

CAPITAL SOUTHWEST CORP

Form 497AD

August 07, 2018



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CSWC Company Overview CSWC is a middle market lending firm focused on supporting the acquisition and growth of middle market companies across the capital structure • CSWC was formed in 1961, and elected to be regulated as a BDC in 1988 •

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Publicly traded on Nasdaq: Common Stock ("CSWC") and December 2022 Notes ("CSWCL") • Internally Managed BDC with RIC tax treatment for tax purposes •  
December 2014 announced intent to spin off of industrial growth company ("CSW Industrials"; Nasdaq: CSWI) tax free •  
January 2015 launched credit investment strategy • September 2015 completed tax free spin off of CSWI • 20 employees based in Dallas, Texas •  
Total Balance Sheet Assets of \$451 MM as of June 30, 2018 • Manage I 45 Senior Loan Fund ("I 45 SLF") in partnership with Main Street Capital (Nasdaq: "MAIN")  
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Q1 2019 Highlights Financial Highlights • Q1 2019 Pre Tax Net Investment Income (“NII”) of \$5.0 MM or \$0.31 per share •  
Announced Supplemental Dividend Program \$0.60 per share Supplemental Dividend paid during the quarter

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Expect to pay \$0.10 per share Supplemental Dividend per quarter going forward, subject to approval by the Board of Directors •  
Total Annualized Earnings Return on Equity of 15.1% for the quarter • Investment Portfolio at Fair Value increased to \$411 MM from \$393 MM in prior quarter  
\$66.9 MM committed in three new originations and three additions \$39.9MM proceeds received from three portfolio exits •  
Received \$2.2 MM dividend from I 45 SLF, an effective yield of 13.1% at fair value •  
\$145 MM available on Credit Facility and \$12.5 MM in cash and cash equivalents as of quarter end •  
Sold a total of 474,950 of our December 2022 Notes through our At The Market (“ATM”) Program from inception in June 2018 through August 3, 2018  
Gross proceeds of \$12.0 MM at an effective yield of 5.88% Page 5

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Track Record of Dividend and NAV Growth Continues • In the last twelve months ending 6/30/18, CSWC generated \$1.11 per share in Pre Tax NII and paid out \$1.07 per share in regular dividends LTM Regular Dividend coverage of 104% of Pre Tax NII

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Ten consecutive quarters of regular dividend per share growth •

Announced Supplemental Dividend Program in 6/30/18 quarter and paid a Supplemental Dividend of \$0.60 per share, generated primarily from realized gains •

Expect to pay \$0.10 per share Supplemental Dividend per quarter going forward, subject to Board approval •

Adjusted NAV (excluding Supplemental Dividends) increased to \$19.73 per share at 6/30/18 from \$19.34 per share at 3/31/18 19.7 % 6.6 % 6.3% 5.6 % 5.2 %  
10.6% 4.2 % 3.0 % 1.8 % 1.2 % Dividend Yield –Quarterly Annualized Total Dividend / CSWC Share Price at Qtr. End

Note: Adjusted NAV per Share calculation adds back all Supplemental Dividends paid Page 6

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Two Pronged Investment Strategy CORE: Lower Middle Market (“LMM”): CSWC led or Club Deals • Companies with EBITDA between \$3 MM and \$15 MM • Typical leverage of 2x –4x Debt to EBITDA through CSWC debt • Commitment size up to \$25 MM with hold sizes generally \$10 MM to \$20 MM •

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Both Sponsored and Non-sponsored deals • Securities include first lien, unitranche, second lien and subordinated debt •  
Frequently make equity co-investments alongside CSWC debt OPPORTUNISTIC: Upper Middle Market (“UMM”): Syndicated or Club, First and Second Lien •  
Companies typically have in excess of \$50 MM in EBITDA • Typical leverage of 3x –5.5x Debt to EBITDA through CSWC debt position •  
Hold sizes generally \$5 MM to \$15 MM • Floating Rate first and second Lien debt securities • More liquid assets relative to Lower Middle Market investments •  
Provides flexibility to invest/divest opportunistically based on market conditions and liquidity position Page 7

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Strong Quarter of CSWC Originations \$66.9 MM in new committed investments during the quarter (\$53.3 MM funded at close) at a weighted average debt YTM of 11.1% Q1 2019 Portfolio Originations Unfunded Total Debt Total Equity Commitments Funded at Close

