



Gladstone Investment Corp. (GAIN)

Updated May 14th, 2021 by Jonathan Weber

Key Metrics

Current Price:	\$14	5 Year CAGR Estimate:	2.0%	Market Cap:	\$460M
Fair Value Price:	\$10	5 Year Growth Estimate:	3.0%	Ex-Dividend Date:	05/18/21
% Fair Value:	146%	5 Year Valuation Multiple Estimate:	-7.3%	Dividend Payment Date:	05/28/21
Dividend Yield:	6.0%	5 Year Price Target	\$11	Years Of Dividend Growth:	9
Dividend Risk Score:	F	Retirement Suitability Score:	D	Last Dividend Increase:	2.9%

Overview & Current Events

Gladstone Investment is a business development company (BDC) that focuses on US-based small- and medium-sized companies. Industries which Gladstone Investment targets include aerospace & defense, oil & gas, machinery, electronics, and media & communications. The company was founded in 2005 and is headquartered in McLean, VA.

Gladstone Investment reported its fourth quarter (Q4 2020 ended March 31) earnings results on May 11. The company generated total investment income - Gladstone Investment's revenue equivalent - of \$16.7 million during the quarter, which represents a decline of 4% compared to the prior year's quarter. This number beat the analyst consensus estimate by \$3 million, as analysts expected a wider decline from the company's top line.

Gladstone Investment's adjusted net investment income-per-share totaled \$0.20 during the fiscal fourth quarter. That was down from the previous quarter's level of \$0.24. Gladstone Investment's net asset value per share totaled \$11.52 on a per-share basis at the end of the quarter, which was up meaningfully versus the \$11.11 of NAV-per-share that the company reported at the end of the previous quarter. The increase was based on the fact that net profits, on a not-adjusted basis, during the quarter were higher than the dividend payments that Gladstone Investment Corp. made during the same period. 2020's NIIPS was down quite meaningfully versus 2019, due to the impact of the pandemic. It looks like the company will recover meaningfully during the current fiscal year, however, as recent quarterly results were already close to the pre-crisis run rate again.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
NIIPS	\$0.73	\$0.62	\$0.68	\$0.73	\$0.75	\$0.68	\$0.74	\$0.77	\$0.90	\$0.69	\$0.80	\$0.93
DPS	\$0.48	\$0.61	\$0.60	\$0.71	\$0.73	\$0.75	\$0.75	\$0.82	\$0.84	\$0.84	\$0.84	\$0.88
Shares¹	22	26	26	26	30	30	33	33	33	33	33	35

Gladstone Investment's net investment income per share is quite lumpy. During the financial crisis the company's profits declined substantially, but Gladstone Investment remained profitable. Over the last five years profits grew by 4.3% annually, which is not a very high growth rate, but which is also not at all disappointing for a high-yielding investment.

Gladstone Investment's business model is relatively straightforward. The company lends money to small- and mid-sized companies. Position sizes for debt investments usually range from \$5 million to \$30 million. The company also takes equity stakes in such companies, with position sizes for equity investments typically ranging from \$10 million to \$40 million. The companies Gladstone Investment does business with usually cannot access debt or equity markets directly, as bond sales and public listings are not possible for them due to their small size. Gladstone Investment makes its money via spreads between the interest rates the company pays on cash that it borrows, and the interest rates the company receives on cash that it lends - the same principle as with banks. Declining interest rates could turn into a headwind, but so far Gladstone Investment's weighted average interest yield has held up very well; the company generated a yield of around 13% before the pandemic. A short-term headwind will stem from higher loan losses that will be caused by the coronavirus crisis, but we do not see this impacting profitability in the long run.

¹ 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	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
P/NII	10.1	12.1	10.7	10.5	10.2	11.9	12.8	15.3	8.9	17.8	17.5	12.0
Avg. Yld.	6.5%	8.1%	8.2%	9.2%	10.1%	9.3%	7.9%	7.0%	10.5%	6.8%	6.0%	7.9%

Gladstone Investment has been valued at a low-double-digit price to net investment income multiple throughout the majority of the last decade. Today, shares trade above this historic valuation, using our earnings-per-share estimate for the current fiscal year (FY 2021). We thus believe that multiple contraction will be a meaningful headwind for the company's total return outlook, since we expect that valuations will come down over the years.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	65.8%	98.4%	88.2%	97.3%	103%	110%	101%	106%	93.3%	122%	105%	95.2%

