



Annaly Capital Management (NLY)

Updated October 28th, 2023 by Samuel Smith

Key Metrics

Current Price:	\$14.7	5 Year CAGR Estimate:	18.5%	Market Cap:	\$7.3B
Fair Value Price:	\$20	5 Year Growth Estimate:	0.9%	Ex-Dividend Date:	12/28/23 ¹
% Fair Value:	73%	5 Year Valuation Multiple Estimate:	6.4%	Dividend Payment Date:	1/31/23 ²
Dividend Yield:	17.7%	5 Year Price Target	\$21	Years of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

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.

On October 25, 2023, Annaly Capital Management, Inc. (NLY) released its financial results for the third quarter of 2023. The report highlighted a GAAP net loss of (\$1.21) per average common share for the quarter. Additionally, earnings available for distribution ("EAD") were reported at \$0.66 per average common share for the same period. The quarter was marked by a sharp rise in interest rates, driven partially by strong economic data and changing perceptions around U.S. government debt. This resulted in a negative 8.8% economic return for the quarter and a reported leverage of 6.4x. In terms of portfolio activity, NLY maintained the notional value of its Agency holdings, continued to favor specified pools over TBAs to improve the convexity profile, and expanded its Agency CMBS portfolio by approximately \$500 million. The company also adjusted its hedging strategy in anticipation of the end of the hiking cycle, shifting a significant portion of their hedge duration to the 7- to 20-year part of the curve. The broader economic conditions, coupled with the firm's portfolio activity and market positioning, played a crucial role in NLY's financial performance for the quarter. The earnings call and the report provided insights into the company's strategic adjustments amid evolving market conditions and outlined its financial standing as of the third quarter of 2023.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	\$15.76	-\$3.56	\$1.96	\$5.92	\$5.88	\$0.16	\$4.76	\$4.40	\$4.64	\$4.23	\$2.86	\$2.99
DPS	\$6.00	\$4.80	\$4.80	\$4.80	\$4.80	\$4.80	\$4.00	\$3.64	\$3.52	\$3.52	\$2.60	\$2.72
Shares³	236.9	236.9	231.2	254.7	289.9	350.0	357.6	349.6	365.1	493.6	494.8	475.0

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 rising interest rates, Annaly saw a narrowing between interest income and expenses, as well requiring greater amounts of leverage to produce declining results.

Moving forward, further increases in interest rates could reduce refinancing activity. As long as the real estate market remains on sound footing, Annaly should continue to grow gradually and support its hefty dividend. However, any meaningful pullback could significantly hurt the business and force it to cut its dividend again.

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	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2027
Avg. P/E	2.5	NA	19	6.7	8	NA	8	6.9	7.7	4.5	5.1	7.0
Avg. Yld.	15.0%	10.7%	12.8%	12.0%	10.1%	13.6%	10.5%	11.9%	10.2%	18.5%	17.7%	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 undervalued at present based on expected 2023 results.

