



Oxford Square Capital Corp. (OXSQ)

Updated November 27th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	\$2.63	5 Year CAGR Estimate:	11.6%	Market Cap:	\$178.6 M
Fair Value Price:	\$3.22	5 Year Growth Estimate:	-4.0%	Ex-Dividend Date:	12/17/2024
% Fair Value:	82%	5 Year Valuation Multiple Estimate:	4.1%	Dividend Payment Date:	12/31/2024
Dividend Yield:	16.0%	5 Year Price Target	\$2.63	Years Of Dividend Growth:	0
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

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 six industries, with the highest exposure in software and business services, at 36.1% and 29.1%, respectively. The company's assets have a gross investment value of \$262.9 billion in 63 positions, with 58% of debt securities being secured. OXSQ generated \$52 million in investment income last year and is based in Greenwich, Connecticut.

On November 5th, 2024, Oxford Square reported its Q3 results for the period ending September 30th, 2024. For the quarter, the company generated about \$10.3 million of total investment income, down from \$11.4 million in the previous quarter. This was due to lower interest income from its debt investments and lower income from its securitization vehicles.

Further, the weighted average yield of the company's debt investments was 13.7% at current cost, down from 13.9% in the previous quarter. Still, the weighted average cash distribution yield of the company's cash income producing CLO equity investments at current rose notably from 13.7% to 14.5%. The weighted average effective yield of the company's CLO equity investments at current cost was 9.6%, about the same as in the previous quarter.

Total expenses, which primarily include interest paid on its own financing and managers' fees, amounted to \$4.2 million, \$0.5 million higher than Q2-2024. Thus, net investment income, NII (the net investment income) was \$6.2 million, down \$1.5 million sequentially. On a per-share basis, NII came in at \$0.10. Net asset value (NAV) per share was \$2.35 versus \$2.43 last quarter. Based on the company's current portfolio composition, we now forecast a FY2024 IIS of \$0.46.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
IIS¹	\$1.17	\$0.66	\$0.52	\$0.60	\$0.67	\$0.81	\$0.40	\$0.32	\$0.42	\$0.51	\$0.46	\$0.38
DPS	\$1.19	\$1.13	\$1.15	\$0.80	\$0.79	\$0.80	\$0.61	\$0.42	\$0.42	\$0.54	\$0.42	\$0.36
Shares²	58.8	59.8	51.9	51.5	49.7	47.8	49.4	49.6	49.8	59.3	64.8	75.0

The company's investment income per share has been declining at a 10-year CAGR of 8.8%, as Oxford Square has been failing when it comes to refinancing its investment at attractive yields, resulting in declining investment spreads. Further, the company has been historically over-distributing dividends to shareholders, decaying its NAV, and hence its future income generation due to fewer assets.

Rising interest rates should help boost the company's results in the medium-term. Still, with the company's investments declining in value and a generally falling NAV creating a downward spiral on reinvested capital, income generation could further decline. Hence, we expect a -4% IIS/share decline in the medium-term. As has been the case in the past several times, we expect further dividend cuts over the medium-term due to their barely sustainable levels. We have embedded

¹ Investment Income per share

² Share count is in millions.

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a -3% distribution decline on an annualized basis in our estimates as a result. Since 2019, the company has switched its distributions' frequency from quarterly to monthly.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	8.1	10.5	11.1	11.3	10.6	7.9	7.0	13.8	10.8	5.3	5.7	7.0
Avg. Yld.	11.5%	18.3%	19.9%	11.2%	12.2%	12.9%	21.0%	9.5%	12.2%	20.2%	16.0%	13.7%

As per the company's goal and obligation (as 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 15% over the past decade. Despite management's latest distribution slash to a monthly \$0.035 payout, the stock has declined enough to push the current yield to 16%. We believe a valuation multiple of 7.0x adequately reflects the stock's risk/reward profile. OXSQ is better valued through its book value, which currently stands at \$2.35, lower than the stock's price of \$2.63. This is likely because investors expect a rebound in NAV following higher NII. It could be the case in the short-term, but believe the long-term trend of NAV deterioration will last. We remind that NAV/share stood at \$5.03, \$4.92, \$4.65, \$3.67, \$3.34, and \$2.78 in Q3-2021, Q4-2021, Q1-2022, Q2-2022, Q3-2022, and Q4-2022 respectively.

