



Annaly Capital Management (NLY)

Updated November 3rd, 2021 by Samuel Smith

Key Metrics

Current Price:	\$8.6	5 Year CAGR Estimate:	7.7%	Market Cap:	\$12.4B
Fair Value Price:	\$7.8	5 Year Growth Estimate:	-0.4%	Ex-Dividend Date:	12/29/21 ¹
% Fair Value:	110%	5 Year Valuation Multiple Estimate:	-1.9%	Dividend Payment Date:	01/30/22 ²
Dividend Yield:	10.2%	5 Year Price Target	\$8.00	Years of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	B	Last Dividend Increase:	NA

Overview & Current Events

Annaly Capital Management, Inc., a diversified capital manager, invests in and finances residential and commercial assets. The trust invests in various types of agency mortgage-backed securities, non-agency residential mortgage assets, and residential mortgage loans. It also originates and invests in commercial mortgage loans, securities, and other commercial real estate investments. Annaly provides financing to private equity-backed middle market businesses and operates as a broker-dealer. The trust has elected to be taxed as a real estate investment trust (REIT). As a REIT, it is not subject to federal income tax to the extent that it distributes its taxable income to its shareholders. Annaly Capital Management, Inc. was founded in 1996 and is based in New York, New York.

Q3 results were reported on October 27th. Annaly reported a 2.9% quarterly economic return and tangible economic return in Q3. Economic leverage stood at 4.4x, down from 4.7x in the prior quarter. Book value per common share stood at \$8.39, up slightly from \$8.37 sequentially.

Net interest margin, excluding PAA, stood at 2.04% against 2.09% in Q2 while Q3 net interest spread, excluding PAA, stood at 1.97%, up from 1.93% in the prior quarter. Meanwhile, GAAP net income came in at \$0.34 per average common share for the quarter. The company also reported 15.3% of annualized GAAP return on average equity and 12.8% of annualized EAD return on average equity.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
EPS	\$0.39	\$1.79	\$3.94	-\$0.89	\$0.49	\$1.48	\$1.47	\$0.04	\$1.19	\$1.10	\$1.12	\$1.10
DPS	\$2.44	\$2.05	\$1.50	\$1.20	\$1.20	\$1.20	\$1.20	\$1.20	\$1.00	\$0.91	\$0.88	\$1.00
Shares³	970.3	947.3	947.5	947.7	924.8	1018.9	1159.6	1400.1	1430.3	1398.5	1444.3	1800

Instability in the markets created valuation declines across the sector in late 2019 into 2020 as interest rate volatility put pressure on the bottom lines of mortgage REITs, revealing the cyclical nature of this investment vehicle. With increasing interest rates, Annaly saw a narrowing between interest income and expenses, as well requiring greater amounts of leverage to produce declining results.

The stock price has also continued to decline as additional shares have been issued to grow the capital base without the results transferring to the bottom line. Moving forward, the stabilization of interest rates could help them to catch up later this year. However, with interest rates still far below long-term averages, there will be pressure to continue increasing interest rates as the economy continues to grow, negatively impacting Annaly.

Given lingering disruptive impacts from the coronavirus outbreak, we expect weak earnings per share growth to go along with management's precautionary dividend cut. Prepayments are a further risk given how low rates are, which drives refinance activity.

¹ Estimated date

² Estimated date

³ 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
Avg. P/E	40.55	7.86	2.53	---	19.02	6.74	8.08	220	8.0	6.9	7.7	7.0
Avg. Yld.	15.4%	14.6%	15.0%	---	12.8%	12.0%	10.1%	13.6%	10.5%	11.9%	10.2%	13.0%

The cyclical nature of this trust's earnings makes them difficult to value based on challenging years like 2018. We believe that the fair value P/E should be around 8 based on past performance, but current headwinds for the industry are causing us to reduce our estimate to 7 times earnings. As a result, we believe the stock is slightly overvalued at present based on expected 2021 results.

