



New Mountain Finance Corp. (NMFC)

Updated November 20th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	\$11.49	5 Year CAGR Estimate:	10.0%	Market Cap:	\$1.24 B
Fair Value Price:	\$12.07	5 Year Growth Estimate:	0.0%	Ex-Dividend Date:	12/17/2024
% Fair Value:	95%	5 Year Valuation Multiple Estimate:	1.0%	Dividend Payment Date:	12/31/2024
Dividend Yield:	11.1%	5 Year Price Target	\$12.07	Years Of Dividend Growth:	2
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

New Mountain Finance Corp. is a BDC (Business Development Company) specializing in financing quality, middle-stage businesses that display “defensive growth” characteristics. Its businesses typically generate anywhere from \$10 to \$200 million of EBITDA, to which NMFC provides senior secured debt, including 1st lien, 2nd lien, and uni-tranche loans. Its portfolio consists of 128 individual investments, the top 10 of which represent around \$826.5 billion or 25.2% of its investments at fair value. In terms of its key industry exposures, around 32% of its investments operate in the enterprise software industry, 22% in business services, and another notable 19% of its capital is allocated to healthcare. For management to align its interest with shareholders, around 12% of the company’s shares are owned by its employees, showcasing strong insider confidence. New Mountain Finance generated nearly \$295 million of gross investment income last year and is based in New York, New York.

On October 30th, 2024, the company reported its Q3 results for the period ending September 30th, 2024. During the quarter, the company generated net investment income per share of \$0.34, compared to \$0.40 last year.

Overall, operations remained very stable, and management reiterated that the company is well-positioned to continue finding opportunities in “defensive growth” industries. Management also mentioned they remain confident that NMFC remains well-positioned to continue to deliver a strong and stable dividend moving forward. In line with the introduction of a supplemental dividend program four quarters ago, a supplemental dividend of \$0.01 will be paid along with the regular payout in September. NAV/share was \$12.62, down from \$12.74 sequentially. We still forecast FY2024 IIS/share of \$1.42. We have used an annualized base dividend of \$1.28 in our estimates. However, DPS this year should be at least \$1.37 based (\$1.28 base dividend plus one \$0.04, two \$0.02, and one \$0.01 supplemental dividends).

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
IIS¹	\$0.88	\$0.55	\$1.72	\$1.47	\$0.95	\$1.32	\$0.60	\$2.08	\$0.75	\$1.34	\$1.42	\$1.42
DPS	\$1.48	\$1.36	\$1.36	\$1.36	\$1.36	\$1.36	\$1.24	\$1.20	\$1.22	\$1.49	\$1.28	\$1.28
Shares²	52	60	65	74	76	85	97	97	97	101	108	130

BDCs tend to specialize and allocate capital in the niche industry they have the most expertise. New Mountain Finance focuses on ‘defensive growth’ industries, allocating capital to companies that they understand well and can produce relatively resilient cash flows. With rates hovering near 0% until recent years, financing had become cheaper than ever. This was especially the case with defensive industries in which NMFC specializes, as they can attract low-cost capital, gradually lowering NMFC’s investment spreads. For context, the company’s portfolio used to yield 10.3% back in Q3 2018. This figure was slowly, but gradually falling, bottoming at 8.8% in Q1 2022. Consequently, the company generated declining returns over time, resulting in small dividend cuts over the years. Rates are now higher, resulting in NMFC’s portfolio yield hovering at 11.9% in Q3 2024. We expect no growth in IIS or the dividend moving forward, as they are already starting off a high base which could sway either way in the medium-term amid future macro developments.

¹ Investment Income per Share

² 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.



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Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/IIS	16.45	26.3	8.2	9.21	14.2	10.3	15.0	6.5	16.1	8.5	8.1	8.5
Avg. Yld.	10.0%	9.4%	11.8%	9.3%	10.3%	10.0%	10.0%	8.8%	10.0%	13.0%	11.1%	10.6%

Following New Mountain's latest dividend hike (Nov. 22, 2022), the stock now trades with a yield of about 11.1%. That's modestly higher compared to its industry peers these days. We have set our fair P/IIS at 8.5X, which implies that shares are slightly undervalued. On top of the hefty base yield, NMFC is showing confidence by also paying supplemental dividends. Also, the fact its investments focus on defensive-growth industries should attract investor interest in the stock. Shares trade below their NAV, which, in our view, raises NMFC's margin of safety.

