



# Ellington Residential Mortgage REIT (EARN)

Updated June 14<sup>th</sup>, 2023 by Quinn Mohammed

## Key Metrics

<b>Current Price:</b>	\$7.20	<b>5 Year CAGR Estimate:</b>	11.3%	<b>Market Cap:</b>	\$99 M
<b>Fair Value Price:</b>	\$6.79	<b>5 Year Growth Estimate:</b>	2.0%	<b>Ex-Dividend Date:</b>	06/29/2023
<b>% Fair Value:</b>	106%	<b>5 Year Valuation Multiple Estimate:</b>	-1.2%	<b>Dividend Payment Date:</b>	07/25/2023
<b>Dividend Yield:</b>	13.3%	<b>5 Year Price Target</b>	\$7.50	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	C	<b>Rating:</b>	Hold

## Overview & Current Events

Ellington Residential Mortgage REIT acquires, invests in, and manages residential mortgage and real estate-related assets. Ellington focuses primarily on residential mortgage-backed securities, specifically those backed by a U.S. Government agency or U.S. government-sponsored enterprise. The corporation trades on the NYSE under the ticker symbol EARN. EARN is headquartered in Old Greenwich, Connecticut and is a small-cap company with a market capitalization of \$99 million. Ellington Residential Mortgage REIT is externally managed by Ellington Residential Mortgage Management LLC.

The mortgage REIT has an agency residential mortgage-backed securities (RMBS) portfolio of \$890 million and a non-agency RMBS portfolio of \$14.7 million. Agency MBS are created and backed by government agencies or enterprises, while non-agency MBS are not guaranteed by the government.

On August 4<sup>th</sup>, 2022, Ellington reduced its dividend to \$0.08 monthly, a 20% decrease compared to the \$0.10 paid monthly from October 2021 to May 2022.

On May 11<sup>th</sup>, 2023, Ellington Residential reported its first quarter results for the period ending March 31<sup>st</sup>, 2023. The company generated net income of \$2.3 million, or \$0.17 per share. Ellington achieved adjusted distributable earnings of \$2.8 million in the quarter, leading to adjusted earnings of \$0.21 per share, which does not cover the dividend paid in the period. EARN achieved a net interest margin of 1.16% in Q1. At quarter end, Ellington had \$36.7 million of cash and cash equivalents, and \$7.4 million of other unencumbered assets. The debt-to-equity ratio was 7.6X. Book value per share declined from the previous quarter to \$8.31, a 1.1% sequential decrease.

## Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
<b>Adj. EPS</b>	\$2.09	\$3.04	\$2.41	\$1.71	\$1.91	\$1.34	\$0.91	\$1.26	\$1.27	\$1.06	<b>\$0.97</b>	<b>\$1.07</b>
<b>DPS</b>	\$1.14	\$2.20	\$2.00	\$1.65	\$1.57	\$1.45	\$1.18	\$1.12	\$1.18	\$1.04	<b>\$0.96</b>	<b>\$0.96</b>
<b>Shares<sup>1</sup></b>	6.6	9.1	9.1	9.1	11.6	12.8	12.5	12.4	12.7	12.7	<b>14.0</b>	<b>15.0</b>

Ellington has seen its adjusted distributable earnings (referred to as core earnings prior to Q2 2022) per share shrink rather than grow for the most part. Since 2017, the compound annual growth rate has been -11.1%. In its first few years, the company held their share count consistent, but following 2016, the number of shares outstanding has grown, which can be another barrier to growing earnings on a per share basis. The corporation has a few avenues of growth, which all revolve around optimizing their MBS portfolio. Capitalizing on opportunities driven by market volatility and uncertainty could yield results, as well as continuing to rotate capital to non-Agency RMBS. Additionally, Ellington will protect their book value and manage volatility through interest rate hedges and liquidity management. Despite this, the company has a poor track record of earnings, leading us to anticipate minor growth of 2.0%. The dividend has been cut every single year (results from 2013 only account for half the year) in its history with an increase in 2021, followed by the dividend schedule being modified to monthly over quarterly, which some shareholders may appreciate. And in May 2022, the dividend was cut yet again, by 20%.

<sup>1</sup> 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.



# Ellington Residential Mortgage REIT (EARN)

Updated June 14<sup>th</sup>, 2023 by Quinn Mohammed

## Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	7.8	5.6	6.1	7.4	7.4	8.3	12.2	8.3	9.3	7.8	<b>7.4</b>	<b>7.0</b>
Avg. Yld.	7.0%	10.3%	14.4%	13.8%	10.9%	13.1%	11.7%	10.8%	9.4%	14.3%	<b>13.3%</b>	<b>12.8%</b>

Ellington's P/E ratio has hovered around 8.0 times core earnings since 2013. The average P/E ratio has grown slightly recently, with the 5-year average P/E of 9.2. Today, EARN trades at 7.4 times earnings, below its historical valuation. We believe the company earns a fair value of 7.0 times earnings; thus, we estimate a small valuation headwind to total annual returns. The current 13.3% yield is in excess of its historic average of 11.6%.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