Safety, Quality, Competitive Advantage, & Recession Resiliency

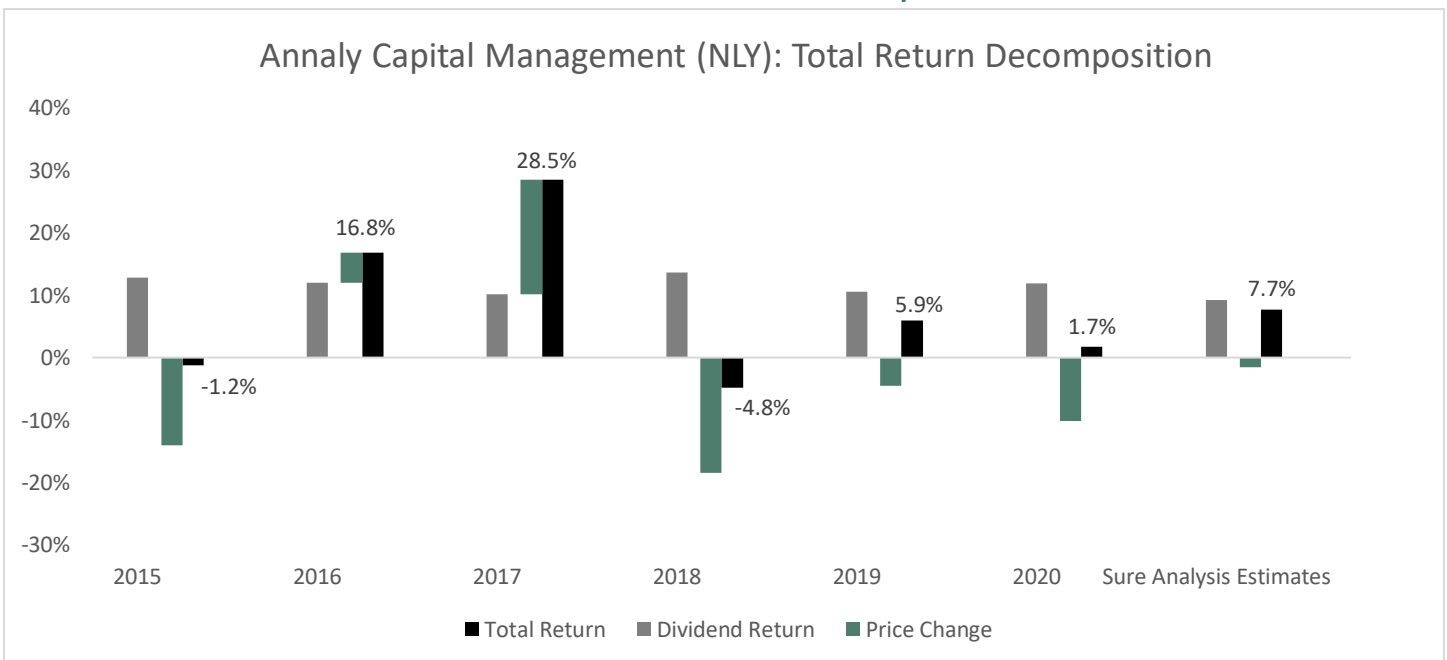
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	626%	115%	38%	-135%	245%	81%	82%	3000%	84%	83%	79%	91%

The advantage Annaly has over some of its mortgage REIT competitors is diversification within their income stream, providing them the opportunity to pivot depending on the circumstance. That said, Annaly is very interest rate sensitive. Although it is less levered than others in the sector, we have concern that Annaly is using more leverage to generate results and issuing additional shares to drive capital expansion, rather than growing based on increased profitability. With debt ratios rising and interest rates being currently stable, but with the potential to rise further, the payout ratio will almost surely remain very high.

Final Thoughts & Recommendation

With a total return outlook of 7.7% and a mouthwatering 10.2% dividend yield compensating for considerable uncertainty in its business model, we rate the stock a hold given the inherent risk involved in mREITs, as well as the decent but not great total return outlook.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	640	2169	3997	-615	734	1565	1684	275	-1992	-585
SG&A Exp.	237	236	232	209	200	250	224	330	302	239
D&A Exp.	2	4	3	5	20	42	28	72	32	41
Net Profit	344	1736	3730	-842	467	1434	1570	54	-2163	-891
Net Margin	53.9%	80.0%	93.3%	136.9%	63.5%	91.6%	93.2%	19.8%	108.6%	152.4%
Free Cash Flow	2417	7640	-12893	6128	-3643	1407	1621	-42174	-64665	-32149
Income Tax	59	36	8	5	-2	-2	7	-2	-11	-28

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	109630	133452	81922	88355	75191	87905	101760	105788	130295	88455
Cash & Equivalents	994	616	552	1741	1769	1540	707	1736	1851	1244
Acc. Receivable	412	419	273	278	231	270	325	426	455	284
Goodwill & Int.	53	62	95	133	110	758	676	659	471	228
Total Liabilities	93869	117528	69517	75022	63285	75329	86888	91670	114499	74433
Accounts Payable	146	198	186	228	205	347	910	1154	940	1075
Long-Term Debt	540	826	859	1266	4734	7865	7119	8041	10564	7036
Total Equity	15584	15011	11492	12415	10983	11368	13145	12334	13810	12472
D/E Ratio	0.03	0.05	0.07	0.10	0.40	0.63	0.48	0.57	0.67	0.50

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	0.4%	1.4%	3.5%	-1.0%	0.6%	1.8%	1.7%	0.1%	-1.8%	-0.8%
Return on Equity	2.7%	11.3%	28.1%	-7.0%	4.0%	12.8%	12.8%	0.4%	-16.5%	-6.8%
ROIC	2.6%	10.5%	24.9%	-6.0%	3.0%	7.7%	7.4%	0.2%	-8.9%	-3.8%
Shares Out.	874	972	947	947	947	969	1066	1210	1319	1430
Revenue/Share	0.73	2.16	4.01	-0.65	0.78	1.61	1.58	0.23	-1.39	-0.41
FCF/Share	2.76	7.60	-12.9	6.47	-3.85	1.45	1.52	-34.8	-45.1	-22.7

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

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