



Oaktree Specialty Lending Corporation (OCSL)

Updated February 11th, 2024, by Patrick Neuwirth

Key Metrics

Current Price:	\$20	5 Year CAGR Estimate:	20.3%	Market Cap:	\$1.5 B
Fair Value Price:	\$23	5 Year Growth Estimate:	10.0%	Ex-Dividend Date¹:	03/14/24
% Fair Value:	87%	5 Year Valuation Multiple Estimate:	2.9%	Dividend Payment Date¹:	03/29/24
Dividend Yield:	11.0%	5 Year Price Target	\$37	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 December 31st, 2023, the investment portfolio accounted for \$3.0 billion at fair value diversified across 146 portfolio companies, with a focus on application software (15.2%), Biotech (4.2%) and Data Processing & Outsourced Services (4.2%). The company was founded in 1995, has 1,100 employees, and is headquartered in Los Angeles, California.

On February 1st, 2024, Oaktree Specialty Lending Corp. released its first quarter of fiscal 2024 results for the period ending December 31st, 2023. For the quarter, the company reported adjusted net investment income (NII) of \$44.2 million or \$0.57 per share, as compared with \$47.8 million or \$0.62 per share in the fourth quarter of fiscal 2023. The quarterly decrease in earnings was primarily due driven by lower adjusted total investment income, partially offset by lower incentive fees. The weighted average yield on new debt investments was 11.6%, slightly down from 12.0% in the fourth quarter of fiscal 2023. Total debt outstanding was \$1,660 million by the end of the reporting quarter, with a total debt to equity ratio of 1.10x and a net debt to equity ratio of 1.02x, after adjusting for cash and cash equivalents. New debt investment originations totaled \$82.3 million during the quarter. The debt-to-equity ratios indicate a conservative capital structure, maintaining financial flexibility. The management expresses confidence in the company's positioning and ability to navigate current market conditions. They remain focused on generating strong returns for shareholders. However, a guidance for the full year was not provided.

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	\$2.30	\$3.70
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 36% 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 share. In addition to the quarterly dividend, a special cash distribution of \$0.07 per share was declared, payable in cash in December 2023.

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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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	8.7	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%	7.9%

During the past decade shares of Oaktree have traded with an average valuation of about 23.5 times earnings and today, it stands at 8.7. 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 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	2024	2029
Payout	127%	787%	304%	275%	279%	233%	229%	239%	275%	89%	96%	79%

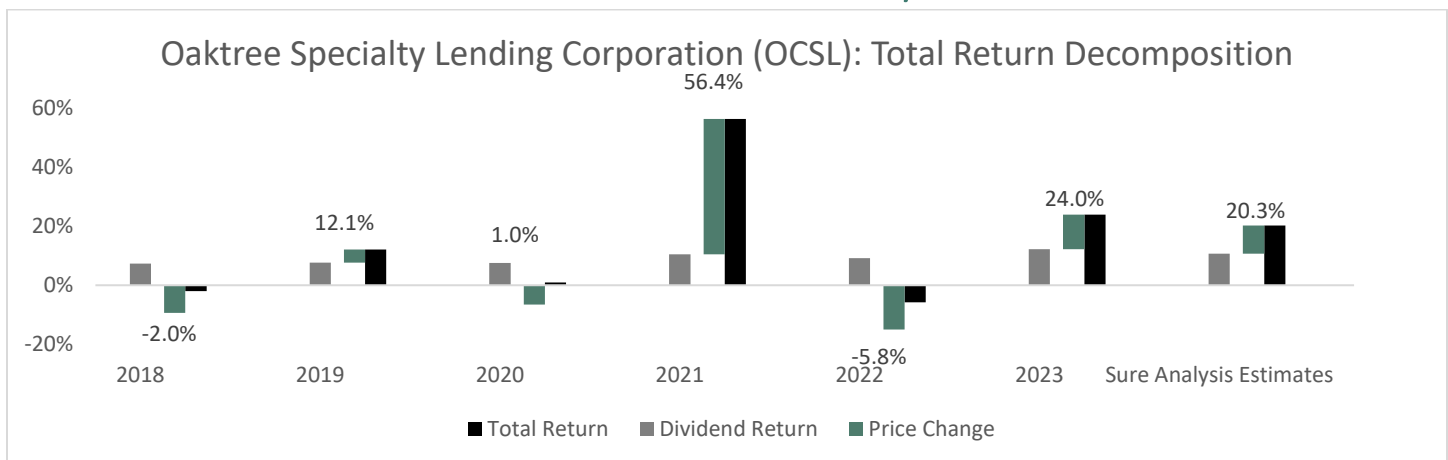
During the past five years, the company's dividend payout ratio has averaged above 200%. At present, Oaktree's dividend could be considered safe since the quarterly adjusted investment income of \$0.57 covered the quarterly dividend of \$0.55. Management believes that it has been very conservative in 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 \$3.0 billion investment portfolio diversified across 146 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 20.3% 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, Q1-24 Investor presentation

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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	125	29	(44)	(184)	57	127	52	248	39	125
SG&A Exp.	13	14	23	15	11	8	7	9	9	11.7
Net Profit	113	15	(67)	(197)	47	126	39	237	29	117
Net Margin	89.9%	52.9%	153%	107%	81.6%	99.2%	75.0%	95.6%	74.7%	93.6%
Free Cash Flow	(546)	146	165	487	54	216	(153)	(231)	22	229
Income Tax			-	-	1	1	(2)	4	4	1.7

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	2,668	2,586	2,343	1,616	1,551	1,481	1,641	2,636	2,646	3,218
Cash & Equivalents	87	138	118	53	13	15	39	29	24	136
Total Liabilities	1,190	1,233	1,201	748	693	550	726	1,324	1,401	1,702
Accounts Payable	10	9	6	6	7	4	3	8	12	19
Long-Term Debt	1,152	1,199	1,149	675	637	473	709	1,269	1,301	1,601
Total Equity	1,478	1,353	1,142	868	858	931	915	1,313	1,246	1,516
LTD/E Ratio	0.78	0.89	1.01	0.78	0.74	0.51	0.78	0.97	1.04	1.06

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	4.7%	0.6%	-2.7%	-9.9%	3.0%	8.3%	2.5%	11.1%	1.1%	4.0%
Return on Equity	7.9%	1.1%	-5.3%	-19.6%	5.4%	14.1%	4.3%	21.3%	2.3%	8.5%
ROIC	4.8%	0.6%	-2.7%	-10.3%	3.1%	8.7%	2.6%	11.3%	1.1%	4.1%
Shares Out.	50	48	47	47	47	47	60	61	61	72
Revenue/Share	2.51	0.54	(0.86)	(3.90)	1.22	2.71	1.11	4.59	0.64	1.74
FCF/Share	(10.94)	2.72	3.27	10.33	1.14	4.59	(3.25)	(4.27)	0.37	3.17

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

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