Monroe Capital Corporation (MRCC)

Updated April 20th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	$10.77	**5 Year CAGR Estimate:**	10.4%	**Market Cap:**	$227M
Fair Value Price:	$12.33	**5 Year Growth Estimate:**	0.0%	**Ex-Dividend Date:**	06/12/2021[1]
% Fair Value:	87%	**5 Year Valuation Multiple Estimate:**	2.8%	**Dividend Payment Date:**	06/30/2021
Dividend Yield:	9.3%	**5 Year Price Target**	$12.3	**Years Of Dividend Growth:**	N/A
Dividend Risk Score:	F	**Retirement Suitability Score:**	B	**Last Dividend Increase:**	N/A

Overview & Current Events

Monroe Capital Corporation is a specialty finance company focused on providing financing solutions primarily to lower middle-market companies in the United States and Canada. It is externally managed by Monroe Capital and has chosen to be treated as a development company (BDC). The company primarily invests in senior and "unitranche" secured loans ranging between $2.0 million and $25.0 million each. It generates nearly $60 million annually in total investment income and is headquartered in Chicago, Illinois.

On March 2nd, 2021, Monroe Capital Corporation reported its Q4 results for the fiscal year ended December 31st, 2020. Total investment income during those three months was $12.6 million, compared to $13.4 million in Q3. The $0.8 million decline was attributable to a decrease in interest income, primarily due to a smaller average investment portfolio size during the quarter. However, due to management and incentive fee waivers, net investment income (NII) only declined by 4.4% compared to Q3. On a per-share basis, NII declined from $0.26 to $0.25 quarter-over-quarter. The net asset value (NAV) per share increased by 1.6% to $11.0 during the quarter, primarily due to net gains on the portfolio, since the NII/share or $0.25 was in line with the Q4 dividend of $0.25 per share.

As of December 31st, the company's portfolio comprises 89 companies, totaling $547 million, with a weighted average annualized yield of 7.7%. Around 85.8% of its funds are allocated in 1st Lien Senior Secure and 1st Lien "unitranche" securities, while equities only account for 4.4%. In terms of the portfolio's industry exposure, high-tech, business services, and financials & real estate accounted for 14.9%, 14.4%, and 13.3%.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
NII/share	---	$0.15	$1.13	$1.57	$1.60	$1.55	$1.40	$1.57	$1.42	$1.45	***$1.45***	***$1.45***
DPS	---	$0.34	$1.36	$1.36	$1.40	$1.40	$1.40	$1.40	$1.40	$1.10	***$1.00***	***$1.10***
Shares[2]	---	5.4	7.6	9.6	11.7	14.5	18.6	20.3	20.4	20.9	***22.2***	***30.0***

Since Monroe Capital Corporation's IPO in 2012, the company has produced stable net investment income per share, maintaining a robust relationship between its investment yields and financing costs. Performance remained resilient even during 2020, a year of significant challenges, assisted by management's fee waivers, which showcased prudent behavior. The mid-year dividend cut from a quarterly rate of $0.35 to $0.25 also displayed management's prudent behavior. Management assured investors that there was not a coverage issue, as Monroe achieved an adequate NII/share. Instead, this was only a precautionary decision, and they would readjust the dividend upon evidence of a sustained economic recovery resulting in a positive impact on its NII.

With the economy gradually doing so, we have implemented a DPS CAGR of 2% over the next five years to price in the possibility of such a hike materializing. We are also expecting NII/share to remain rather stable in the medium term, as even if NII/share grows slightly moving forward, the possibility of a lower investment yield later cannot be ignored, and hence it has to be accounted for.

[1] Estimated dates based on past dividend dates

[2] 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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The share count should continue to grow moving forward as Monroe continues issuing equity to funds its investments. Finally, while the dividend has always been covered, not deteriorating the underlying NAV, the NAV/share has gradually declined from $14.72 in its IPO to $11 as of its latest report, due to some of its equity and debt investments resulting in realized and unrealized loss of investment capital.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/NII	---	---	12.0	9.0	8.9	9.4	11.1	8.7	8.8	5.1	***7.4***	***8.5***
Avg. Yld.	---	2%	10%	10%	10%	10%	9%	10%	11%	15%	***9.3%***	***9.0%***

Monroe's valuation had remained close to that of its industry peers until 2019, hovering in the high-single to low double-digits. Despite the company generating robust investment income during 2020, NAV/share fell by 9.8% to $11 amid unrealized portfolio losses. Along with the fact that Mr. Market didn't like the dividend cut, its valuation has now been compressed to around 7.4 times its net investment income. We expect the stock's valuation to expand closer to its fair value, at a P/NII of around 8.5, as investors get to appreciate more the company's high yield and potential for a dividend increase moving forward. The stock is also currently trading under its NAV/share at its current price of $10.74.

