



Oxford Square Capital Corp. (OXSQ)

Updated March 24th, 2021 by Nikolaos Sismanis

Key Metrics

Current Price:	\$4.3	5 Year CAGR Estimate:	8.2%	Market Cap:	\$213.2M
Fair Value Price:	\$4.3	5 Year Growth Estimate:	0.0%	Ex-Dividend Date:	04/15/2021
% Fair Value:	100%	5 Year Valuation Multiple Estimate:	0.1%	Dividend Payment Date:	04/30/2021
Dividend Yield:	9.8%	5 Year Price Target	\$4.3	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Last Dividend Increase:	N/A

Overview & Current Events

Oxford Square Capital Corp. is a BDC (Business Development Company) specializing in financing early and middle-stage businesses through loans and CLOs. The company holds an equally split portfolio of First-Lien, Second-Lien, and CLO equity assets spread across 9 industries, with the highest exposure in business services and healthcare, at 35.1% and 24.2%, respectively. The company's assets have a gross investment value of around \$300 million in 54 positions, with 67.2% of debt securities being secured. OXSQ generates around \$50 million in annual interest payments and is based in Greenwich, Connecticut.

On March 22nd, Oxford Square reported its Q4 results for the quarter ended December 31st, 2020. The company generated approximately \$8.6 million of total investment income, an increase of 4.8% compared to Q3, but 35.68% lower year-over-year due to the pandemic shrinking Oxford Square's investment portfolio. Expenses, which primarily include interest paid on its own financing and managers' fees, amounted to ~\$4 million, relatively unchanged from Q3. As a result, NII (net investment income) amounted to around \$4.7 million, or \$0.10/share, wrapping up the annual NII/share at \$0.40, a 51% decline compared to FY2019. Once again, the massive slump was attributed to the gradual decline in interest rates, making it impossible for the company to lend at its historically much higher rates. Additionally, management's consistently unsustainable distributions have caused Oxford Square's NAV to gradually deteriorate, resulting in fewer debt reinvestments over time, subsequently lowering its interest income over the years dramatically. Amid higher payouts against net income generation during 2020, the company ended the year with a NAV/share of \$4.55, compared to \$5.12 in the prior year. Assuming management does not intend to over-distribute once again, we expect this year's IIS/share to be around \$0.45.

Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
IIS¹	\$0.96	\$1.12	\$1.07	\$1.17	\$0.66	\$0.52	\$0.60	\$0.67	\$0.81	\$0.40	\$0.45	\$0.45
DPS	\$0.99	\$1.12	\$1.16	\$1.19	\$1.13	\$1.15	\$0.80	\$0.79	\$0.80	\$0.61	\$0.42	\$0.42
Shares²	32.4	38	51.1	58.8	59.8	51.9	51.5	49.7	47.8	49.4	49.1	50.0

The company's investment income per share has been declining at a 10-year CAGR of 9.3%, as financing has become cheaper, preventing Oxford Square from refinancing at its previously higher rates. Additionally, the company has been historically over-distributing dividends to shareholders, decaying its NAV, and hence, future income generation due to fewer assets. Considering that the Fed has made it clear that they intend to hold rates near 0, we find it incredibly unlikely that Oxford Square will be able to return to its previously gross interest generated.

Consequently, we expect IIS & DPS to remain stable in the medium term, as management's recent dividend cut should result in Oxford Square retaining some cash, hopefully starting to regrow its NAV. With rates a bit unlikely to continue moving any lower, income generation should stabilize over the next few years.

¹ Investment Income per Share

² Share count is in millions.

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Since 2019, the company has switched its distributions' frequency from quarterly to monthly.

Valuation Analysis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Now	2026
Avg. P/E	9.3	8.4	9.0	8.1	10.5	11.1	11.3	10.6	7.9	7.0	9.6	9.6
Avg. Yld.	11.4%	11.0%	11.4%	11.5%	18.3%	19.9%	11.2%	12.2%	12.9%	21.0%	9.8%	9.7%

As per the company's goal and obligation (being a Business Development Company) to distribute the majority of its net income to shareholders, the stock's yield has hovered around the mid-teens, averaging nearly 14% over the past decade. Despite management's recent distribution slash to a monthly \$0.035 payout, the market stock has declined enough to push the current yield to 9.8%. Now that the valuation and yield of Oxford Square have matched those of its peers, we expect them to remain relatively stable moving forward. That is assuming the current distributions remain covered, avoiding further NAV deterioration.

