



Oaktree Specialty Lending Corporation (OCSL)

Updated November 16th, 2023, by Patrick Neuwirth

Key Metrics

Current Price:	\$20	5 Year CAGR Estimate:	21.4%	Market Cap:	\$1.5 B
Fair Value Price:	\$25	5 Year Growth Estimate:	10.0%	Ex-Dividend Date¹:	12/14/23
% Fair Value:	80%	5 Year Valuation Multiple Estimate:	4.2%	Dividend Payment Date¹:	12/29/23
Dividend Yield:	11.0%	5 Year Price Target	\$39	Years Of Dividend Growth:	4
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

Oaktree Specialty Lending Corp. is a specialty finance company, or BDC. It provides lending services and invests in small and mid-sized companies. The company's investment objective is to maximize its portfolio's total return by generating current income from debt investments, and to a lesser extent, capital appreciation from equity investments. Its investments generally range in size from \$10 million to \$100 million and are principally in the form of the first lien, second lien, or collectively, senior secured, and subordinated debt investments, which may also include an equity component made in connection with investments by private equity sponsors. As of September 30th, 2023, the investment portfolio accounted for \$2.9 billion at fair value diversified across 143 portfolio companies, with a focus on software (16.5%) and Specialty Retail (5.4%). The company was founded in 1995, has 1,100 employees, and is headquartered in Los Angeles, California.

On November 14th, 2023, Oaktree Specialty Lending Corp. released its fourth quarter fiscal 2023 results for the period ending September 30th, 2023. For the quarter the company reported adjusted net investment income (NII) of \$47.8 million or \$0.62 per share, as compared with \$47.6 million or \$0.62 per share in the year-ago quarter. For the full-year 2023, adjusted net investment income ended at \$177.8 million or \$2.47 per share, as compared with \$128.6 million or \$2.12 per share in 2022. The quarterly increase in earnings was primarily due to increased original issue discount ("OID") acceleration from investment repayments, partially offset by reduced fee income. The annual increase was driven by higher base rates affecting the company's floating rate debt portfolio and the expansion of the investment portfolio resulting from the merger with Oaktree Strategic Income II, Inc. ("OSI2").

The weighted average yield on new debt investments was 12.0%, up from 10.2% for the same period last year, primarily due to higher base rates. Total debt outstanding was \$1,660 million as of September 30, 2023, with a total debt to equity ratio of 1.10x and a net debt to equity ratio of 1.01x, after adjusting for cash and cash equivalents. The company issued \$300 million in unsecured notes with a 7.10% interest rate. Management is optimistic about sustaining this momentum in the future, indicating their confidence in the company's positioning and ability to capitalize on investment opportunities.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
NII²	\$2.37	\$0.30	\$0.71	\$0.51	\$0.43	\$0.49	\$0.51	\$0.64	\$0.71	\$2.47	\$2.45	\$3.95
DPS	\$3.00	\$2.36	\$2.16	\$1.40	\$1.20	\$1.14	\$1.17	\$1.53	\$1.95	\$2.20	\$2.20	\$2.94
Shares³	50	54	50	47	47	47	47	54	61	77	77	80

The company has a net investment income growth rate of 0.5% per year over the past decade and 38% over the past five years. We expect net investment income to increase by 10% per year for the next five years. The company has been able to increase its yearly dividend payout for 4 consecutive years. Over the last five years, the average annual dividend growth rate is 14.1%. In February 2023, the company increased its quarterly dividend by 1.9% from \$0.54 to \$0.55 per

¹ Estimated date

² Adjusted net investment income

³ 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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share. In addition to the quarterly dividend, a special cash distribution of \$0.07 per share was declared, payable in cash on December 29, 2023, to stockholders of record on December 15, 2023.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	12.2	73.4	--	--	14.8	5.7	17.0	4.3	44.8	16.0	8.1	10.0
Avg. Yld.	1.9%	10.7%	13.0%	9.2%	8.2%	7.6%	8.2%	8.2%	9.1%	10.0%	11.0%	7.5%

During the past decade shares of Oaktree have traded with an average valuation of about 23.5 times earnings and today, it stands at 8.1. We are using 10.0 times earnings as a fair value baseline, implying the potential for a valuation tailwind. The company's dividend yield is currently 11.0% which is above the average yield over the past decade of 9.5%. Both of these figures imply that the stock is somewhat undervalued.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Payout	127%	787%	304%	275%	279%	233%	229%	239%	275%	89%	90%	75%

