



# SLR Investment Corp. (SLRC)

Updated November 12<sup>th</sup>, 2023 by Nikolaos Sismanis

## Key Metrics

|                             |         |  |         |                                  |           |
|-----------------------------|---------|--|---------|----------------------------------|-----------|
| <b>Current Price:</b>       | \$14.76 | <b>5 Year CAGR Estimate:</b>               | 7.6%    | <b>Market Cap:</b>               | \$805.2 M |
| <b>Fair Value Price:</b>    | \$15.21 | <b>5 Year Growth Estimate:</b>             | -2.2%   | <b>Ex-Dividend Date:</b>         | 12/13/23  |
| <b>% Fair Value:</b>        | 97%     | <b>5 Year Valuation Multiple Estimate:</b> | 0.6%    | <b>Dividend Payment Date:</b>    | 12/28/23  |
| <b>Dividend Yield:</b>      | 11.1%   | <b>5 Year Price Target</b>                 | \$13.61 | <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

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.

As of September 30<sup>th</sup>, 2023, SLR Investment’s portfolio consisted of 154 companies with exposures of 37.1% in senior secured loans, 25.2% in asset-based senior secured loans, 22.6% in equipment senior secured financings, and 15.1% in life science senior secured loans. SLR Investment Corp. generates around \$180 million in total investment income annually and is based in New York, New York.

On November 7<sup>th</sup>, 2023, SLR Investment Corp. reported its Q3 results for the period ending September 30<sup>th</sup>, 2023. For the quarter, total investment income totaled \$59.6 million, about 25% higher year-over-year. The increase was primarily due to a larger portfolio as well as an increase in rates. Expenses totaled \$36.3 million, 32% higher compared to last year. The stronger increase in expenses was primarily due to higher management fees, incentive fees, and interest expense on a larger portfolio. Additionally, the increase was due to notably higher interest expenses on borrowings.

Still, on a per-share basis, net investment income grew by six cents to \$0.42, or up about 16% year-over-year. We now forecast NII/share of \$1.69 for fiscal 2023. The company also switched from a monthly dividend to a quarterly dividend. The annualized dividend rate remained unchanged at \$1.64.

## Growth on a Per-Share Basis

| Year                      | 2013    | 2014    | 2015    | 2016    | 2017    | 2018    | 2019    | 2020    | 2021    | 2022    | 2023           | 2028           |
|---------------------------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|----------------|----------------|
| <b>NAV/shr</b>            | \$22.50 | \$22.05 | \$20.79 | \$21.74 | \$21.81 | \$21.75 | \$21.44 | \$20.16 | \$19.93 | \$18.33 | <b>\$18.06</b> | <b>\$16.16</b> |
| <b>NII/shr</b>            | \$1.91  | \$1.56  | \$1.52  | \$1.68  | \$1.62  | \$1.77  | \$1.71  | \$1.40  | \$1.43  | \$1.48  | <b>\$1.69</b>  | <b>\$1.51</b>  |
| <b>DPS</b>                | \$2.00  | \$1.60  | \$1.60  | \$1.60  | \$1.60  | \$1.64  | \$1.64  | \$1.64  | \$1.64  | \$1.64  | <b>\$1.64</b>  | <b>\$1.47</b>  |
| <b>Shares<sup>1</sup></b> | 44.2    | 42.5    | 42.5    | 42.2    | 42.3    | 42.3    | 42.3    | 42.3    | 42.3    | 52.4    | <b>54.6</b>    | <b>80.0</b>    |

With nearly 65.7% 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. Furthermore, historical patterns reveal that distributions have consistently surpassed the underlying NII generation, leading to a decline in the company’s NAV/share over recent years. Although the current rise in interest rates has resulted in a growing NII/share, covering the dividend, we maintain a cautious outlook. Our NAV/share, NII/share, and DPS CAGR estimates remain at a negative 2.2% each over the medium term, accounting for the potential resurgence of the NAV deterioration trend in later years.

<sup>1</sup> 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       | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020  | 2021  | 2022  | Now   | 2028  |
|------------|------|------|------|------|------|------|------|-------|-------|-------|-------|-------|
| Avg. P/NII | 12   | 13.1 | 11.5 | 11.9 | 13.1 | 11.9 | 12.0 | 11.4  | 10.6  | 10.3  | 8.7   | 9.0   |
| Avg. P/NAV | 1.02 | 0.93 | 0.84 | 0.92 | 0.97 | 0.97 | 0.96 | 0.79  | 0.94  | 0.83  | 0.82  | N/A   |
| Avg. Yld.  | 8.7% | 7.8% | 9.2% | 8.0% | 7.5% | 7.8% | 8.0% | 10.3% | 10.9% | 10.8% | 11.1% | 10.8% |

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 an 18% discount to NAV. Thus, the yield has climbed to notable levels as investors demand a higher return for the underlying risks attached. At its current price levels, we believe the stock is more or less fairly valued. On May 9<sup>th</sup>, 2023, the BoD approved a \$50 million share buyback program to address the NAV discount. Still, no buybacks have occurred this year, while only \$3 million worth of stock was repurchased last year through a similar program.

