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OxySure (OXYS) Improves Bottom Line as It Ramps Up Revenues

OxySure Systems Inc. (OTCBB: OXYS), a medical technology company focused on the design, manufacture and distribution of specialty medical and respiratory solutions recently reported its second quarter financial results.

Digging a little deeper into the company's latest quarterly report shows some real bottom line improvements. The company continued its trend towards a cash flow breakeven point, while its balance sheet also showed great improvement. And as the company's distribution agreements kick in, investors could see significant upside in the third quarter.

March Towards Profitability

OxySure has been steadily marching towards a cash flow breakeven point and profitability over the past several quarters. Operating cash flow is an important line item to watch because net income can include non-cash charges, such as depreciation. The metric can also provide insight into a company's ability to generate free cash flow and its future need for financing.

For the six months ended June 30, 2012, the company's net cash used in operating activities fell 46.5% to just $182,273 from $340,545 during the six months ended June 30, 2011. The improvement stemmed largely from lower interest expenses in connection with convertible notes, which fell 75% from $209,429 during the second quarter of 2011 to just $52,306 last quarter, according to the firm's 10-Q filing with the SEC.

The dramatic improvement in operating cash flow suggests a couple things. First, the company is in a stronger bargaining position in relation to growth financing, since it's using up less cash from operations and therefore less reliant on outside capital sources. And second, reaching a cash flow breakeven point sooner than expected means that net income and profitability may be just around the corner, unlocking significant value for shareholders.

Friendly Debt Ownership

OxySure's balance sheet may be somewhat misunderstood by investors, given its current ratio of less than 0.10x. A current ratio above 1.0x is normally the desired metric by investors. But in the company's case, friendly insiders control nearly three-quarters of its debt, charge no interest rate, and are willing to restructure, if necessary, making it better than most debt.

CEO Julian Ross's JTR Investments Ltd. owns the largest note payable valued at $1,018,656 with a 0% interest rate. JTR Investments Ltd also owns a second note in the amount of $250,000, also with a 0% interest rate. Agave Resources LLC, controlled by OxySure Director Donald Reed, owns another large note payable valued at $750,000 with a 0% interest rate. Combined, these insider-owned notes payable represent in excess of $2.0 million, or in excess of 80% of the total notes payable on the balance sheet.

It should also be noted that the other significant note holder, Sinacola Commercial Properties, Limited, the company's landlord, is also an equity stockholder of the company. Sinacola owns approximately $420,815 in convertible notes as at June 30, 2012. In May 2012 Sinacola converted $251,407 in convertible notes into common stock at an aggregate conversion price of approximately $1.10 per share. It appears that Sinacola's interests are significantly aligned with those of investors.

Finally, it should be noted that the company entered into a moratorium agreement with Vencore Solutions, LLC, in terms of which the maturity $307,662 of the company's leases were effectively postponed until July 1, 2013. Therefore, a true adjustment of the current ratio calculation as at June 30, 2012 should exclude the amount of $307,662.

If the "friendly notes" are excluded from the current ratio calculation, and the effect of the Vencore moratorium is taken into account, the adjusted current ratio becomes a much more respectable .37X. Further, the working capital deficit becomes a much more respectable $470,371.

In addition to the much lower realistic risk of default, the willingness of management and directors to invest their own money into the company also represents a vote of confidence. Some empirical studies have suggested that greater insider ownership has a positive effect on corporate performance through effective cost controls and more prudent decision-making.

Less Future Dilution

OxySure's number of outstanding warrants and stock options also decreased significantly last quarter, which is good news for existing shareholders looking to avoid dilution to their common stock. While the company has largely avoided the effects of dilution in the past, the most recent reduction in outstanding warrants and stock options limits future dilution to shareholders.

Last quarter, the number of outstanding warrants fell 36% to about 1.9 million, while the number of outstanding stock options fell about 25% to around 1.5 million, compared to a year ago. Meanwhile, common shares issuable upon conversion of convertible preferred stock fell even more dramatically by 64% to 1.3 million and convertible note shares out dropped 26% to about 1.7 million over the same period.

Ramping up Revenues

Last quarter, OxySure reported revenues that increased 126% over the first quarter and were roughly in-line with year ago results from the second quarter of 2011. Cost of goods sold (COGS) also moved in the right direction with a roughly 20% reduction year over year. Combined, these trends suggest that the company has been successful in ramping up its revenues.

The company also announced a number of significant distribution agreements recently. For instance, in June, the company signed an agreement with Systemax's Global Industrial. These agreements can take some time to move into full effect, but management believes that tangible results in connection with these agreements could be seen as soon as the third quarter of this year.

The company's business model also supports increasing revenues over time. After placing the OxySure Model 615 units, the cartridges must be replaced after use or expiration, whichever happens sooner. The company has seen a positive trend in cartridge replacement, especially in schools. For example, some school districts consume as many as 20 to 30 cartridges per month, especially during periods when seasons change, or when school starts up, or when athletic season starts up. The result is a recurring revenue model that builds revenues over time, even without significantly increasing the existing customer base.

And finally, the company benefits from both enormous end markets, ranging from schools to recreational vehicles, and more frequent usage than AEDs or fire extinguishers. For example, independent reports show that OxySure is 300X more likely to be needed versus an AED.

Great Investment Opportunity

OxySure Systems Inc. (OTCBB: OXYS) represents a great investment opportunity at its current levels. With a market capitalization of just $18 million, the company trades at just a fraction of its potential valuation over the coming years. Meanwhile, the firm's recent financial reports outline significant bottom line improvements that greatly enhance shareholder value.

For more information, please see the following resources:

- BiotechStockTrader: Hosted Article
- OxySure Website
- Recent SEC Filings for OXYS

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Forward-Looking Statements

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