum, driven by the 8.2% distribution yield, offset by a valuation headwind. Shares earn a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Revenue	---	8	17	15	14	3	25	24	16	23
SG&A Exp.	---	1	3	2	2	2	3	3	3	3
Net Profit	---	(0)	14	13	12	1	24	23	14	23
Net Margin	---	-3.2%	83.2%	83.9%	86.4%	38.5%	97.4%	96.8%	88.2%	98.1%
Free Cash Flow	---	(176)	(20)	(44)	(26)	54	60	(47)	(126)	84

Balance Sheet Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total Assets	---	187	217	273	385	363	522	522	459	578
Cash & Equivalents	---	3	3	3	42	53	152	109	5	107
Total Liabilities	---	15	43	65	181	174	253	252	198	316
Accounts Payable	---	5	2	1	37	57	153	124	26	105
Long-Term Debt	---	9	39	61	143	116	98	124	169	209
Shareholder's Equity	---	172	174	208	204	188	269	270	261	262

Profitability & Per Share Metrics

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Return on Assets	---	---	6.9%	5.2%	3.6%	0.3%	5.5%	4.5%	2.8%	4.4%
Return on Equity	---	---	8.0%	6.6%	5.7%	0.5%	10.6%	8.7%	5.2%	8.8%
ROIC	---	---	7.1%	5.2%	3.8%	0.3%	7.2%	6.1%	3.4%	5.1%
Shares Out.	---	8.6	9.5	11.4	11.5	11.5	12.9	16.0	16.0	16.0
Revenue/Share	---	0.91	1.76	1.32	1.17	0.24	1.94	1.51	0.98	1.46
FCF/Share	---	(20.35)	(2.07)	(3.83)	(2.25)	4.67	4.63	(2.91)	(7.85)	5.25

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

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