

Palmer Square Capital BDC

Good inaugural quarter

Maintain Rating: NEUTRAL | PO: 16.50 USD | Price: 16.26 USD

Beat the Street; risk/reward balanced

Palmer Square (PSBD) reported Q4 core EPS \$0.57, modestly above the BofA forecast of \$0.55. The variance was largely due to a stronger than expected recurring interest income. GAAP EPS was \$0.81 (impressive 19.3% GAAP ROE) due to portfolio appreciation. Overall, fundamentals were positive as the portfolio yield increased, credit remains pristine, and NAV/share increased 1.7%. We think PSBD's unique strategy of investing in a diversified portfolio of liquid, non-investment grade senior secured loans to large corporate issuers paired with certain opportunistic investments can generate attractive risk adjusted returns due to asset selection, low fees, moderate leverage & attractive funding costs. That said, we think risk/reward is balanced at current valuation.

NAV/share +1.7% to \$17.04; leverage stable at 1.4x

NAV/share was \$17.04 vs. \$16.76 the prior quarter. The increase was due to core earnings exceeding the dividend (+0.03/share) and portfolio appreciation (+\$0.25/share). NAV/share as of January was \$17.17. Importantly, there could be additional upside to NAV/share as credit spreads continue to tighten. Reported leverage, net was 1.39x, largely unchanged QoQ. PSBD's target leverage is ~1.5x. Available liquidity was solid at \$262M. There are no debt maturities in 2024 and we believe 2025 debt maturities (2 revolving credit facilities) will be extended during 1H24. Additionally, PSBD is exploring alternative funding options, including a potential collateralized loan issuance (CLO).

Portfolio stable at \$1.1B; to scale to \$1.4B in 2024

The portfolio (fair value) was unchanged at \$1.1B. Originations of \$85M and exits/sales of \$53M resulted in net portfolio commitments of \$33M. Overall, portfolio composition was conservative (92% first lien senior secured & ST investments) and focused on recurring revenue businesses (underweight cyclicals). Additionally, borrower concentration is low (top 10 investments are 10.4% vs. 20-30% for many top performing peers), which should benefit credit over time. We expect the portfolio to scale to ~\$1.4B in 2024 as PSBD deploys the proceeds from its IPO in January 2024. There have been no non-accrual investments since inception.

Earnings outlook unchanged; Maintaining \$16.50 PO

Maintaining our 24/25E core EPS forecast of \$1.88/\$1.72. Introducing our 26E core EPS forecast of \$1.65. Maintaining our PO of \$16.50. Maintain Neutral.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	1.78	2.25	1.88	1.72	1.65
GAAP EPS	(3.22)	4.19	1.88	1.72	1.65
EPS Change (YoY)	21.1%	26.4%	-16.4%	-8.5%	-4.1%
Consensus EPS (Bloomberg)			1.93	1.79	NA
DPS	1.89	2.16	1.70	1.69	1.63
Valuation (Dec)					
P/E	9.1x	7.2x	8.6x	9.5x	9.9x
GAAP P/E	NM	3.9x	8.6x	9.5x	9.9x
Dividend Yield	11.6%	13.3%	10.5%	10.4%	10.0%

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Equity

Key Changes

(US\$)	Previous	Current
2024E DPS	1.73	1.70

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Stock Data

Price	16.26 USD
Price Objective	16.50 USD
Date Established	12-Feb-2024
Investment Opinion	C-2-8
52-Week Range	15.57 USD -17.12 USD
Mrkt Val / Shares Out (mn)	538 USD / 33.1
Free Float	16.7%
Average Daily Value	2.95 USD
BofA Ticker / Exchange	PSBD / NYS
Bloomberg / Reuters	PSBD US / PSBD.N
ROE (2024E)	12.5%

iQprofileSM Palmer Square Capital BDC

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Interest Income	51	68	82	79	76
% change	64.3%	32.7%	21.7%	-4.2%	-3.1%
Net Fee Income	NA	NA	NA	NA	NA
Securities Gains / (Losses)	NA	NA	NA	NA	NA
Total Operating Income	51	68	82	79	76
Operating Expenses	(10)	(10)	(22)	(22)	(22)
% change	21.0%	-2.1%	121.1%	2.1%	-1.4%
Provisions Expense	NA	NA	NA	NA	NA
% change	NA	NA	NA	NA	NA
Operating Pre-Tax Income	(74)	108	61	57	55
Operating Net Income to Comm S/Hold.	(74)	108	61	57	55
GAAP Net Income	(74)	108	61	57	55