Safety, Quality, Competitive Advantage, & Recession Resiliency

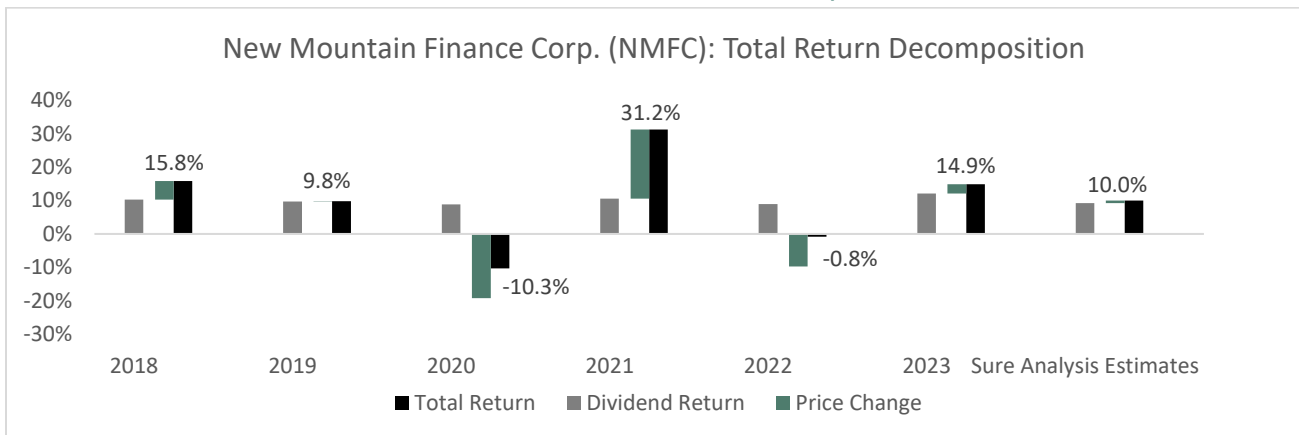
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	168%	247%	79%	93%	143%	103%	207%	58%	163%	111%	90%	90%

New Mountain's payout ratio has become a bit more uncomfortable compared to the company's earlier years, primarily due to poorer available credit opportunities. However, considering that its portfolio is well-diversified, with its more heavily weighted sectors (software and healthcare) performing well during the pandemic, we expect its medium-term results to remain relatively stable. This was adequately displayed during FY2020, during which the company produced a slightly increased net investment income. The most substantial risk we can identify is NMFC's sky-high cost of equity, similar to its peers. New Mountain has been issuing stock to fund its investments. While its investment yield has now recovered substantially following rising interest rates, NMFC's cost of equity remains very high. Thus, management is likely to favor additional debt issuance compared to shares. This could increase the company's leverage over time, incurring additional credit risks. NMFC's leverage currently stands at 1.23 – a healthy number, nonetheless.

Final Thoughts & Recommendation

Despite New Mountain's business model being hurt by low rates in the past, which led to dividend cuts, the company has generated consistently positive returns for its shareholders. With rates now on the rise, investment income per share has already moved notably higher. While some fundamental risks regarding NMFC's investment yields persist, we like the company's diversified portfolio and favorable sector exposure. Additionally, we believe that management's substantial skin in the game increases investors' safety margins, aligning both parties' interests. We forecast annualized returns of 10.0% in the medium-term. This forecast doesn't include the potential for further returns driven by New Mountain's supplemental dividends. Shares earn a buy rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	71.24	35.68	113.0	109.97	75.81	109.12	56.90	203.7	89.1	144
SG&A Exp.	5.00	7.33	7.36	8.07	10.04	8.91	9.79	9.58	9.9	9.9
Net Profit	45.58	32.96	111.68	109.40	72.35	112.56	58.47	201.4	74.7	135
Net Margin	64.0%	92.4%	98.8%	99.5%	95.4%	103.2%	102.7%	98.9%	83.9%	93.8%
Free Cash Flow	-289.6	-63.3	60.5	-166.3	-393.5	-718.5	301.1	-22.1	35	333
Income Tax	0.93	1.34	-0.49	0.42	0.40	0.00	-0.99	0.23	9.3	1.8

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	1514.9	1588.1	1656.0	1928.0	2448.7	3266.1	3098	3296	3355	3159
Cash & Equivalents	23.45	30.10	45.93	34.94	49.66	48.57	78.97	58.08	71.2	70
Total Liabilities	712.7	751.2	717.5	893.0	1442.4	1982.6	1861	1953	2029	1827
Accounts Payable	27.81	7.78	5.91	5.11	32.54	18.26	42.43	25.30	19.63	20.44
Long-Term Debt	670.6	728.1	696.7	869.5	1384.1	1942.3	1798	1907	1981	1785
Total Equity	802.2	836.9	938.6	1035.0	1006.3	1283.5	1222	1321	1314	1320
LTD/E Ratio	0.84	0.87	0.74	0.84	1.38	1.51	1.47	1.44	1.51	1.35

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	4.2%	2.1%	6.9%	6.1%	3.3%	3.9%	1.8%	6.3%	2.3%	4.2%
Return on Equity	6.3%	4.0%	12.6%	11.1%	7.1%	9.8%	4.7%	15.8%	5.7%	10.2%
ROIC	4.3%	2.2%	7.0%	6.2%	3.4%	4.0%	1.9%	6.4%	2.3%	4.2%
Shares Out.	56.16	66.97	72.86	84.00	88.63	100.46	110.08	110.21	115.43	123.49
Revenue/Share	1.27	0.53	1.55	1.31	0.86	1.09	0.52	1.85	0.77	1.16
FCF/Share	-5.16	-0.95	0.83	-1.98	-4.44	-7.15	2.74	-0.20	0.30	2.69

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

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