



SLR Investment Corp. (SLRC)

Updated August 8th, 2022 by Nikolaos Sismanis

Key Metrics

Current Price:	\$15.09	5 Year CAGR Estimate:	6.5%	Market Cap:	\$826.2 M
Fair Value Price:	\$14.50	5 Year Growth Estimate:	-2.2%	Ex-Dividend Date:	08/17/22
% Fair Value:	104%	5 Year Valuation Multiple Estimate:	-0.8%	Dividend Payment Date:	09/01/22
Dividend Yield:	10.9%	5 Year Price Target	\$12.97	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Hold

Overview & Current Events

SLR Investment Corp. is a closed-end, externally managed, non-diversified management investment company that has elected to be regulated as a business development company (“BDC”). The company invests primarily in leveraged middle-market companies with annual revenues typically between \$50 million and \$1 billion. They do so in the form of senior secured loans, financing leases, and to a lesser extent, unsecured loans and equity securities. SLR’s investments generally range between \$5 million and \$100 million each. On June 30th, 2022, the company’s portfolio consisted of 127 companies with a 30.0% exposure in senior secured loans, a 30.9% exposure in asset-based senior secured loans and credit solutions, a 14.1% exposure in Kingsbridge Holdings (equipment lessor), a 24.3% exposure in equipment senior secured financings, and 14.8% exposure in life science senior secured loans. SLR Investment Corp. generates around \$165 million in total investment income annually and is based in New York, New York.

On August 2nd, 2022, SLR Investment Corp. reported its Q2-2022 results for the period ending March 31st, 2022. For the quarter, total investment income totaled \$42.8 million, 20.2% higher year-over-year. The increase was primarily due to a larger portfolio. Expenses totaled \$22.5 million, 15.4% higher compared to last year. The relatively lower increase in expenses was primarily due to the reduction in incentive fees related to the merger with SUNS. Net investment income for the quarter totaled \$20.3 million or \$0.37 on a per share basis. This compared with a net investment income of \$14.8 million, or \$0.35 on a per share basis. We continue to forecast NII/share to land close to \$1.45 for fiscal 2022.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
NAV/shr	\$22.70	\$22.50	\$22.05	\$20.79	\$21.74	\$21.81	\$21.75	\$21.44	\$20.16	\$19.93	\$18.53	\$16.58
NII/shr	\$2.20	\$1.91	\$1.56	\$1.52	\$1.68	\$1.62	\$1.77	\$1.71	\$1.40	\$1.41	\$1.45	\$1.30
DPS	\$2.40	\$2.00	\$1.60	\$1.60	\$1.60	\$1.60	\$1.64	\$1.64	\$1.64	\$1.64	\$1.64	\$1.47
Shares¹	38.7	44.2	42.5	42.5	42.2	42.3	42.3	42.3	42.3	42.3	57.8	80.0

With nearly 80% of SLR Investment Corp’s income-producing investment portfolio attached to floating rates, the company’s net investment income had been under pressure over the past few years. On the one hand, with interest rates on the rise, the company’s bottom line should benefit. Further, with the base annual management fee down from 1.75% to 1.5% following the recent merger with SUNS, net margins should rise. However, going back to our coverage of SUNS prior to the merger, we believe that the company’s investment portfolio appeared rather weak. Thus, it’s uncertain whether SLR’s net investment income will actually benefit from the merger. In addition, the company revised the distribution policy post-merger, now making monthly distributions instead of quarterly. However, distributions have historically, and especially lately, exceeded the underlying NII generation. This has resulted in the company’s NAV/share declining over the past few years. A lower NAV leads to lower NII (smaller asset base), and so on. Thus, we believe that unless the recent merger and rising rates boost results, the company’s NII/share DPS will eventually decline in the coming years. While DPS may not decline annually, we have set our NAV/share, NII/share, and DPS CAGR estimates at a negative 2.2% each over the medium-term, reflecting the ongoing NAV deterioration rate.

¹ Share count 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	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Avg. P/NII	10.5	12.0	13.1	11.5	11.9	13.1	11.9	12.0	11.4	13.3	10.4	10.0
Avg. P/NAV	1.02	1.02	0.93	0.84	0.92	0.97	0.97	0.96	0.79	0.94	0.81	---
Avg. Yld.	10.4%	8.7%	7.8%	9.2%	8.0%	7.5%	7.8%	8.0%	10.3%	8.7%	10.9%	11.3%

Since SLR's distributions started exceeding the underlying NII generation, shares have been trading at a discount to NAV as investors are already pricing in NAV's continuous deterioration. Shares are currently trading at a nearly 20% discount to NAV. Thus, the yield has climbed to massive levels as investors demand a higher return for the underlying risks attached. We have set the fair P/NII multiple at 10, reflecting further valuation headwinds ahead amid SLR's current unsustainable payouts. The BoD recently approved a \$50 million share buyback program to exploit the discount to NAV. However, we question whether further complexity to an already risky capital allocation strategy will be beneficial.