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Total Assets	1,114	1,089	1,289	1,382	1,382
Average Interest Earning Assets	NA	NA	NA	NA	NA
Total Gross Customer Loans	0	0	0	0	0
% change	NA	NA	NA	NA	NA
Total Customer Deposits	NA	NA	NA	NA	NA
% change	NA	NA	NA	NA	NA
Tangible Equity	NA	NA	NA	NA	NA
Common Shareholders' Equity	405	422	552	567	573

Key Metrics (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Interest Margin	NA	NA	NA	NA	NA
Effective Tax Rate	NM	NM	NM	NM	NM
Loan / Deposit Ratio	NA	NA	NA	NA	NA
Tangible Common Equity / Assets	0%	0%	0%	0%	0%
ROA	NA	NA	NA	NA	NA
ROE	11.7%	14.0%	12.5%	10.2%	9.6%
RoTE	NA	NA	NA	NA	NA
Dividend Payout Ratio	NA	51.6%	90.4%	97.9%	99.1%
Efficiency Ratio (Cost / Income Ratio)	19.5%	14.4%	26.2%	27.9%	28.4%

Quality of Earnings (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Total Non-Interest Inc / Operating Inc	0%	0%	0%	0%	0%
NPLs plus Foreclosed Real Estate / Loans	NA	NA	NA	NA	NA
Loan Loss Reserves / NPLs	NA	NA	NA	NA	NA
Loan Loss Reserves / Total Loans	NA	NA	NA	NA	NA

Company Sector

Financial Services-Consumer/Commercial

Company Description

PSBD began investing in 2020 and is a specialty finance company, regulated as a BDC under the Investment Company Act of 1940, as amended, which invests in debt. PSBD's investment objective is to maximize total return through current income and capital appreciation. The company primarily invests in the liquid broadly-syndicated loan market.

Investment Rationale

We rate PSBD Neutral. We believe it has a differentiated strategy which can generate solid risk-adjusted returns due to: (1) liquid portfolio focus, (2) larger average portfolio company size, (3) best-in-class fee structure creates greater shareholder alignment. That said, PSBD has limited operating history and it has not operated through a full economic cycle. We view valuation as fair given shares trade about in-line with peers, and we see limited catalysts for the shares to re-rate higher.

Stock Data

Average Daily Volume 181,307

Quarterly Earnings Estimates

	2023	2024
Q1	0.55A	0.47E
Q2	0.56A	0.47E
Q3	0.57A	0.46E
Q4	0.57A	0.48E

Initial Public Offering

PSBD completed its initial public offering (IPO) in January 2024. The company issued 5.45 million shares of its common stock at \$16.45 per share (approximately 0.97x 4Q23 NAV/share of \$17.04) for gross proceeds of roughly \$90M. Pre-IPO shareholders are subject to a lock-up schedule. 180 days after the IPO, one-third of such shares unlock; on day 270 an additional one-third unlock; on day 360 the remaining one-third are unlocked.

Dividend outlook

The 4Q23 dividend was \$0.54/share vs. \$0.56 the prior quarter. PSBD will declare the 1Q24 dividend in March. In the BofA model, the total dividend is made up of two components: (1) a core dividend of \$0.40/share per quarter; and (2) a quarterly variable supplemental dividend. We estimate PSBD will pay supplemental dividends totaling \$0.10 per share in 2024 and \$0.09 in 2025. Our dividend forecast is \$1.70 in 2024 and \$1.69 in 2025, and \$1.63 in 2026.