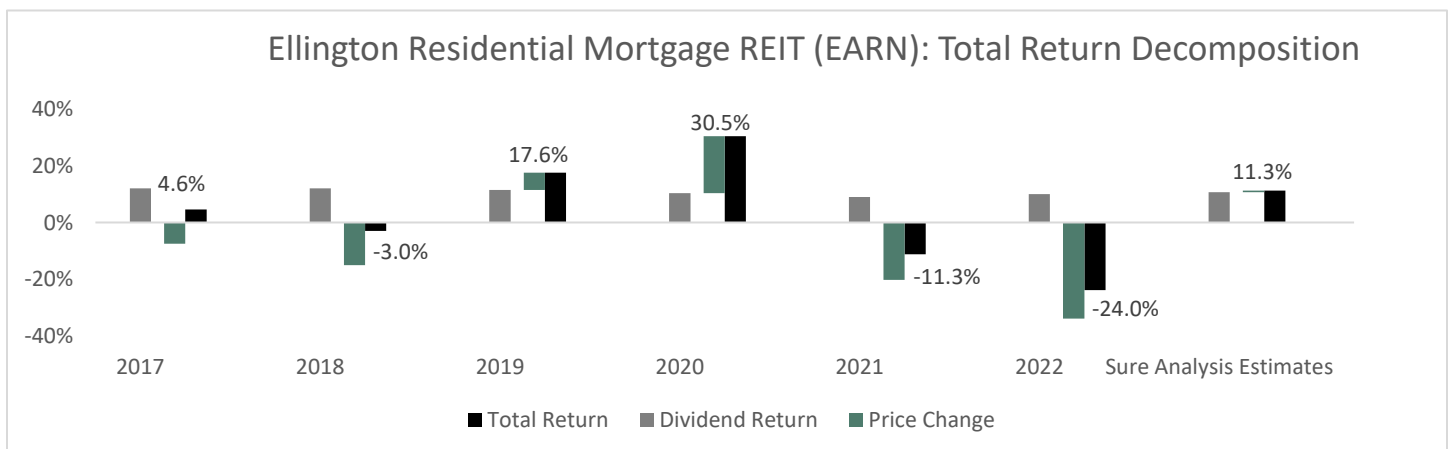
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	55%	72%	83%	96%	82%	108%	130%	89%	93%	98%	<b>99%</b>	<b>90%</b>

EARN's dividend is far from trustworthy given the corporation has a trail of cuts in the rearview. In at least four years of the last eight full calendar years in operation, the company's payout ratio was near or above 100%. Currently, even after another dividend cut, the dividend appears to be under heavy pressure. Ellington claims that their portfolio managers are among the most experienced in the MBS sector and their analytics have been developed over the company's 28-year history. The company possesses advanced proprietary models for prepayments and credit analysis. Also, roughly 25% of the company's employees are focused on research and information technology. While the company's details were not public in the 2008 real estate crash, a recession of that magnitude would most definitely affect EARN. It's focus on government-sponsored MBS provide some safety, but a prolonged recession in the future would likely affect EARN's bottom line, and result in further dividend reductions.

## Final Thoughts & Recommendation

Ellington Residential has a poor historical track record, both in core earnings per share and in the dividend. In fact, EARN slashed the dividend for six years in a row leading up to 2021 and then again in 2022. Despite these constant cuts, the yield remains very high, as share price has also cratered over the long term. Results are volatile, and thus, quite risky. We forecast annualized returns of 11.3% in the intermediate term, driven almost entirely by the stock's 13.3% yield. We also assume a 2% annual adjusted distributable earnings growth rate and a potential for a small valuation headwind. Still, Ellington Residential receives a hold rating due to its abysmal dividend history and the fact its dividend is still not on solid footing, leaving it open to even further potential dividend cuts.

## Total Return Breakdown by Year



[Click here to rate and review this research report. Your feedback is important to us.](#)

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.



# Ellington Residential Mortgage REIT (EARN)

Updated June 14<sup>th</sup>, 2023 by Quinn Mohammed

## Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	2	22	5	17	16	(6)	28	26	(1)	-25
SG&A Exp.	2	3	3	3	4	3	3	3	4	1
Net Profit	(2)	16	0	12	11	(11)	22	20	(6)	-30
Net Margin	-79.4%	73.8%	0.6%	70.4%	65.4%	195%	80.8%	77.5%	1132%	120.5%
Free Cash Flow	26	21	25	20	34	29	18	24	28	22

## Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	1,511	1,521	1,557	1,429	1,887	1,676	1,489	1,195	1,598	1054
Cash & Equivalents	50	45	40	34	56	19	35	58	69	35
Accounts Receivable	5	5	4	5	6	6	5	4	5	3
Total Liabilities	1,344	1,358	1,412	1,287	1,694	1,522	1,328	1,028	1,444	941
Accounts Payable	24	1	2	3	4	6	4	2	3	50
Shareholder's Equity	167	163	145	142	193	154	161	166	154	112

## Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	---	1.1%	0.0%	0.8%	0.7%	-0.6%	1.4%	1.5%	-0.5%	-2.3%
Return on Equity	-1.9%	9.8%	0.0%	8.3%	6.5%	-6.5%	14.1%	12.3%	-3.9%	-22.7%
ROIC	---	9.8%	0.0%	8.3%	6.5%	-6.5%	14.1%	12.3%	-3.9%	-22.7%
Shares Out.	6.6	9.1	9.1	9.1	11.6	12.8	12.5	12.4	12.7	13.16
Revenue/Share	0.37	2.40	0.57	1.85	1.42	(0.45)	2.21	2.10	-0.04	-1.90
FCF/Share	3.88	2.33	2.71	2.18	2.97	2.25	1.41	1.97	2.20	1.70

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

## Disclaimer

Nothing presented herein is, or is intended to constitute, specific investment advice. Nothing in this research report should be construed as a recommendation to follow any investment strategy or allocation. Any forward-looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. While Sure Dividend has used reasonable efforts to obtain information from reliable sources, we make no representations or warranties as to the accuracy, reliability or completeness of third-party information presented herein. No guarantee of investment performance is being provided and no inference to the contrary should be made. There is a risk of loss from an investment in marketable securities. Past performance is not a guarantee of future performance.