



# Oxford Square Capital Corp. (OXSQ)

Updated May 16<sup>th</sup>, 2021 by Nikolaos Sismanis

## Key Metrics

<b>Current Price:</b>	\$4.85	<b>5 Year CAGR Estimate:</b>	6.0%	<b>Market Cap:</b>	\$240 M
<b>Fair Value Price:</b>	\$4.40	<b>5 Year Growth Estimate:</b>	0.0%	<b>Ex-Dividend Date:</b>	06/15/2021
<b>% Fair Value:</b>	110%	<b>5 Year Valuation Multiple Estimate:</b>	-1.9%	<b>Dividend Payment Date:</b>	06/30/2021
<b>Dividend Yield:</b>	8.7%	<b>5 Year Price Target</b>	\$4.4	<b>Years Of Dividend Growth:</b>	0
<b>Dividend Risk Score:</b>	F	<b>Retirement Suitability Score:</b>	C	<b>Last Dividend Increase:</b>	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 8 industries, with the highest exposure in business services and healthcare, at 36.4% and 27.5%, respectively. The company's assets have a gross investment value of around \$320 million in 53 positions, with 6.3% of debt securities being secured. OXSQ generates around \$50 million in annual interest payments and is based in Greenwich, Connecticut.

On April 27<sup>th</sup>, Oxford Square reported its Q1 results for the quarter ended March 31<sup>st</sup>, 2021. The company generated approximately \$9.4 million of total investment income, an increase of 9.3% compared to the previous quarter but 13.53% lower on a YoY basis. This was due to the declining rates over this period, which affected the company's investment yields. The weighted average yield of its debt investments was 7.7% at the current cost, compared with 8.0% as of December 31<sup>st</sup>, 2020. Cash income from its CLO equity investments also saw declining yields, from 19.2% to 17.9% during this period. Total expenses, which primarily include interest paid on its own financing and managers' fees, amounted to \$4.5 million, 15.3% higher compared to Q4. As a result, NII (net investment income) amounted to around \$4.8 million, or \$0.10/share, stable QoQ. Net asset value (NAV) per share was \$4.88 compared to \$4.55 in the previous quarter due to last year's distribution cut. Assuming management does not intend to over-distribute, as has been the case in the past, which has led to a deteriorating NAV, we expect this year's IIS/share to be around \$0.44.

## Growth on a Per-Share Basis

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
<b>IIS<sup>1</sup></b>	\$0.96	\$1.12	\$1.07	\$1.17	\$0.66	\$0.52	\$0.60	\$0.67	\$0.81	\$0.40	<b>\$0.44</b>	<b>\$0.44</b>
<b>DPS</b>	\$0.99	\$1.12	\$1.16	\$1.19	\$1.13	\$1.15	\$0.80	\$0.79	\$0.80	\$0.61	<b>\$0.42</b>	<b>\$0.42</b>
<b>Shares<sup>2</sup></b>	32.4	38	51.1	58.8	59.8	51.9	51.5	49.7	47.8	49.4	<b>49.5</b>	<b>50.0</b>

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 mid-2020 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.

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

<sup>1</sup> Investment Income per Share

<sup>2</sup> 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	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	<b>11.0</b>	<b>10.0</b>
Avg. Yld.	11.4%	11.0%	11.4%	11.5%	18.3%	19.9%	11.2%	12.2%	12.9%	21.0%	<b>8.7%</b>	<b>9.5%</b>

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 stock has declined enough to push the current yield to 8.7%. Now that the valuation and yield of Oxford Square have matched those of its peers, we expect these to remain relatively stable moving forward. We believe a valuation multiple of 10 adequately reflects the stock's risk/reward investment case. From a NAV perspective, the stock is fairly priced, with no premium attached.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