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Funded at Close at Close Debt Spread over Debt Yield to Name Industry Type Market (in \$000s) (in \$000s) (in \$000s) LIBOR Maturity 1st Lien / RLOC  
 Gauge American Nuts (1) Food, Agriculture & Beverage LMM \$20,656 \$3,000 \$2,969 8.00% 11.3% / DDTL / Equity Environmental Pest Service  
 Consumer Services 1st Lien / DDTL LMM \$16,250 \$0 \$7,000 7.25% 10.4% Fast Sandwich Restaurants 1st Lien / RLOC LMM \$3,800 \$0 \$3,650 9.00% 12.1%  
 Delphi Add On Healthcare Services 1st Lien UMM \$5,000 \$0 \$0 7.50% 10.5% Media, Marketing & 1st Lien / Elite SEM Add On LMM \$2,500 \$111 \$0 8.42%  
 12.8% Entertainment Equity ITA Term Loan B Add On Transportation & Logistics 1st Lien LMM \$2,000 \$0 \$0 8.50% 11.6% Total \$50,206 \$3,111 \$13,619  
 11.1% 1. Gauge American Nuts amounts include a \$3.5 MM revolving loan, consisting of \$2.5 MM funded at closing and \$1 MM commitment  
 available to company. Subsequent to quarter end, the revolving loan was refinanced by a traditional revolving lender. As of July 31, 2018,  
 CSWC had \$18.1 MM funded on the 1st Lien Term Loan and a delay draw commitment of \$2 MM to fund an earn out to sellers based on  
 certain EBITDA growth targets. Note: Market refers to Upper Middle Market ("UMM") and Lower Middle Market ("LMM") Page 8

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CSWC Portfolio Prepayments and Exits Prepayments and exits continue to demonstrate our track record of generating attractive risk adjusted returns on shareholders' capital • During the quarter, we received \$39.9 MM in proceeds from two Lower Middle Market

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exits and one Upper Middle Market prepayment, generating a weighted average IRR of 23.6% •

Cumulative IRR of 17.2% on 22 portfolio exits generating \$162 MM in proceeds since launch of credit strategy in January 2015 Q1 2019 Portfolio Exits

Proceeds	Realized Gain	Name	Industry	Type	Market	(in \$000s)	(in \$000s)	IRR	
		TitanLiner	Energy	(Upstream)	Equity	LMM	\$24,779	\$18,620	28.9%
		Wastewater Specialties	Industrial Services	1st Lien	LMM	\$10,139	\$138	16.6%	
		Pre Paid Legal Services	Consumer Services	2nd Lien	UMM	\$5,000	\$31	11.6%	
Total / Wtd. Avg.		\$39,918	\$18,789	23.6%	Note: Market refers to Upper Middle Market ("UMM") and Lower Middle Market ("LMM")				

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CSWC Portfolio Asset Mix by Market Maintaining appropriate portfolio leverage while receiving attractive risk adjusted returns  
Investment Portfolio Statistics at 6/30/18 Lower Middle Upper Middle (In Thousands) Market (1) Market Number of Portfolio Companies 19 10 Total Cost

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\$227,901 \$73,033 Total Fair Value \$271,373 \$73,382 Average Hold Size (at Cost) \$11,995 \$7,303 % First Lien Investments (at Cost) 78.2% 75.2%  
% Second Lien Investments (at Cost) 0.0% 24.8% % Subordinated Debt Investments (at Cost) 8.3% 0.0% % Equity (at Cost) 13.5% 0.0% Wtd. Avg. Yield (2)(3)  
12.0% 10.5% Wtd. Avg. EBITDA of Issuer (\$MM's) (3) \$8.6 \$81.2 Wtd. Avg. Leverage through CSWC Security (3) (4) 3.4x 4.0x

Note: All metrics above exclude the I 45 Senior Loan Fund 1. At June 30, 2018, we had equity ownership in approximately 73.7% of our LMM investments 2.

The weighted average annual effective yields were computed using the effective interest rates for all debt investments at cost as of June 30, 2018, including accretion of original issue discount but excluding fees payable upon repayment of the debt instruments and any debt investments on non accrual status. As of June 30, 2018, there were no investments on non accrual status. Weighted average annual effective yield is higher than what an investor in shares in our common stock will realize on its investment because it does not reflect our expenses or any sales load paid by an investor. 3.

Weighted average metrics are calculated using investment cost basis weighting 4.

Includes CSWC debt investments only. Calculated as the amount of each portfolio company's debt (including CSWC's position and debt senior or pari passu to CSWC's position, but excluding debt subordinated to CSWC's position) in the capital structure divided by each portfolio company's adjusted EBITDA. Management uses this metric as a guide to evaluate relative risk of its position in each portfolio debt investment Page 10

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Robust Lower Middle Market First Lien Credit Portfolio CSWC Credit Portfolio continues to migrate to LMM and First Lien Investments •  
LMM Investments have increased to 73% of the credit portfolio at 6/30/18 from 18% at 6/30/16 •

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First Lien Investments have increased to 86% of the credit portfolio at 6/30/18 from 42% at 6/30/16 Robust LMM Credit Portfolio Growth  
Credit Portfolio Heavily Weighted to First Lien Page 11

