

February 6, 2020

New Residential Investment Corp

NRZ Reports Impressive 4Q19 Earnings Beat Driven by Strong Originations and Higher UPB Providing Additional Dividend Support

WHAT YOU SHOULD KNOW: Before the market open today, New Residential (NRZ) reported strong 4Q19 results posting Core Earnings Per Diluted Share of \$0.61 exceeding our estimate and the consensus estimate of \$0.52 by a wide margin. The beat was driven by impressive originations volumes and higher MSR UPB balances in the period that both benefited from NRZ's recent acquisition of Ditech which closed on October 2nd 2019. NRZ's hedging strategy that was implemented during FY19 effectively preserved book value during a volatile interest rate environment – 4Q19 BVPS of \$16.21 was down \$0.05 QoQ. We believe strong core earnings performance provides more comfort around NRZ's dividend coverage and ability to grow earnings and book value going forward, which we believe is underappreciated by the market.

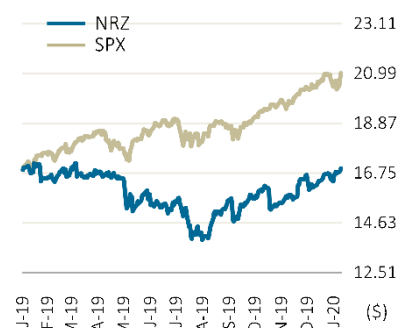
- **Servicing** – Servicing UPB increased to \$630B from \$593B in 3Q19 – the increase was primarily driven by \$62B of UPB acquired from Ditech during 4Q19. Higher 4Q19 average UPB balances boosted earnings performance and the outlook remains strong with NRZ's preliminary agreement to acquire and additional ~\$40B of UPB which is expected to close during 1Q20.
- **Originations** – NRZ originated \$10.6B in 4Q19, up 85% QoQ due to the acquisition of Ditech and growth in originations channels. The company's FY20 origination volume outlook also increased significantly to \$50B+ from ~\$40B – this volume provides additional operating income, organic MSR replenishment and reduces MSR replenishment costs which should provide a material cash flow benefit in FY20.
- **Outlook** – NRZ's exposure to Non-Agency MSRs benefited 4Q19 CPR speeds between 4% and 5% compared to industry average – between lower prepayment speeds and MSR acquisitions, NRZ is well positioned to continue growing servicing UPB and operating earnings in FY20. Combined with 100%+ growth origination volumes and improved recapture performance, MSR UPB should further stabilize and replenishment costs should continue to fall.
- **Operating Company Earnings and Book Value Upside** – NRZ's acquisitions of/investments in ancillary services business have a minimal basis on the company's balance sheet and are beginning to generate more operating earnings which could be a source of book value upside. On the conference call, management noted that \$250M+ of operating earnings is an achievable result during FY20. At a 6.5X multiple, \$250M of earnings could be worth an additional ~\$2.70 of value and would increase BV per share to \$18.90 or 16.6% on a sum-of-the-parts basis.
- **Non-QM Opportunity** – While the precise Non-QM opportunity if the QM patch expires and/or if the GSE's change their footprint going forward is difficult to put a fine estimate on, it could easily create a \$200B+ origination opportunity. NRZ should be well positioned to take advantage of potential Non-QM opportunities.

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NRZ	\$16.95
12 month target	\$18.00

Buy	
52 week range	\$13.91 - \$17.17
Market Cap (M)	\$7,042

Price Performance



Source: IDC, BTIG Estimates and Company Documents
(\$ in millions, except per share amount)

NRZ's MSR portfolio has less sensitivity to lower interest rates because the portfolio is relatively more seasoned compared to the industry average with a weighted average loan age (WALA) of 84 months vs. 51 months for the industry and has an average loan balance of \$151K vs. 183K industry average. Combined with a higher concentration of Non-Agency MSRs, this reduces prepayment sensitivity in low/falling interest rate environment. NRZ estimates 21% of the company's MSRs are refinancable in the current interest rate environment vs. 41% for the industry.

Exhibit 1: NRZ's MSR Portfolio Detail as of 4Q19

	Full MSRs					Excess MSRs					Total
	FHLMC	FNMA	GNMA	Non-Agency	Full MSR Total	FHLMC	FNMA	GNMA	Non-Agency	Excess MSR Total	
UPB (\$B)	118	252	52	83	506	34	25	22	45	125	630
WAC	4.3%	4.3%	4.0%	4.7%	4.3%	4.6%	4.7%	4.8%	48.0%	4.7%	4.4%
WALA (months)	52	72	37	168	79	84	102	103	167	126	84
LTV	67%	63%	87%	81%	70%	54%	49%	59%	67%	59%	69%
FICO	752	744	684	645	721	734	720	695	673	700	719
60+ DQ	0.5%	1.4%	3.4%	15.4%	3.7%	0.8%	1.8%	0.9%	9.3%	4.6%	3.8%

Source: BTIG and Company Reports

As NRZ's originations segment continues to grow volumes at an accelerated pace, we believe it is important to reiterate the potential MSR replenishment cost savings that could be realized combined with internal replenishment of the MSR portfolio. During 4Q19, the company increased targeted FY20 origination volume to over \$50B from ~\$40B driven by growth in all four channels.

While the margins will likely take some time to come up to industry averages as NRZ grows the origination platform, potential cash flow accretion could be material. For example, if NRZ is able to originate \$50B in FY20, \$28B of additional volume during in FY20 vs. FY19 at a 50 bps margin, that would save ~\$140M in annual MSR replenishment costs.

Exhibit 2: MSR replenishment cost savings model (in millions)

	0 bps	10 bps	20 bps	30 bps	40 bps	50 bps	60 bps	70 bps	80 bps
\$20B	\$0	\$20	\$40	\$60	\$80	\$100	\$120	\$140	\$160
\$22B	\$0	\$22	\$44	\$66	\$88	\$110	\$132	\$154	\$176
\$24B	\$0	\$24	\$48	\$72	\$96	\$120	\$144	\$168	\$192
\$26B	\$0	\$26	\$52	\$78	\$104	\$130	\$156	\$182	\$208
\$28B	\$0	\$28	\$56	\$84	\$112	\$140	\$168	\$196	\$224
\$30B	\$0	\$30	\$60	\$90	\$120	\$150	\$180	\$210	\$240
\$32B	\$0	\$32	\$64	\$96	\$128	\$160	\$192	\$224	\$256
\$34B	\$0	\$34	\$68	\$102	\$136	\$170	\$204	\$238	\$272
\$36B	\$0	\$36	\$72	\$108	\$144	\$180	\$216	\$252	\$288
\$38B	\$0	\$38	\$76	\$114	\$152	\$190	\$228	\$266	\$304
\$40B	\$0	\$40	\$80	\$120	\$160	\$200	\$240	\$280	\$320

Source: BTIG Estimates and Company Reports



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NEW RESIDENTIAL INVESTMENT CORP (NRZ, Buy, \$18.00 PT; Current Price: \$16.95; Analyst: Giuliano.Bologna)

Appendix: Analyst Certification and Other Important Disclosures

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New Residential Investment Corp (NRZ, Buy, \$18.00 PT)

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