



Annaly Capital Management (NLY)

Updated November 8th, 2024 by Samuel Smith

Key Metrics

| | | | | | |
|-----------------------------|--------|--|-------|----------------------------------|-----------------------|
| Current Price: | \$19.8 | 5 Year CAGR Estimate: | 11.4% | Market Cap: | \$11 B |
| Fair Value Price: | \$20.0 | 5 Year Growth Estimate: | 0.9% | Ex-Dividend Date: | 12/28/24 ¹ |
| % Fair Value: | 100% | 5 Year Valuation Multiple Estimate: | 0.0% | Dividend Payment Date: | 1/31/25 ² |
| Dividend Yield: | 13.0% | 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.

Annaly Capital Management (NYSE: NLY) reported its third-quarter 2024 financial results on October 23, 2024, revealing an EPS for distribution of \$0.66, slightly below the consensus estimate of \$0.67 and unchanged from the same quarter last year. The book value per common share rose to \$19.54 from \$19.25 in Q2 but fell just short of the expected \$19.57. Notably, the economic return surged to 4.9% from 0.9% in the prior quarter, while economic leverage slightly decreased to 5.7x.

Total assets expanded to \$101.5 billion, up from \$93.7 billion in Q2, driven by a robust portfolio of \$81.8 billion, which includes a highly liquid agency portfolio of \$7.25 billion, marking a \$6.4 billion increase quarter-over-quarter. Despite a decline in net interest income to \$13.4 million from \$53.6 million in Q2, Annaly improved its net interest spread to 1.32%, up from 1.24% in the previous quarter and 1.18% a year ago. Net servicing income also increased to \$109.6 million, reflecting the company's effective management of its servicing operations.

CEO David Finkelstein highlighted the benefits of the Federal Reserve's rate-cutting cycle, which enhanced Agency MBS performance and allowed the deployment of \$1.2 billion in accretive common equity into high-quality, up-in-coupon specified pools and TBA securities. Annaly's stock saw a modest increase of 0.3% in after-hours trading, reflecting investor confidence despite missing EPS expectations. The company continues to focus on optimizing its portfolio and capital structure to drive future growth and returns for its shareholders.

Growth on a Per-Share Basis

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|---------------------------|---------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| EPS | -\$3.56 | \$1.96 | \$5.92 | \$5.88 | \$0.16 | \$4.76 | \$4.40 | \$4.64 | \$4.23 | \$2.86 | \$2.86 | \$2.99 |
| DPS | \$4.80 | \$4.80 | \$4.80 | \$4.80 | \$4.80 | \$4.00 | \$3.64 | \$3.52 | \$3.52 | \$2.60 | \$2.60 | \$2.72 |
| Shares³ | 236.9 | 231.2 | 254.7 | 289.9 | 350.0 | 357.6 | 349.6 | 365.1 | 493.6 | 500.1 | 560.5 | 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.

¹ Estimated date

² Estimated date

³ In millions

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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.

Valuation Analysis

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | Now | 2029 |
|-----------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Avg. P/E | NA | 19 | 6.7 | NA | 8 | 8 | 6.9 | 7.7 | 4.5 | 5.1 | 6.9 | 7.0 |
| Avg. Yld. | 10.7% | 12.8% | 12.0% | 10.1% | 13.6% | 10.5% | 11.9% | 10.2% | 18.5% | 17.7% | 13.1% | 13.0% |

The cyclical nature of this trust's earnings makes them difficult to value based on challenging years in the past. 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 fairly valued at present based on expected 2024 results.

Safety, Quality, Competitive Advantage, & Recession Resiliency

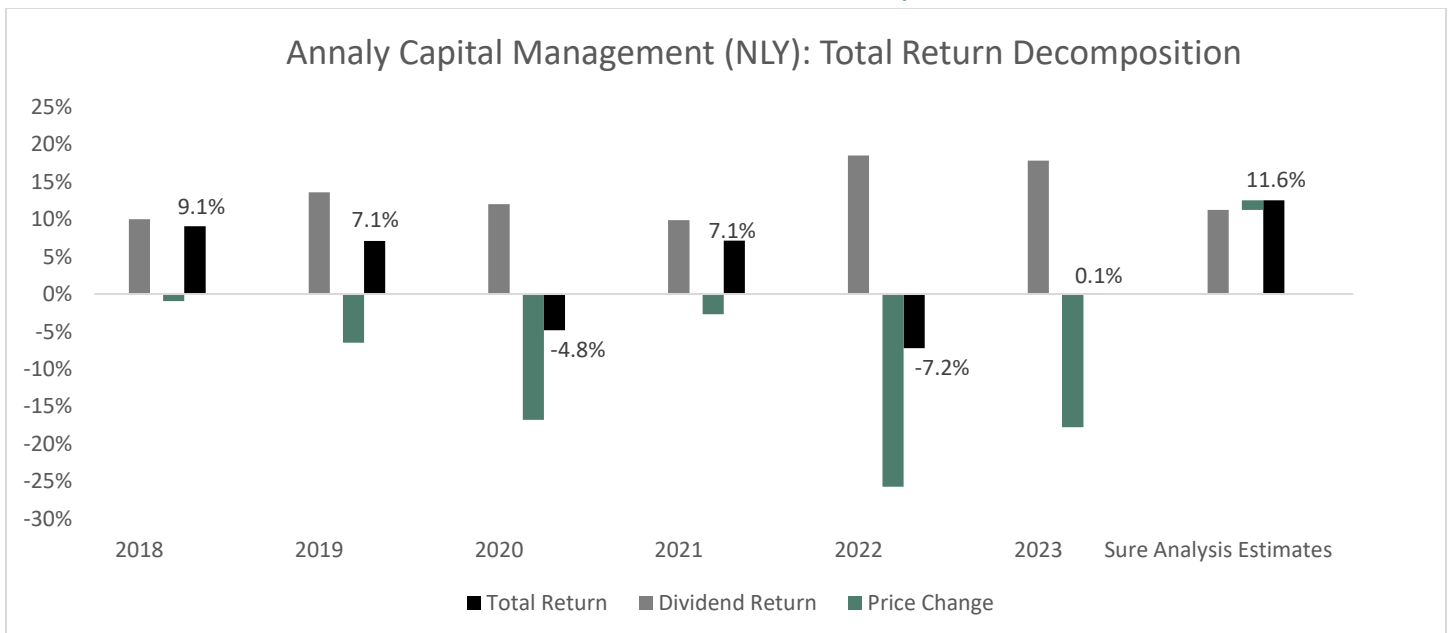
| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|--------|------|------|-------|-------|------|-------|-------|-------|-------|-------|-------|-------|
| Payout | NA | NA | 81.1% | 81.6% | NA | 84.0% | 82.7% | 75.9% | 83.2% | 90.9% | 90.9% | 91.0% |