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Interest Rate Sensitivity Debt Portfolio Exposure at 6/30/18 Well Positioned for Rising Interest Rate Environment Fixed vs. Floating Portfolio Composition (1)  
Illustrative      Illustrative      Change in Base Interest Rates NII Change (\$'s) NII Change (Per Share) (50bps) (\$1,250,241) (\$0.08) 50 bps \$1,271,182

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\$0.08 100bps \$2,542,364 \$0.16 150bps \$3,813,547 \$0.24 200bps \$5,084,729 \$0.31

(1) Portfolio Composition includes I 45 assets pro rata as a % of CSWC's equity investment in the fund

Note: Illustrative change in NII is based on a projection of CSWC's existing debt investments as of 6/30/18, adjusted only for changes in Base Interest Rate. Base Interest Rate used in this analysis is 3 Month LIBOR of 2.34% at 6/30/18. The results of this analysis include the I 45 Senior Loan Fund, which is comprised of 100% floating rate assets and liabilities. Page 13

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(In Thousands) 9/30/2017 12/31/2017 3/31/2018 6/30/2018 Total Debt Investments at Fair Value \$223,807 \$217,964 \$220,807 \$228,468 Number of Issuers  
46444345 Wtd. Avg. Issuer EBITDA \$79,009 \$73,392 \$73,995 \$72,607 Avg. Investment Size as a % of Portfolio 2.2% 2.3% 2.3% 2.2%  
Wtd. Avg. Net Leverage on Investments (1) 3.5x 3.3x 3.6x 3.7x Wtd. Avg. Yield 7.7% 7.4% 7.5% 7.7% Wtd. Avg. Duration (Yrs) 4.8 4.7 4.6 4.5  
(1) Through 1 45 Security Page 14

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Income Statement Quarter Ended Quarter Ended Quarter Ended Quarter Ended (In Thousands, except per share amounts) 9/30/17 12/31/17 3/31/18 6/30/18  
Investment Income Interest Income \$5,282 \$5,566 \$6,575 \$7,643 Dividend Income \$3,088 \$3,149 \$3,069 \$3,075 Fees and Other Income \$139 \$304 \$230

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\$389	Total Investment Income	\$8,509	\$9,019	\$9,874	\$11,107	Expenses	Cash Compensation	\$1,606	\$1,885	\$1,884	\$1,910	Share Based Compensation		
\$384	\$479	\$477	\$475	General & Administrative	\$1,364	\$907	\$1,086	\$1,353	Spin off Related Expenses	\$173	\$172	\$0	\$0	Total Expenses (excluding Interest)
\$3,527	\$3,443	\$3,447	\$3,738	Interest Expense	\$911	\$1,275	\$1,951	\$2,373	Pre Tax Net Investment Income	\$4,071	\$4,301	\$4,476	\$4,996	
				Taxes and Gain / (Loss)	Income Tax Benefit (Expense)	(\$134)	\$362	(\$279)	(\$379)	Net realized gain (loss) on investments	\$210	\$617	\$131	\$18,819
					Net increase (decrease) in unrealized appreciation of investments	\$4,496	\$4,963	\$10,649	(\$11,783)					
				Net increase (decrease) in net assets resulting from operations	\$8,643	\$10,243	\$14,977	\$11,653	Weighted Average Diluted Shares Outstanding	16,078	16,176			
					16,139	16,201	Pre Tax Net Investment Income Per Dil. Weighted Average Share	\$0.25	\$0.27	\$0.28	\$0.31	Page 15		

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Balance Sheet Quarter Ended Quarter Ended Quarter Ended Quarter Ended (In Thousands, except per share amounts) 9/30/2017 12/31/2017 3/31/2018  
6/30/18 Assets Portfolio Investments \$321,860 \$367,120 \$393,095 \$411,330 Cash & Cash Equivalents \$33,329 \$20,527 \$7,907 \$12,532

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Deferred Tax Asset \$1,846 \$2,080 \$2,050 \$2,116 Other Assets \$11,635 \$13,123 \$14,438 \$24,948 Total Assets \$368,670 \$402,850 \$417,490 \$450,926  
Liabilities December 2022 Notes \$0 \$55,236 \$55,305 \$56,646 Credit Facility \$56,000 \$35,000 \$40,000 \$65,000 Other Liabilities \$20,156 \$14,084 \$13,897  
\$21,899 Total Liabilities \$76,156 \$104,320 \$109,202 \$143,545 Shareholders Equity Net Asset Value \$292,514 \$298,530 \$308,288 \$307,381  
NAV per Share \$18.26 \$18.44 \$19.08 \$18.87 Debt to Equity 0.19x 0.30x 0.31x 0.40x Page 16