Safety, Quality, Competitive Advantage, & Recession Resiliency

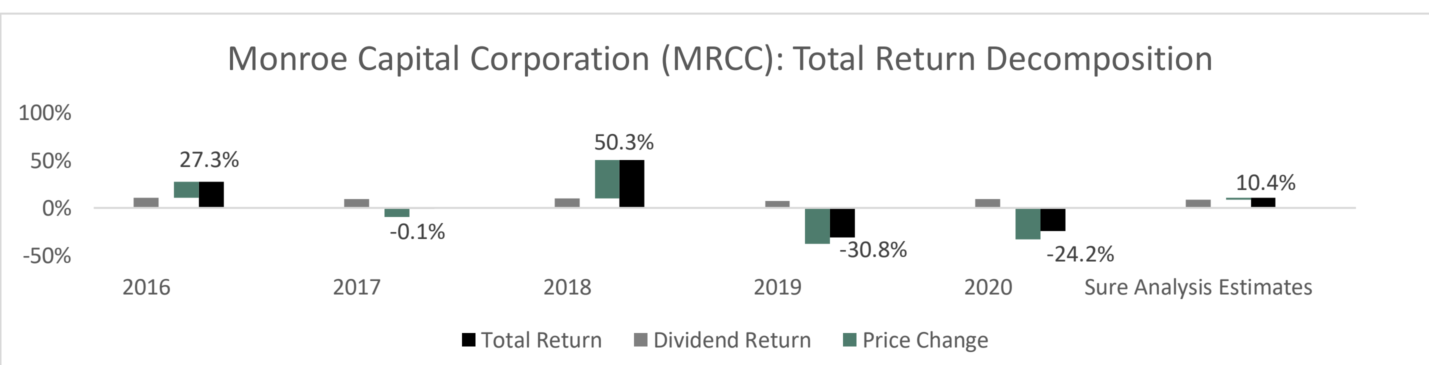
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	---	---	120%	87%	88%	90%	100%	89%	99%	76%	***69%***	***76%***

Monroe's dividend could be considered relatively safe, adequately covered by the company's net investment income generation. We believe another dividend cut is quite unlikely at this point. The company's qualities include a well-diversified portfolio of companies with a robust investment yield and a prudent management team. That being said, Monroe has not been tested by a prolonged recession, which could indeed damage its performance if it were to occur. Being a business development company of modest size, the company does not enjoy any noteworthy competitive advantage, other than the experience of its investment advisor, Monroe Capital, whose senior management average more than 30 years of experience, overseeing around $9.4 billion in assets under management.

Final Thoughts & Recommendation

Overall, we believe that Monroe Capital Corporation is a prudently managed company that has showcased resilient investment income results, despite experiencing some NAV losses over the years. Powered by our expectations of a potential dividend increase over time, along with the possibility for valuation expansion towards the stock's fair value and actual NAV/share, we forecast annualized returns of around 10.4% going forward. Hence, shares earn a Buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue		1	13	17	22	29	17	11	24	7
SG&A Exp.		0	2	3	3	3	4	4	4	3
Net Profit		1	10	14	18	24	12	6	19	2
Net Margin		76.8%	77.0%	79.8%	82.6%	84.4%	73.2%	53.9%	81.5%	25.3%
Free Cash Flow		(132)	(63)	(12)	(83)	(52)	(70)	(55)	(39)	75

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets		139	226	244	357	425	507	580	655	585
Cash & Equivalents		4	15	5	5	6	4	4	2	7
Accounts Receivable		56	88	110	173	184	229	321	406	351
Total Liabilities		0	1	1	2	3	4	5	5	5
Long-Term Debt		55	84	106	163	178	222	314	396	344
Shareholder's Equity		84	138	134	185	241	279	259	249	234
D/E Ratio		0.66	0.61	0.79	0.88	0.74	0.80	1.21	1.59	1.47

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets			5.4%	5.9%	6.0%	6.2%	2.6%	1.1%	3.1%	0.3%
Return on Equity		2.3%	8.8%	10.2%	11.2%	11.5%	4.7%	2.2%	7.6%	0.7%
ROIC			5.4%	6.0%	6.1%	6.4%	2.6%	1.1%	3.2%	0.3%
Shares Out.		5.4	7.6	9.6	11.7	14.5	18.6	20.3	20.4	20.9
Revenue/Share		0.23	1.66	1.82	1.85	1.98	0.89	0.53	1.15	0.31
FCF/Share		(24.5)	(8.25)	(1.20)	(7.08)	(3.57)	(3.74)	(2.71)	(1.92)	3.58

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

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