Safety, Quality, Competitive Advantage, & Recession Resiliency

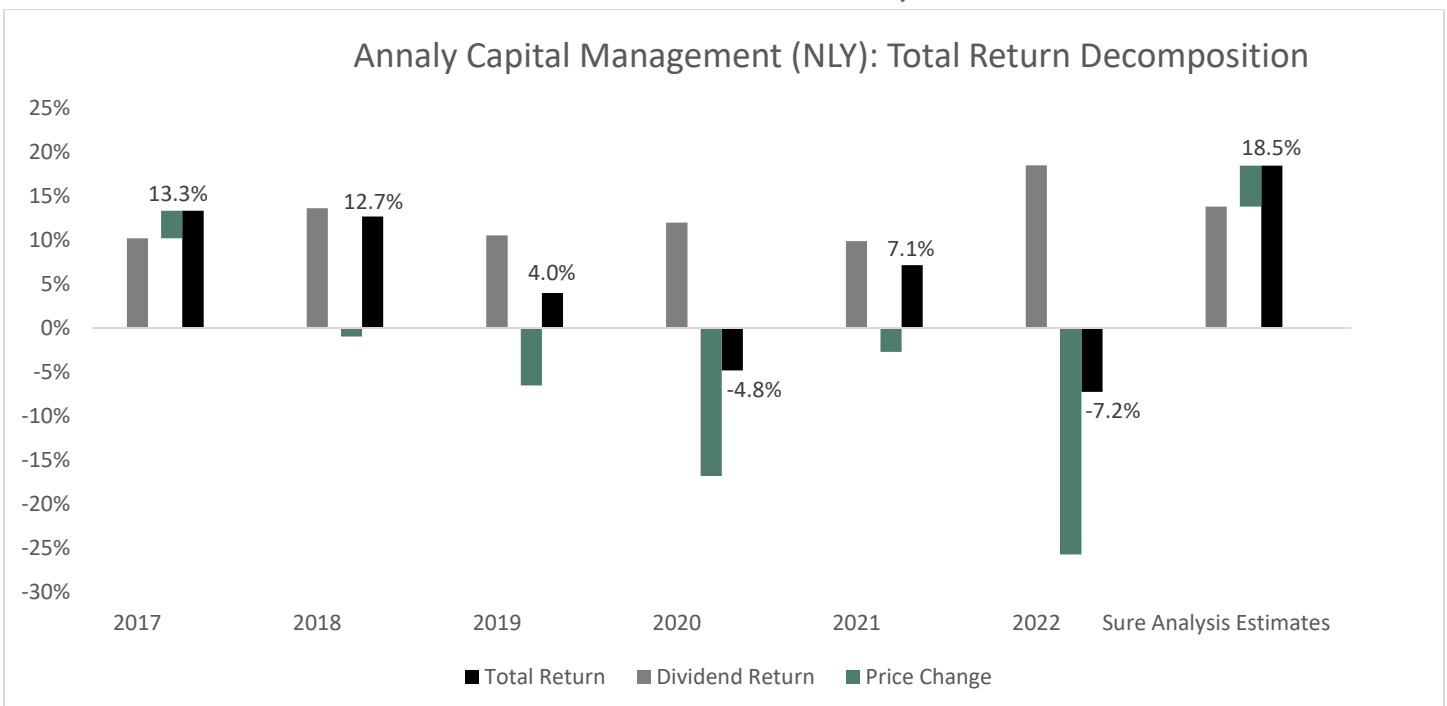
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	38.1%	NA	NA	81.1%	81.6%	NA	84.0%	82.7%	75.9%	83.2%	90.9%	91.0%

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 are concerned 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 an annualized total return outlook of 18.5% and a mouthwatering 17.7% dividend yield compensating for considerable uncertainty in its business model, we rate the stock a speculative Buy given the inherent risk involved in mREITs alongside the strong total return potential.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	3,997	(615)	734	1,565	1,684	275	(1,992)	(585)	2,662	1,954
SG&A Exp.	232	209	200	250	224	330	272	222	186	163
D&A Exp.	3	5	20	42	28	72	32	41	25	21
Net Profit	3,730	(842)	467	1,434	1,570	54	(2,163)	(891)	2,390	1,725
Net Margin	93.3%	136.9%	63.5%	91.6%	93.2%	19.8%	108.6%	152.4%	89.8%	88.3%
Free Cash Flow	-12,893	6,128	(3,643)	1,407	1,621	2,622	(1,200)	528	2,539	4,358
Income Tax	8	5	(2)	(2)	7	(2)	(11)	(28)	5	46

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets (\$B)	82	88	75	88	102	106	130	88	77	82
Cash & Equivalents	552	1,741	1,769	1,540	707	1,736	1,851	1,244	1,342	1,577
Acc. Receivable	273	278	231	270	325	426	455	284	238	1,212
Goodwill & Int.	95	133	110	758	676	659	471	228	638	1,765
Total Liabilities (\$B)	70	75	63	75	87	92	114	74	64	70
Accounts Payable	186	228	205	347	910	1,154	940	1,075	239	1,483
Long-Term Debt	859	1,266	4,734	7,865	7,119	8,041	10,564	7,036	7,108	8,795
Total Equity	11,492	12,415	10,983	11,368	13,145	12,334	13,810	12,472	11,633	9,734
LTD/E Ratio	0.07	0.10	0.40	0.63	0.48	0.57	0.67	0.50	0.54	0.78

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	1.4%	3.5%	-1.0%	0.6%	1.8%	1.7%	0.1%	-1.8%	-0.8%	2.2%
Return on Equity	11.3%	28.1%	-7.0%	4.0%	12.8%	12.8%	0.4%	-16.5%	-6.8%	16.1%
ROIC	10.5%	24.9%	-6.0%	3.0%	7.7%	7.4%	0.2%	-8.9%	-3.8%	8.5%
Shares Out.	236.9	236.9	231.2	254.7	289.9	350.0	357.6	349.6	364.9	468.3
Revenue/Share	16.06	(2.60)	3.10	6.45	6.32	0.91	(5.55)	(1.65)	7.46	4.75
FCF/Share	(51.80)	25.87	(15.38)	5.80	6.08	8.67	(3.34)	1.49	7.11	2.2%

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

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