Safety, Quality, Competitive Advantage, & Recession Resiliency

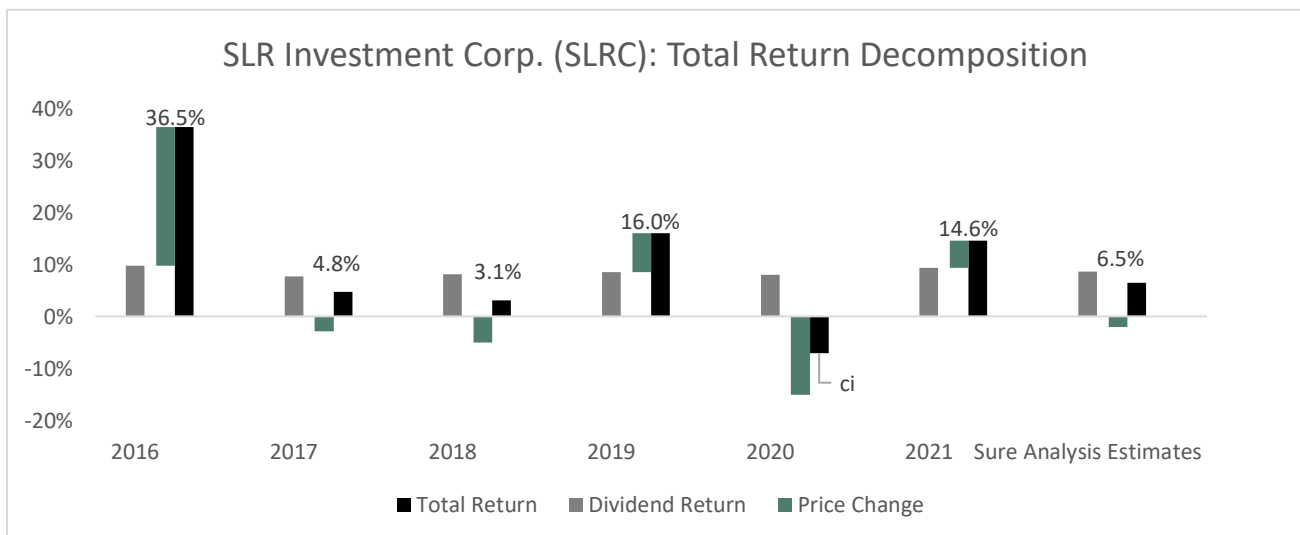
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	109%	105%	103%	105%	95%	99%	93%	96%	117%	116%	113%	113%

While SLR may continue to deteriorate its NAV to sustain the current distribution rate, we don't believe that this is a viable strategy over the long run. A sudden cut may occur, similar to 2013. It's worth noting that SLR's portfolio primarily consists of loans associated with equipment financings, corporate leases, and other asset-based lendings. Therefore, a potential recession that could reduce demand for such equipment amid reduced corporate CAPEX could further impact SLR's results. SLR maintains an investment grade rating from both Moody's (Baa3) and Fitch's (BBB-), nonetheless.

Final Thoughts & Recommendation

SLR Investment Corp is a unique BDC, with its focus on asset-based senior secured loans and equipment financing, distinguishing it from its more traditional peers. While the recent merger and rising rates could benefit the company, we believe that the ongoing NAV deterioration will persist at the current distribution rate. We forecast annualized returns of 6.5% through the medium-term, as dividend returns from the sky-high yield could be offset by declines in NII, DPS, and valuation headwinds. Shares earn a hold rating. But, again, investors should not blindly trust the dividend.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	124	86	57	21	117	82	76	66	24	70
SG&A Exp.	8	10	9	8	10	9	9	8	8	10
Net Profit	116	75	48	14	107	70	67	56	15	60
Net Margin	93.4%	87.7%	84.7%	68.2%	91.2%	85.8%	87.7%	84.4%	65.5%	85.7%
Free Cash Flow	(229)	799	157	(498)	148	(243)	191	188	(61)	(135)

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	1,430	1,708	1,686	1,617	1,651	1,642	1,683	1,950	1,936	2,011
Cash & Equivalents	14	585	635	278	312	151	207	436	389	323
Total Liabilities	552	713	750	735	732	720	764	1,044	1,084	1,169
Accounts Payable	47	474	511	19	329	165	273	441	401	342
Long-Term Debt	489	225	225	430	387	539	474	587	671	812
Shareholder's Equity	878	996	937	883	919	922	919	906	852	842
LTD/E Ratio	0.56	0.23	0.24	0.49	0.42	0.59	0.52	0.65	0.79	0.96

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	9.2%	4.8%	2.9%	0.9%	6.5%	4.3%	4.0%	3.1%	0.8%	3.0%
Return on Equity	13.7%	8.0%	5.0%	1.5%	11.9%	7.7%	7.3%	6.1%	1.8%	7.0%
ROIC	9.6%	5.8%	4.1%	1.1%	8.2%	5.1%	4.7%	3.9%	1.0%	3.7%
Shares Out.	38.7	44.2	42.5	42.5	42.2	42.3	42.3	42.3	42.3	42.3
Revenue/Share	3.33	1.93	1.33	0.49	2.77	1.94	1.80	1.57	0.56	1.65
FCF/Share	(6.15)	17.92	3.65	(11.7)	3.51	(5.76)	4.52	4.44	(1.45)	(3.20)

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

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