Exhibit 1: Unchanged 24/25E core EPS forecast of \$1.88/\$1.72 & introduce our 26E core EPS forecast of \$1.65

PSBD summary income statement

	2022A	2023A	1Q24E	2Q24E	3Q24E	4Q24E	2024E	2025E	2026E
Income Statement (thousand)									
Interest From Investments - Interest Income	73,705	107,739	31,681	34,099	34,356	34,732	134,868	129,763	123,877
Dividend income	610	4,067	-	-	-	-	-	-	-
PIK interest income	-	2	-	-	-	-	-	-	-
Other income	184	418	150	150	150	150	600	800	1,000
Total Investment Income	74,500	112,226	31,831	34,249	34,506	34,882	135,468	130,563	124,877
Interest Expense	23,452	44,484	12,548	13,426	13,683	13,391	53,048	51,586	48,381
Net Interest Income	51,048	67,742	19,282	20,823	20,823	21,491	82,420	78,977	76,496
Non-Interest Expense	9,967	9,753	5,065	5,405	5,471	5,620	21,560	22,003	21,693
Net Investment Income	41,081	57,990	14,218	15,418	15,353	15,871	60,860	56,974	54,803
Net Realized Gain/(Loss) on Investments	(8,130)	(2,716)	-	-	-	-	-	-	-
Net Unrealized Gain/(Loss) on Investments	(107,433)	52,564	-	-	-	-	-	-	-
Net gain on Investments	(115,563)	49,848	-	-	-	-	-	-	-
Net Increase in Net Assets from Operations	(74,482)	107,838	14,218	15,418	15,353	15,871	60,860	56,974	54,803
Diluted Shares Outstanding	23,131	25,766	30,086	33,070	33,070	33,070	32,324	33,070	33,237
End of Period Shares	24,287	27,103	33,070	33,070	33,070	33,070	33,070	33,070	33,404
Earnings per Share									
GAAP EPS (diluted)	-\$3.22	\$4.19	\$0.47	\$0.47	\$0.46	\$0.48	\$1.88	\$1.72	\$1.65
Core EPS (diluted)	\$1.78	\$2.25	\$0.47	\$0.47	\$0.46	\$0.48	\$1.88	\$1.72	\$1.65
Dividends Paid	\$1.89	\$2.16	\$0.40	\$0.44	\$0.43	\$0.43	\$1.70	\$1.69	\$1.63
NAV (Book Value) per Share	\$14.96	\$17.04	\$17.02	\$17.05	\$17.08	\$17.13	\$17.13	\$17.17	\$17.31

Source: Company reports, BofA Global Research estimates

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Price objective basis & risk

Palmer Square Capital BDC (PSBD)

Our \$16.50 PO is based on a roughly 0.95x multiple to current NAV/share, which we think is achievable as PSBD maintains stable margins and continued portfolio growth.

Downside risks to achieving our price objective are 1) material weakening in credit markets, 2) a deteriorating macroeconomic environment, 3) disruptions in the capital markets, and 4) weaker than expected investment performance.