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

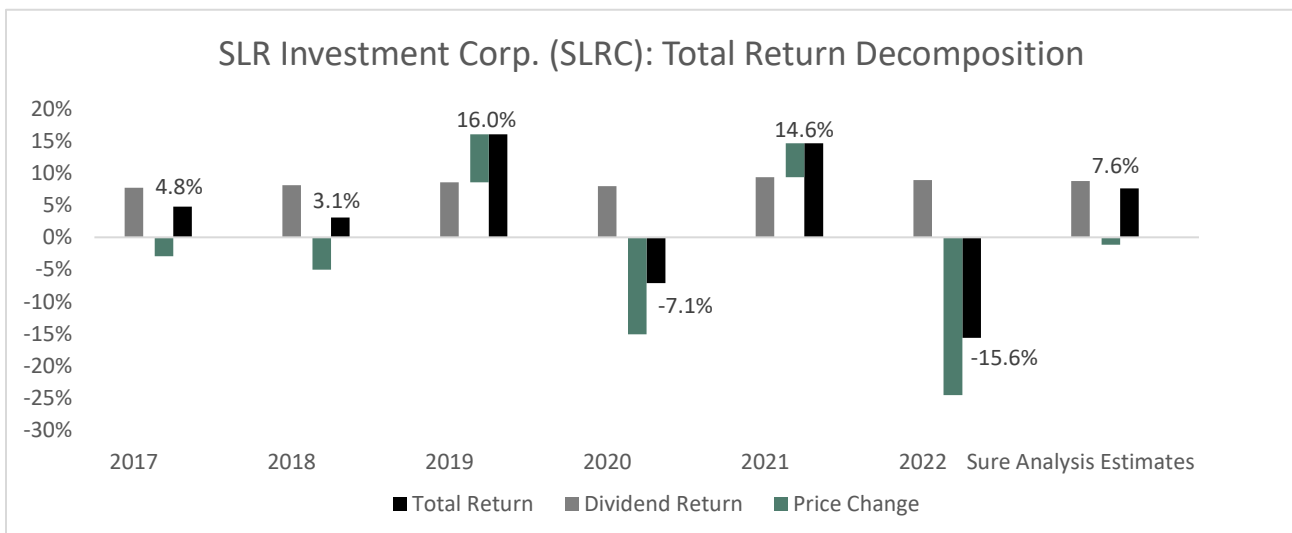
| Year   | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2028 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 105% | 103% | 105% | 95%  | 99%  | 93%  | 96%  | 117% | 116% | ---  | 97%  | 97%  |

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 estimate annualized returns of 7.6% over the medium-term, as soft valuation tailwinds and dividend returns from the high yield could be offset by declines in NII and DPS. 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                  | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  | 2022  |
|-----------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Revenue</b>        | 86    | 57    | 21    | 117   | 82    | 76    | 66    | 24    | 70    | 28    |
| <b>SG&amp;A Exp.</b>  | 10    | 9     | 8     | 10    | 9     | 9     | 8     | 8     | 10    | 12    |
| <b>Net Profit</b>     | 75    | 48    | 14    | 107   | 70    | 67    | 56    | 15    | 60    | 18    |
| <b>Net Margin</b>     | 87.7% | 84.7% | 68.2% | 91.2% | 85.8% | 87.7% | 84.4% | 65.5% | 85.7% | 64.3% |
| <b>Free Cash Flow</b> | 799   | 157   | (498) | 148   | (243) | 191   | 188   | (61)  | (135) | 91    |

## Balance Sheet Metrics

| Year                          | 2013  | 2014  | 2015  | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  | 2022  |
|-------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <b>Total Assets</b>           | 1,708 | 1,686 | 1,617 | 1,651 | 1,642 | 1,683 | 1,950 | 1,936 | 2,011 | 2,538 |
| <b>Cash &amp; Equivalents</b> | 585   | 635   | 278   | 312   | 151   | 207   | 436   | 389   | 323   | 428   |
| <b>Total Liabilities</b>      | 713   | 750   | 735   | 732   | 720   | 764   | 1,044 | 1,084 | 1,169 | 1,538 |
| <b>Accounts Payable</b>       | 474   | 511   | 19    | 329   | 165   | 273   | 441   | 401   | 342   | 433   |
| <b>Long-Term Debt</b>         | 225   | 225   | 430   | 387   | 539   | 474   | 587   | 671   | 812   | 1,086 |
| <b>Shareholder's Equity</b>   | 996   | 937   | 883   | 919   | 922   | 919   | 906   | 852   | 842   | 1000  |
| <b>LTD/E Ratio</b>            | 0.23  | 0.24  | 0.49  | 0.42  | 0.59  | 0.52  | 0.65  | 0.79  | 0.96  | 1.09  |

## Profitability & Per Share Metrics

| Year                    | 2013  | 2014 | 2015   | 2016  | 2017   | 2018 | 2019 | 2020   | 2021   | 2022 |
|-------------------------|-------|------|--------|-------|--------|------|------|--------|--------|------|
| <b>Return on Assets</b> | 4.8%  | 2.9% | 0.9%   | 6.5%  | 4.3%   | 4.0% | 3.1% | 0.8%   | 3.0%   | 0.8% |
| <b>Return on Equity</b> | 8.0%  | 5.0% | 1.5%   | 11.9% | 7.7%   | 7.3% | 6.1% | 1.8%   | 7.0%   | 2.0% |
| <b>ROIC</b>             | 5.8%  | 4.1% | 1.1%   | 8.2%  | 5.1%   | 4.7% | 3.9% | 1.0%   | 3.7%   | 1.0% |
| <b>Shares Out.</b>      | 44.2  | 42.5 | 42.5   | 42.2  | 42.3   | 42.3 | 42.3 | 42.3   | 42.3   | 51.7 |
| <b>Revenue/Share</b>    | 1.93  | 1.33 | 0.49   | 2.77  | 1.94   | 1.80 | 1.57 | 0.56   | 1.65   | 0.55 |
| <b>FCF/Share</b>        | 17.92 | 3.65 | (11.7) | 3.51  | (5.76) | 4.52 | 4.44 | (1.45) | (3.20) | 1.76 |

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

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