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 leveraged 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 11.6% and a mouthwatering 13.1% 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 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|----------------|--------|---------|-------|-------|-------|---------|--------|-------|-------|---------|
| Revenue | (615) | 734 | 1,565 | 1,684 | 275 | (1,992) | (548) | 2,720 | 1,954 | (1,437) |
| SG&A Exp. | 209 | 200 | 250 | 224 | 330 | 272 | 222 | 186 | 163 | 163 |
| D&A Exp. | 5 | 20 | 42 | 28 | 72 | 32 | 41 | 25 | 21 | 25 |
| Net Profit | (842) | 467 | 1,434 | 1,570 | 54 | (2,163) | (891) | 2,390 | 1,725 | (1,643) |
| Net Margin | 136.9% | 63.5% | 91.6% | 93.2% | 19.8% | 108.6% | 162.5% | 87.8% | 88.3% | 114.4% |
| Free Cash Flow | 6,128 | (3,643) | 1,407 | 1,621 | 2,622 | (1,200) | 528 | 2,539 | 4,358 | 1,970 |
| Income Tax | 5 | (2) | (2) | 7 | (2) | (11) | (28) | 5 | 46 | 39 |

Balance Sheet Metrics

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|-------------------------|--------|--------|--------|--------|--------|--------|--------|--------|-------|--------|
| Total Assets (\$B) | 88.36 | 75.19 | 87.91 | 101.76 | 105.79 | 130.30 | 88.46 | 76.76 | 81.85 | 93.23 |
| Cash & Equivalents | 1,741 | 1,769 | 1,540 | 707 | 1,736 | 1,851 | 1,244 | 1,342 | 153 | 276 |
| Acc. Receivable | 278 | 231 | 270 | 325 | 426 | 455 | 284 | 238 | 1,212 | 3,933 |
| Goodwill & Int. | 133 | 110 | 758 | 676 | 659 | 471 | 228 | 638 | 1,080 | 353 |
| Total Liabilities (\$B) | 75.02 | 63.28 | 75.33 | 86.89 | 91.67 | 114.50 | 74.43 | 63.57 | 70.48 | 81.88 |
| Accounts Payable | 228 | 205 | 347 | 910 | 1,154 | 940 | 1,075 | 239 | 1,483 | 3,537 |
| Long-Term Debt | 1,266 | 4,734 | 7,865 | 7,119 | 8,041 | 10,564 | 7,036 | 7,108 | 8,795 | 13,204 |
| Total Equity | 12,415 | 10,983 | 11,368 | 13,145 | 12,334 | 13,810 | 12,472 | 11,633 | 9,734 | 9,719 |
| LTD/E Ratio | 0.10 | 0.40 | 0.63 | 0.48 | 0.57 | 0.67 | 0.50 | 0.54 | 0.78 | 1.17 |

Profitability & Per Share Metrics

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|------------------|--------|---------|-------|-------|-------|--------|--------|-------|-------|--------|
| Return on Assets | -1.0% | 0.6% | 1.8% | 1.7% | 0.1% | -1.8% | -0.8% | 2.9% | 2.2% | -1.9% |
| Return on Equity | -6.5% | 3.7% | 11.7% | 11.4% | 0.4% | -14.5% | -6.0% | 17.6% | 14.0% | -14.5% |
| ROIC | -6.0% | 3.0% | 7.7% | 7.4% | 0.2% | -8.9% | -3.8% | 11.6% | 8.5% | -7.3% |
| Shares Out. | 236.9 | 231.2 | 254.7 | 289.9 | 350.0 | 357.6 | 349.6 | 365.1 | 493.6 | 500.1 |
| Revenue/Share | (2.60) | 3.10 | 6.45 | 6.32 | 0.91 | (5.55) | (1.55) | 7.62 | 4.75 | (2.91) |
| FCF/Share | 25.87 | (15.38) | 5.80 | 6.08 | 8.67 | (3.34) | 1.49 | 7.11 | 10.59 | 3.98 |

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

Disclaimer

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