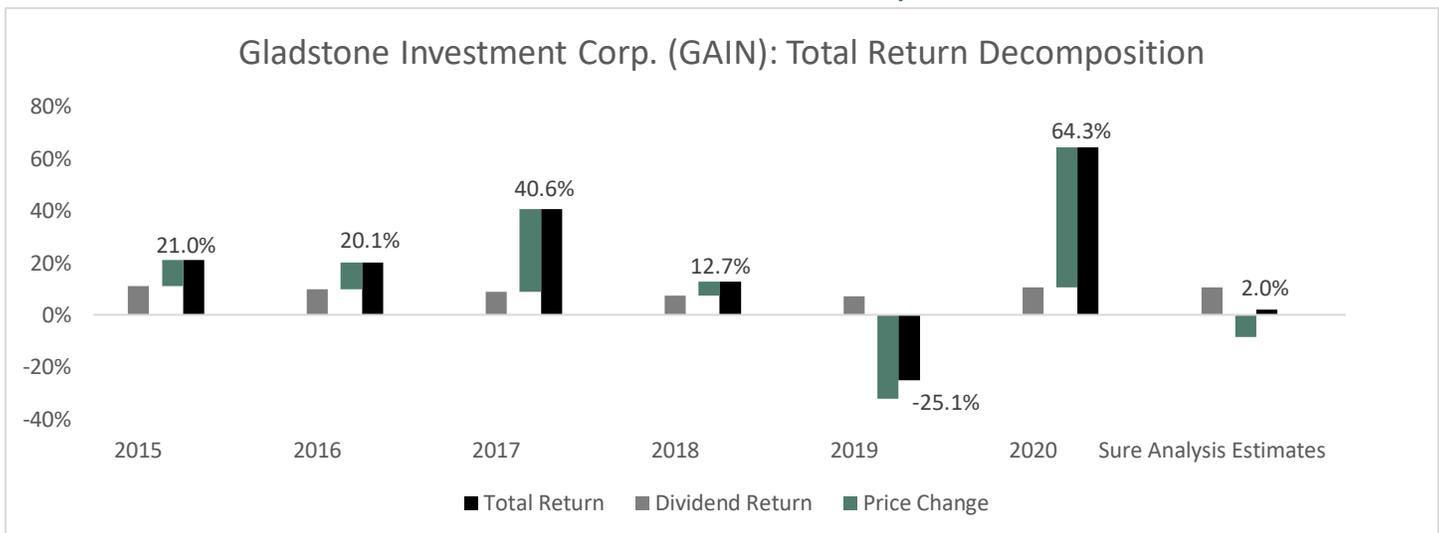
Gladstone Investment's dividend payout ratio, relative to its net investment income, has been close to or above 100% throughout several years over the last decade. The company usually is more profitable than the net investment income metric suggests, due to the fact that Gladstone Investment can also generate gains from its equity investments, which are not reflected in the net investment income metric. The company nevertheless had to cut its dividend during the last financial crisis, but so far, the company is confident it will not have to cut its payout during the pandemic.

Gladstone Investment's equity investment gains explain the company's long-term book value growth. Gladstone Investment's recession performance is not very compelling compared to less cyclical income stocks, but at least the company remained profitable during the last financial crisis, unlike many other financial corporations. We also see Gladstone remaining profitable during the current global crisis, but profits will be down from prior highs.

Final Thoughts & Recommendation

Gladstone Investment is a business development company targeting small companies that do not have the ability to access debt and/or equity markets easily. This allows Gladstone to demand above-average interest rates. The company does not generate a lot of growth, but the high payout ratio allows for an above-average dividend yield. Right now, shares trade well above fair value, which is why we rate Gladstone Investment a sell.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	24	18	(1)	51	29	49	65	99	8	49
SG&A Exp.	3	3	3	3	4	4	4	6	6	6
D&A Exp.	22	17	(1)	50	25	45	61	82	(7)	42
Net Profit	90.4%	93.5%	138%	98.7%	85.3%	90.6%	92.9%	82.2%	-90.4%	87.1%
Net Margin	(49)	(40)	(34)	(98)	4	33	(30)	94	35	(30)
Free Cash Flow	24	18	(1)	51	29	49	65	99	8	49

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	325	380	331	484	503	515	611	635	576	644
Cash & Equivalents	92	86	5	5	4	3	4	2	3	2
Accounts Receivable	118	139	110	210	224	214	257	228	207	261
Total Liabilities	1	1	1	1	1	1	1	1	1	1
Accounts Payable	76	95	67	124	100	75	113	58	54	151
Long-Term Debt	207	241	221	273	279	301	354	407	369	382
Shareholder's Equity	0.37	0.39	0.30	0.45	0.36	0.25	0.32	0.14	0.15	0.40
D/E Ratio	325	380	331	484	503	515	611	635	576	644

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	7.8%	4.9%	-0.4%	12.3%	5.0%	8.8%	10.8%	13.1%	-1.2%	7.0%
Return on Equity	10.8%	7.7%	-0.6%	20.3%	9.0%	15.4%	18.5%	21.4%	-1.9%	11.3%
ROIC	8.4%	5.6%	-0.4%	14.7%	6.4%	11.9%	14.4%	17.5%	-1.6%	8.9%
Shares Out.	22	26	26	26	30	30	33	33	33	33
Revenue/Share	1.10	0.76	(0.04)	1.91	0.96	1.63	2.02	3.02	0.24	1.47
FCF/Share	(2.2)	(1.64)	(1.27)	(3.66)	0.13	1.08	(0.92)	2.85	1.07	(0.90)

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

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