Analyst Certification

I, Derek Hewett, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North America - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Ares Capital Corporation	ARCC	ARCC US	Derek Hewett
	Ares Commercial Real Estate Corporation	ACRE	ACRE US	Derek Hewett
	Bank of Montreal	BMO	BMO US	Ebrahim H. Poonawala
	Bank of Montreal	YBMO	BMO CN	Ebrahim H. Poonawala
	Barings BDC Inc	BBDC	BBDC US	Derek Hewett
	Blackstone Mortgage Trust Inc	BXMT	BXMT US	Derek Hewett
	Blue Owl Capital Corporation	OBDC	OBDC US	Derek Hewett
	Carlyle Secured Lending Inc	CGBD	CGBD US	Derek Hewett
	Citigroup Inc.	C	C US	Ebrahim H. Poonawala
	Compass Diversified Holdings	CODI	CODI US	Derek Hewett
	Crescent Capital BDC	CCAP	CCAP US	Derek Hewett
	Cullen/Frost Bankers Inc	CFR	CFR US	Ebrahim H. Poonawala
	East West Bancorp, Incorporated	EWBC	EWBC US	Ebrahim H. Poonawala
	Fifth Third Bank	FITB	FITB US	Ebrahim H. Poonawala
	First Bancorp Puerto Rico	FBP	FBP US	Brandon Berman
	First Horizon Corporation	FHN	FHN US	Ebrahim H. Poonawala
	FNB Corporation of Pennsylvania	FNB	FNB US	Brandon Berman
	Goldman Sachs	GS	GS US	Ebrahim H. Poonawala
	JPMorgan Chase & Co.	JPM	JPM US	Ebrahim H. Poonawala
	KeyCorp	KEY	KEY US	Ebrahim H. Poonawala
	M&T Bank	MTB	MTB US	Ebrahim H. Poonawala
	Morgan Stanley	MS	MS US	Ebrahim H. Poonawala
	New Mountain Finance Corporation	NMFC	NMFC US	Derek Hewett
	Northern Trust Corporation	NTRS	NTRS US	Ebrahim H. Poonawala
	Nuveen Churchill Direct Lending	NCDL	NCDL US	Derek Hewett
	Royal Bank of Canada	RY	RY US	Ebrahim H. Poonawala
	Royal Bank of Canada	YRY	RY CN	Ebrahim H. Poonawala
	Safehold, Inc	SAFE	SAFE US	Derek Hewett
	Starwood Property Trust	STWD	STWD US	Derek Hewett
	Synovus Financial Corp.	SNV	SNV US	Ebrahim H. Poonawala
	The Bank of New York Mellon Corporation	BK	BK US	Ebrahim H. Poonawala
	Truist Financial	TFC	TFC US	Ebrahim H. Poonawala
	U.S. Bancorp	USB	USB US	Ebrahim H. Poonawala
	Webster Financial Corp.	WBS	WBS US	Brandon Berman
	Wells Fargo & Company	WFC	WFC US	Ebrahim H. Poonawala
	Western Alliance Bancorp	WAL	WAL US	Ebrahim H. Poonawala
NEUTRAL				
	AGNC Investment Corp	AGNC	AGNC US	Derek Hewett
	Ally Financial	ALLY	ALLY US	Brandon Berman
	Annaly Capital Management	NLY	NLY US	Derek Hewett
	Apollo Commercial Real Estate Finance	ARI	ARI US	Derek Hewett
	Associated Banc-Corp	ASB	ASB US	Brandon Berman
	Bain Capital Specialty Finance, Inc.	BCSF	BCSF US	Derek Hewett