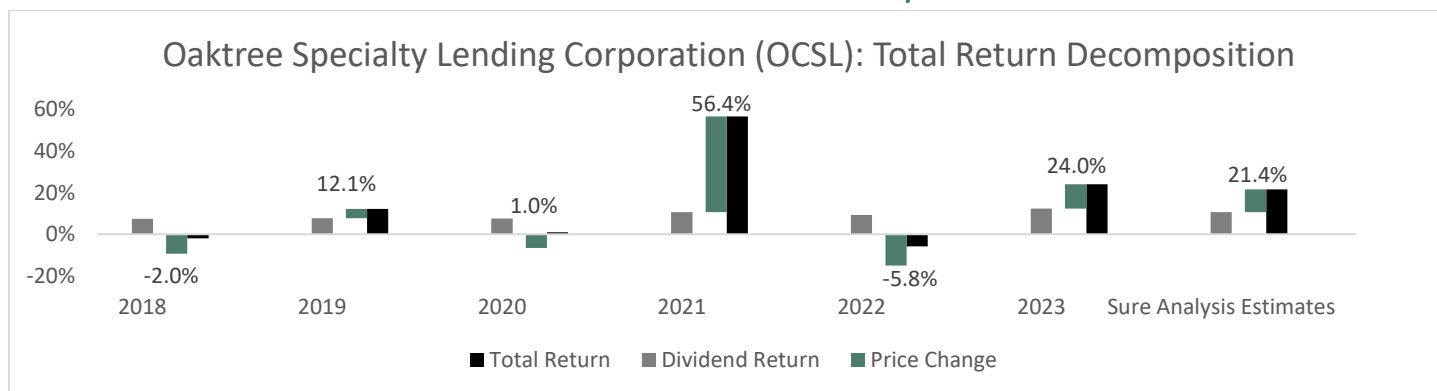
During the past five years, the company's dividend payout ratio has averaged above 200%. At present, Oaktree's dividend could be considered safer since the quarterly adjusted investment income of \$0.62 covered the quarterly dividend of \$0.55. Management believes that it has been very conservative in its approach to dividends.

Oaktree's business model centers around investing in various debt instruments, such as senior secured loans, subordinated loans, and mezzanine loans. The company primarily generates revenue through interest income earned on its loan investments. It may also earn revenue from fees charged for structuring and arranging financing transactions and from dividends received from equity investments. Oaktree's management has a strategy of rotating out of public debt investments and allocating capital into private credit opportunities. By targeting private credit, Oaktree can access potentially higher-yielding investments and take advantage of compelling opportunities in the private market. Its main competitive advantage comes from its management expertise and scale as being in the top 12 of the largest BDCs.

Final Thoughts & Recommendation

Oaktree Specialty Lending Corp. is a well-diversified investment company with a \$2.9 billion investment portfolio diversified across 143 portfolio companies⁴. Its 11% dividend yield provides investors with attractive income. The BDC business model does tend to struggle during recessions, so conservative investors should keep that risk in mind. We estimate total return potential of 21.4% per year for the next five years based on a 10% earnings-per-share growth, the dividend yield, and a valuation tailwind. Shares earn a buy rating.

Total Return Breakdown by Year



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⁴ OCSL, Q4-23 Investor presentation

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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	111	125	29	(44)	(184)	57	127	52	248	39
SG&A Exp.	12	13	14	23	15	11	8	7	9	9
Net Profit	102	113	15	(67)	(197)	47	126	39	237	29
Net Margin	91.6%	89.9%	52.9%	153%	107%	81.6%	99.2%	75.0%	95.6%	74.7%
Free Cash Flow	(462)	(546)	146	165	487	54	216	(153)	(231)	22
Income Tax				-	-	1	1	(2)	4	4

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	2,072	2,668	2,586	2,343	1,616	1,551	1,481	1,641	2,636	2,646
Cash & Equivalents	143	87	138	118	53	13	15	39	29	24
Total Liabilities	703	1,190	1,233	1,201	748	693	550	726	1,324	1,401
Accounts Payable	4	10	9	6	6	7	4	3	8	12
Long-Term Debt	646	1,152	1,199	1,149	675	637	473	709	1,269	1,301
Total Equity	1,369	1,478	1,353	1,142	868	858	931	915	1,313	1,246
LTD/E Ratio	0.47	0.78	0.89	1.01	0.78	0.74	0.51	0.78	0.97	1.04

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	5.9%	4.7%	0.6%	-2.7%	-9.9%	3.0%	8.3%	2.5%	11.1%	1.1%
Return on Equity	9.0%	7.9%	1.1%	-5.3%	-19.6%	5.4%	14.1%	4.3%	21.3%	2.3%
ROIC	6.0%	4.8%	0.6%	-2.7%	-10.3%	3.1%	8.7%	2.6%	11.3%	1.1%
Shares Out.	39	50	48	47	47	47	47	60	61	61
Revenue/Share	2.82	2.51	0.54	(0.86)	(3.90)	1.22	2.71	1.11	4.59	0.64
FCF/Share	(11.73)	(10.94)	2.72	3.27	10.33	1.14	4.59	(3.25)	(4.27)	0.37

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

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