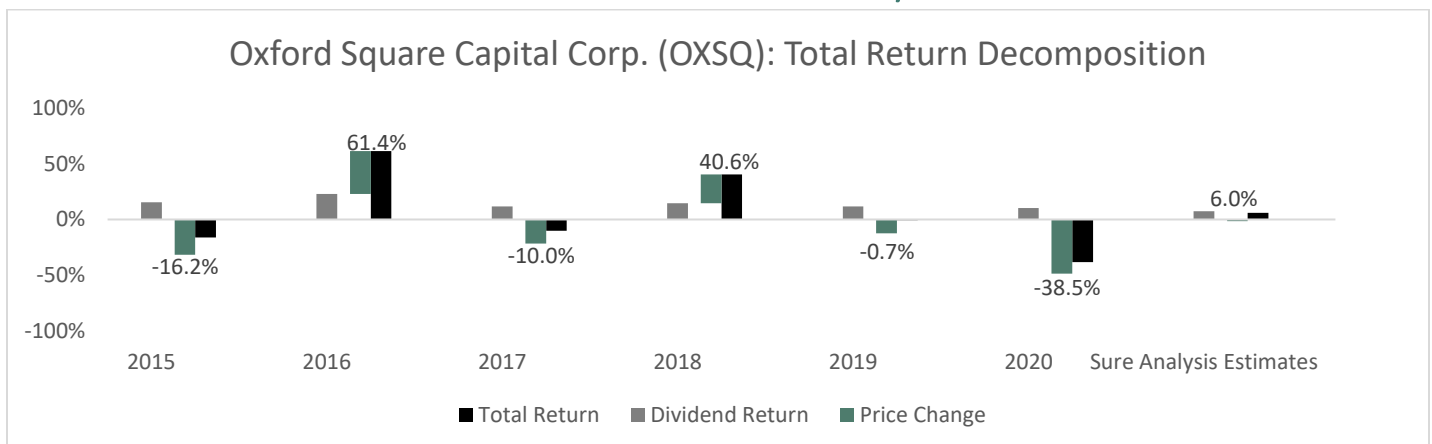
Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2026
Payout	103%	100%	108%	102%	171%	221%	133%	118%	99%	153%	95%	<b>95%</b>

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 step 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 distributions 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-single digits. However, those looking to generate a stable monthly income stream are likely to find more trustworthy and reliable options elsewhere. 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
<b>Revenue</b>	24.80	84.09	83.90	23.88	-57.03	121.57	49.41	-5.52	-28.74	5.54
<b>SG&amp;A Expense</b>	9.39	14.45	23.07	25.08	7.61	10.06	4.66	2.56	2.98	2.91
<b>Net Income</b>	14.21	68.32	58.94	-3.35	-66.13	110.36	43.61	-9.21	-32.80	1.71
<b>Net Margin</b>	57.3%	81.3%	70.3%	-14.0%	---	90.8%	88.3%	---	---	30.9%
<b>Free Cash Flow</b>	-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
<b>Total Assets</b>	424.1	756.0	998.2	1042.6	718.3	612.5	454.1	467.1	385.3	357.7
<b>Cash &amp; Equivalents</b>	4.5	51.4	14.9	20.5	23.2	8.3	30.0	13.9	14.4	59.1
<b>Total Liabilities</b>	119.0	346.4	471.9	521.8	357.4	226.5	65.7	152.4	137.3	132.2
<b>Accounts Payable</b>	17.3	9.2	16.7	20.1	6.3	1.7	0.0	0.5	0.6	23.6
<b>Long-Term Debt</b>	99.7	330.3	450.7	501.1	347.7	220.0	62.3	148.2	134.4	106.9
<b>Total Equity</b>	305.1	409.6	526.2	520.8	360.9	386.0	388.4	314.7	248.0	225.4
<b>DE Ratio</b>	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
<b>Return on Assets</b>	3.8%	11.6%	6.7%	-0.3%	-7.5%	16.6%	8.2%	-2.0%	-7.7%	0.5%
<b>Return on Equity</b>	4.6%	19.1%	12.6%	-0.6%	-15.0%	29.6%	11.3%	-2.6%	-11.7%	0.7%
<b>ROIC</b>	4.0%	11.9%	6.9%	-0.3%	-7.6%	16.8%	8.3%	-2.0%	-7.8%	0.5%
<b>Shares Out.</b>	32.43	40.58	61.11	68.86	69.79	61.77	51.48	49.66	47.76	49.48
<b>Revenue/Share</b>	0.76	2.07	1.37	0.35	-0.82	1.97	0.96	-0.11	-0.60	0.11
<b>FCF/Share</b>	-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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