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Portfolio Statistics Continuing to build a well performing credit portfolio with no non-accruals Quarter Ended Quarter Ended Quarter Ended Quarter Ended  
(In Thousands) 9/30/2017 12/31/2017 3/31/2018 6/30/18 Portfolio Statistics Fair Value of Debt Investments \$187,316 \$226,441 \$239,122 \$272,133

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Average Debt Investment Hold Size \$7,805 \$8,709 \$9,197 \$9,719 Fair Value of Debt Investments as a % of Par 99% 99% 99% 99%  
% of Debt Portfolio on Non Accrual (at Fair Value) 0.0% 0.0% 0.0% 0.0% Weighted Average Investment Rating (1) 2.0 2.0 2.0 2.0  
Weighted Average Yield on Debt Investments 10.71% 10.95% 11.46% 11.73% Total Fair Value of Portfolio Investments \$321,860 \$367,120 \$393,095  
\$411,330 Weighted Average Yield on all Portfolio Investments (2) 10.65% 10.55% 10.48% 10.60% Investment Mix (Debt vs. Equity) (3) (4) 74% / 26%  
75% / 25% 73% / 27% 79% / 21% Investment Mix (Yielding vs. Non Yielding) (4) 94% / 6% 94% / 6% 92% / 8% 94% / 6% (1) CSWC utilizes an internal 1  
4 investment rating system in which 1 represents material outperformance and 4 represents material underperformance. All new investments are initially set to 2  
(2) Includes dividends from Media Recovery, Inc. and I 45 Senior Loan Fund (3) Excludes CSWC equity investment in I 45 Senior Loan Fund (4) At Fair Value  
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Significant Unused Debt Capacity with Long Term Duration Earliest Debt Maturity occurs in November 2021 Facility Total Commitments Interest Rate Maturity  
Principal Drawn Credit Facility(1) \$210.0 MM L + 3.00% with Step Down November 2021 \$65.0 MM December 2022 Notes \$58.9 MM 5.95% December 2022

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\$58.9 MM (NASDAQ: "CSWCL") (2) (1)

The facility has an accordion feature which allows for an increase in total commitments up to \$250.0 MM. Principal Drawn is based upon outstanding balances as of June 30, 2018. (2)

Redeemable at CSWC's option beginning December 2019. Principal drawn is based upon outstanding balances as of June 30, 2018. Subsequent to quarter end, CSWC sold an additional 419,508 notes, bringing total gross proceeds from the ATM Program to \$12.0 MM as of August 3, 2018. Page 18

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Investment Income Detail Constructing a portfolio of investments with recurring cash yield •  
Non-Cash and Non-Recurring investment income remain a minor portion of Total Investment Income Quarter Ended Quarter Ended Quarter Ended

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Quarter Ended	(In Thousands)	9/30/17	12/31/17	3/31/18	6/30/18	Investment Income Breakdown	Cash Interest	\$5,082	\$5,357	\$6,300	\$7,324			
Cash Dividends	\$3,018	\$3,076	\$2,990	\$3,008	PIK Income	\$70	\$72	\$91	\$79	Amortization of purchase discounts and fees	\$200	\$209	\$264	\$312
Management/Admin Fees	\$139	\$146	\$184	\$181	Prepayment Fees & Other Income	\$0	\$159	\$45	\$203	Total Investment Income	\$8,509	\$9,019	\$9,874	\$11,107
Key Metrics	Cash Income as a % of Investment Income	97%	97%	96%	96%	% of Total Investment Income that is Recurring (1)	97%	95%	98%	97% (1) Non Recurring income principally made up of loan prepayment fees	Page 19			

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Key Financial Metrics Strong Earnings ROE as Portfolio continues to appreciate Quarter Ended Quarter Ended Quarter Ended Quarter Ended 9/30/2017  
12/31/2017 3/31/2018 6/30/18 Key Financial Metrics Pre Tax Net Investment Income Per Wtd Avg Diluted Share \$0.25 \$0.27 \$0.28 \$0.31

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Annualized Pre Tax Net Investment Income Return on Equity (ROE) 5.64% 5.82% 6.02% 6.46% Realized Earnings Per Wtd Avg Diluted Share \$0.26 \$0.33 \$0.27  
1.45 Annualized Realized Earnings ROE 5.75% 7.15% 5.82% 30.32% Earnings Per Wtd Avg Diluted Share \$0.54 \$0.63 \$0.93 \$0.72  
Annualized Earnings Return on Equity (ROE) 11.97% 13.87% 20.13% 15.08% Regular Dividends per Share \$0.24 \$0.26 \$0.28 \$0.29  
Supplemental Dividends per Share \$0.00 \$0.00 \$0.00 \$0.60 Total Dividends per Share \$0.24 \$0.26 \$0.28 \$0.89 Dividend Yield (1) 5.6% 6.3% 6.6% 19.7% (1)  
Dividend Yield is calculated as Quarterly Annualized Total Dividend / CSWC Share Price at Qtr. End Page 20

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