Safety, Quality, Competitive Advantage, & Recession Resiliency

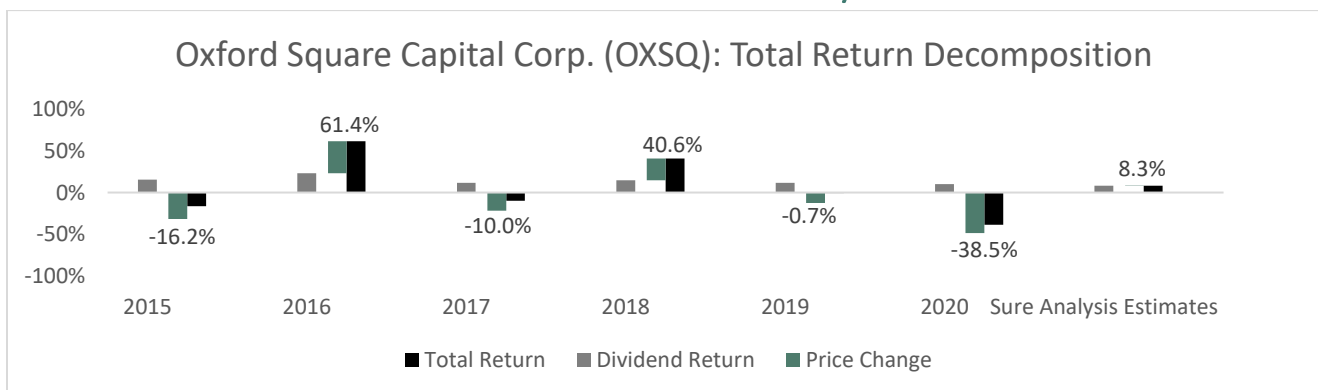
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	103%	100%	108%	102%	171%	221%	133%	118%	99%	153%	93%	93%

OXSQ's payout ratio has often been above 100% over the years, as management used to pay investors more than what the company earned. While the stock's dividend yield has been seemingly attractive over the years, the company has been wiping an equal, and sometimes higher, amount from its NAV. Such a strategy could be sustained only via a gradually increased interest income. However, with rates declining over time, the company's receivables have been further pressurized, worsening its financials annually. This will hopefully stop being the case post the recent steep distribution cut. Overall, we believe that the company's future investment income generation carries substantial risks, while a potential recession and an adverse economic environment could severely damage its interest income.

Final Thoughts & Recommendation

Oxford Square Capital Corp. currently operates in an unfavorable credit market environment, dominated by cheap financing, which prevents it from sustaining and growing its income. Distributions are only marginally covered at the moment. Hence, management may be able to sustain them in the short-term, but another slash should not surprise investors if rates keep moving lower. Combining the robust yield and Oxford Square's reasonable valuation, we can see shares sustaining a positive total return outcome in the mid to high-single digits. However, those looking to generate a stable monthly income stream are likely to find more trustworthy and reliable options elsewhere. Currently, OXSQ remains incredibly risky, with limited potential returns to compensate current investors. Shares earn a Hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	24.80	84.09	83.90	23.88	-57.03	121.57	49.41	-5.52	-28.74	5.54
SG&A Expense	9.39	14.45	23.07	25.08	7.61	10.06	4.66	2.56	2.98	2.91
Net Income	14.21	68.32	58.94	-3.35	-66.13	110.36	43.61	-9.21	-32.80	1.71
Net Margin	57.3%	81.3%	70.3%	-14.0%	---	90.8%	88.3%	---	---	30.9%
Free Cash Flow	-114.5	-215.7	-201.6	-53.01	243.81	182.91	217.63	-33.86	47.76	95.05

Balance Sheet Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Total Assets	424.1	756.0	998.2	1042.6	718.3	612.5	454.1	467.1	385.3	357.7
Cash & Equivalents	4.5	51.4	14.9	20.5	23.2	8.3	30.0	13.9	14.4	59.1
Total Liabilities	119.0	346.4	471.9	521.8	357.4	226.5	65.7	152.4	137.3	132.2
Accounts Payable	17.3	9.2	16.7	20.1	6.3	1.7	0.0	0.5	0.6	23.6
Long-Term Debt	99.7	330.3	450.7	501.1	347.7	220.0	62.3	148.2	134.4	106.9
Total Equity	305.1	409.6	526.2	520.8	360.9	386.0	388.4	314.7	248.0	225.4
DE Ratio	0.33	0.81	0.86	0.96	0.96	0.57	0.16	0.47	0.54	0.47

Profitability & Per Share Metrics

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Return on Assets	3.8%	11.6%	6.7%	-0.3%	-7.5%	16.6%	8.2%	-2.0%	-7.7%	0.5%
Return on Equity	4.6%	19.1%	12.6%	-0.6%	-15.0%	29.6%	11.3%	-2.6%	-11.7%	0.7%
ROIC	4.0%	11.9%	6.9%	-0.3%	-7.6%	16.8%	8.3%	-2.0%	-7.8%	0.5%
Shares Out.	32.43	40.58	61.11	68.86	69.79	61.77	51.48	49.66	47.76	49.48
Revenue/Share	0.76	2.07	1.37	0.35	-0.82	1.97	0.96	-0.11	-0.60	0.11
FCF/Share	-3.53	-5.32	-3.30	-0.77	3.49	2.96	4.23	-0.68	1.00	1.92

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

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