North America - Banks Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Bank of Nova Scotia	YBNS	BNS CN	Ebrahim H. Poonawala
	Bank of Nova Scotia	BNS	BNS US	Ebrahim H. Poonawala
	Blackstone Secured Lending Fund	BXSL	BXSL US	Derek Hewett
	BrightSpire Capital Inc.	BRSP	BRSP US	Derek Hewett
	Canadian Imperial Bank of Commerce	CM	CM US	Ebrahim H. Poonawala
	Canadian Imperial Bank of Commerce	YCM	CM CN	Ebrahim H. Poonawala
	Citizens Financial Group	CFG	CFG US	Ebrahim H. Poonawala
	Comerica Incorporated	CMA	CMA US	Brandon Berman
	Commerce Bancshares Inc.	CBSH	CBSH US	Brandon Berman
	Goldman Sachs BDC, Inc.	GSBD	GSBD US	Derek Hewett
	Golub Capital BDC, Inc.	GBDC	GBDC US	Derek Hewett
	Huntington Bancshares Inc.	HBAN	HBAN US	Ebrahim H. Poonawala
	Ladder Capital Corp	LADR	LADR US	Derek Hewett
	New York Community Bancorp	NYCB	NYCB US	Ebrahim H. Poonawala
	Palmer Square Capital BDC	PSBD	PSBD US	Derek Hewett
	PennyMac Mortgage Investment Trust	PMT	PMT US	Derek Hewett
	Popular Inc	BPOP	BPOP US	Brandon Berman
	Regions Financial	RF	RF US	Ebrahim H. Poonawala
	The PNC Financial Services Group, Inc.	PNC	PNC US	Ebrahim H. Poonawala
	Toronto-Dominion Bank	TD	TD US	Ebrahim H. Poonawala
	Toronto-Dominion Bank	YTD	TD CN	Ebrahim H. Poonawala
	TPG RE Finance Trust, Inc.	TRTX	TRTX US	Derek Hewett
UNDERPERFORM				
	Bank of Hawaii Corp.	BOH	BOH US	Brandon Berman
	First Hawaiian Inc.	FHB	FHB US	Brandon Berman
	Guild Holdings Company	GHLD	GHLD US	Derek Hewett
	Invesco Mortgage Capital, Inc.	IVR	IVR US	Derek Hewett
	loanDepot Inc	LDI	LDI US	Derek Hewett
	MidCap Financial Investment Co	MFIC	MFIC US	Derek Hewett
	Prosperity Bancshares Inc	PB	PB US	Ebrahim H. Poonawala
	State Street Corporation	STT	STT US	Ebrahim H. Poonawala
	Texas Capital Bancshares Inc.	TCBI	TCBI US	Brandon Berman
	Zions Bancorp	ZION	ZION US	Brandon Berman
RSTR				
	Sixth Street Specialty Lending, Inc	TS LX	TS LX US	Derek Hewett

IQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization



Valuation Toolkit

Numerator

Denominator

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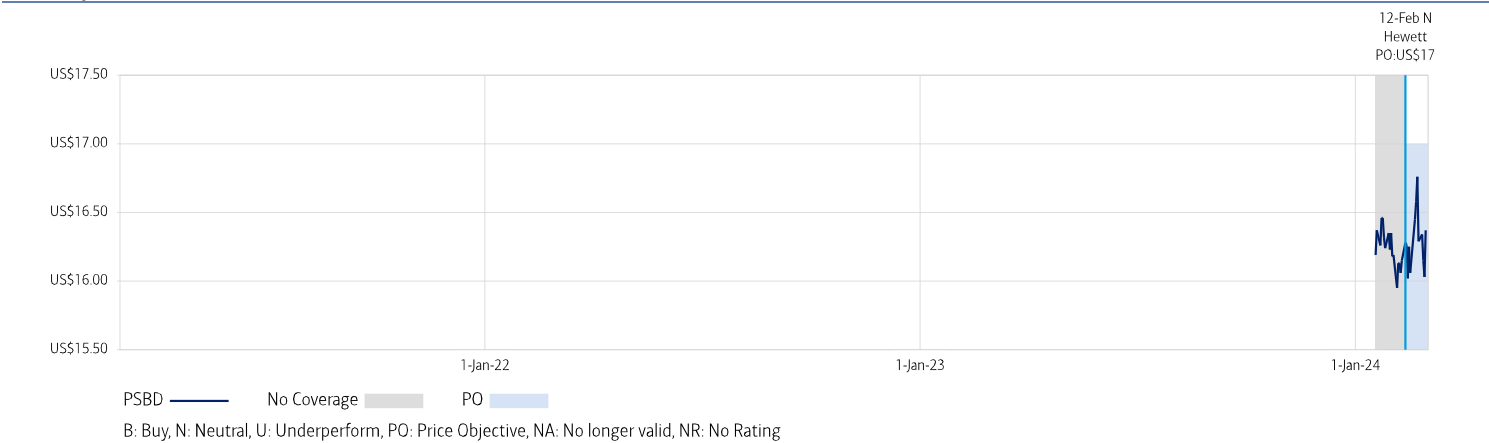
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Palmer Square BDC (PSBD) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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