Safety, Quality, Competitive Advantage, & Recession Resiliency

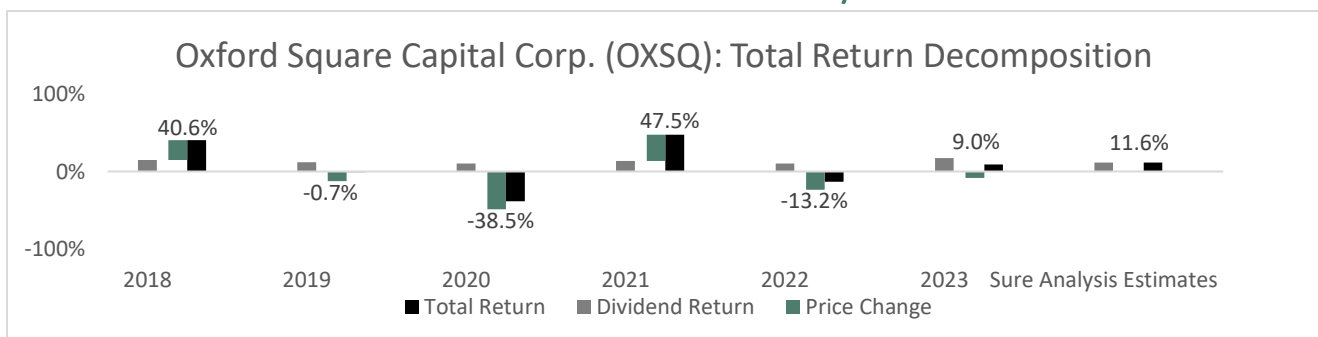
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	102%	171%	221%	133%	118%	99%	153%	131%	100%	106%	91%	96%

OXSQ's payout ratio has often been above 100% over the years, as management has historically paid investors more than what the company earned. While the stock's distribution 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 total investment income declining over time amid a shrinking investment portfolio, we can hardly see any reversal from the current predicament. The ongoing shareholder value deterioration trend does not seem to be nearing an end-, at least not anytime soon. 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. could benefit from rising yields in the short-term, but it is likely to continue deteriorating shareholders' equity value over the medium-term. Thus, another distribution reduction should not surprise investors. Regardless, we project an annualized total return potential of 11.6% in the medium-term. This is because our weakening earnings and distribution estimates could be more than offset by the current yield and the possibility of a soft multiple expansion. Therefore, we have set our rating to a speculative buy. Still, we highlight that income investors should not rely on Oxford Square's distributions.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	23.88	-57.03	121.57	49.41	-5.52	-28.74	5.54	44.9	(81)	22.6
SG&A Expense	25.08	7.61	10.06	4.66	2.56	2.98	2.91	3.35	3	3
Net Income	-3.35	-66.13	110.36	43.61	-9.21	-32.80	1.71	39.58	(86)	17
Net Margin	-14.0%	---	90.8%	88.3%	---	---	30.9%	88.2%	(106%)	75.2%
Free Cash Flow	-53.01	243.81	182.91	217.63	-33.86	47.76	95.05	-107.4	20	66

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	1042.6	718.3	612.5	454.1	467.1	385.3	357.7	433.5	328	278
Cash & Equivalents	20.5	23.2	8.3	30.0	13.9	14.4	59.1	9.0	9.0	5.7
Total Liabilities	521.8	357.4	226.5	65.7	152.4	137.3	132.2	188.9	189.3	126
Accounts Payable	20.1	6.3	1.7	0.0	0.5	0.6	23.6	1.2	1.2	1.2
Long-Term Debt	501.1	347.7	220.0	62.3	148.2	134.4	106.9	185.4	186	123
Total Equity	520.8	360.9	386.0	388.4	314.7	248.0	225.4	244.6	139	151
LTD/E Ratio	0.96	0.96	0.57	0.16	0.47	0.54	0.47	0.76	1.34	0.81

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	-0.3%	-7.5%	16.6%	8.2%	-2.0%	-7.7%	0.5%	10.0%	(22.5%)	5.7%
Return on Equity	-0.6%	-15.0%	29.6%	11.3%	-2.6%	-11.7%	0.7%	16.8%	(44.7%)	11.9%
ROIC	-0.3%	-7.6%	16.8%	8.3%	-2.0%	-7.8%	0.5%	10.4%	(22.7%)	5.8%
Shares Out.	68.86	69.79	61.77	51.48	49.66	47.76	49.48	49.62	49.76	53.9
Revenue/Share	0.35	-0.82	1.97	0.96	-0.11	-0.60	0.11	0.88	(1.64)	0.42
FCF/Share	-0.77	3.49	2.96	4.23	-0.68	1.00	1.92	(2.17)	0.41	1.22

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

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