

Capital Southwest Corporation

The Internally Managed Advantage



Comprehensive Investment Analysis & Outlook (FY2026)

Executive Dashboard: Structural Alpha Meets Macro Headwinds



The Edge (Internal Structure)

- Internally Managed structure drives **~1.7% Operating Expense Ratio** (vs. Peers >3.0%)
- Result: A **200bps structural cost advantage** allows for lower asset risk with equivalent returns.



The Performance (Yield + Growth)

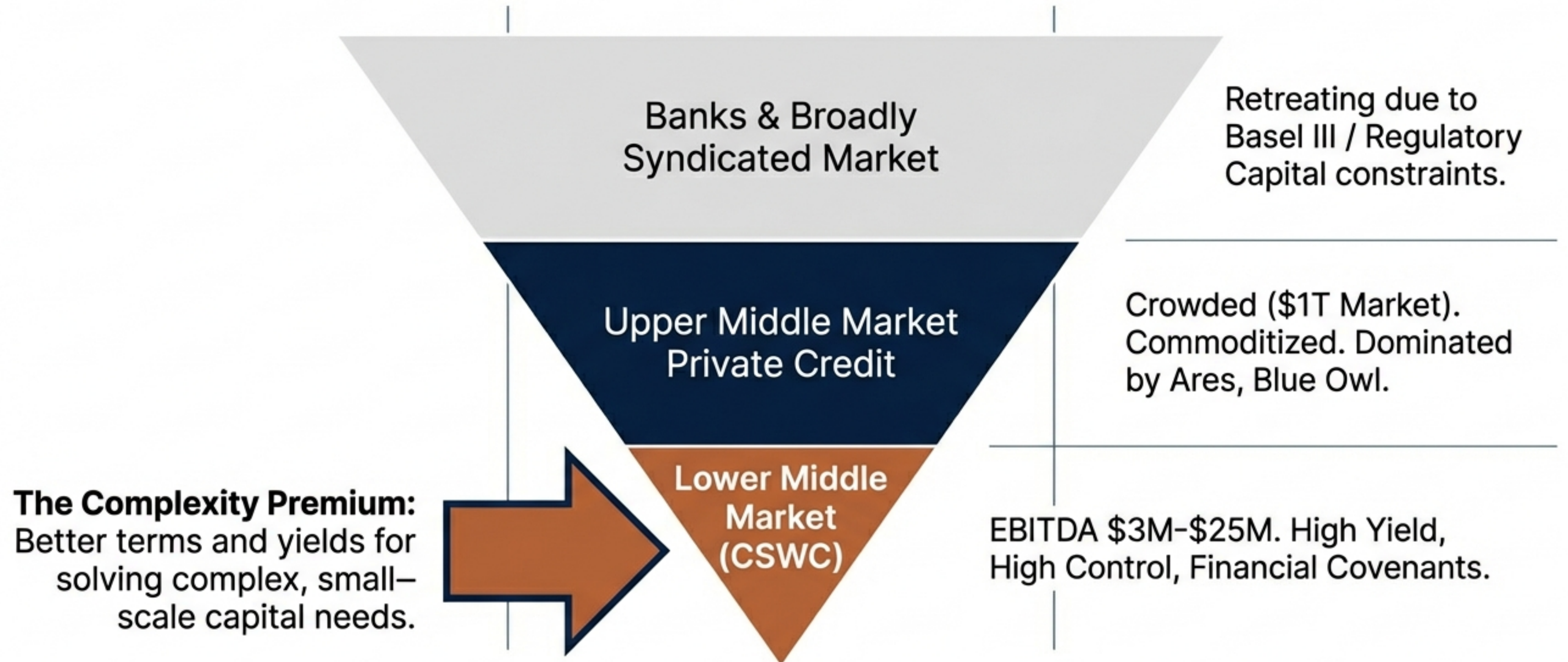
- Dividend Yield: **~11.2%** (Regular + Supplemental).
- Valuation: Trading at **~1.36x Premium to NAV**, validating the model.



The Risk (Cycle Pressure)

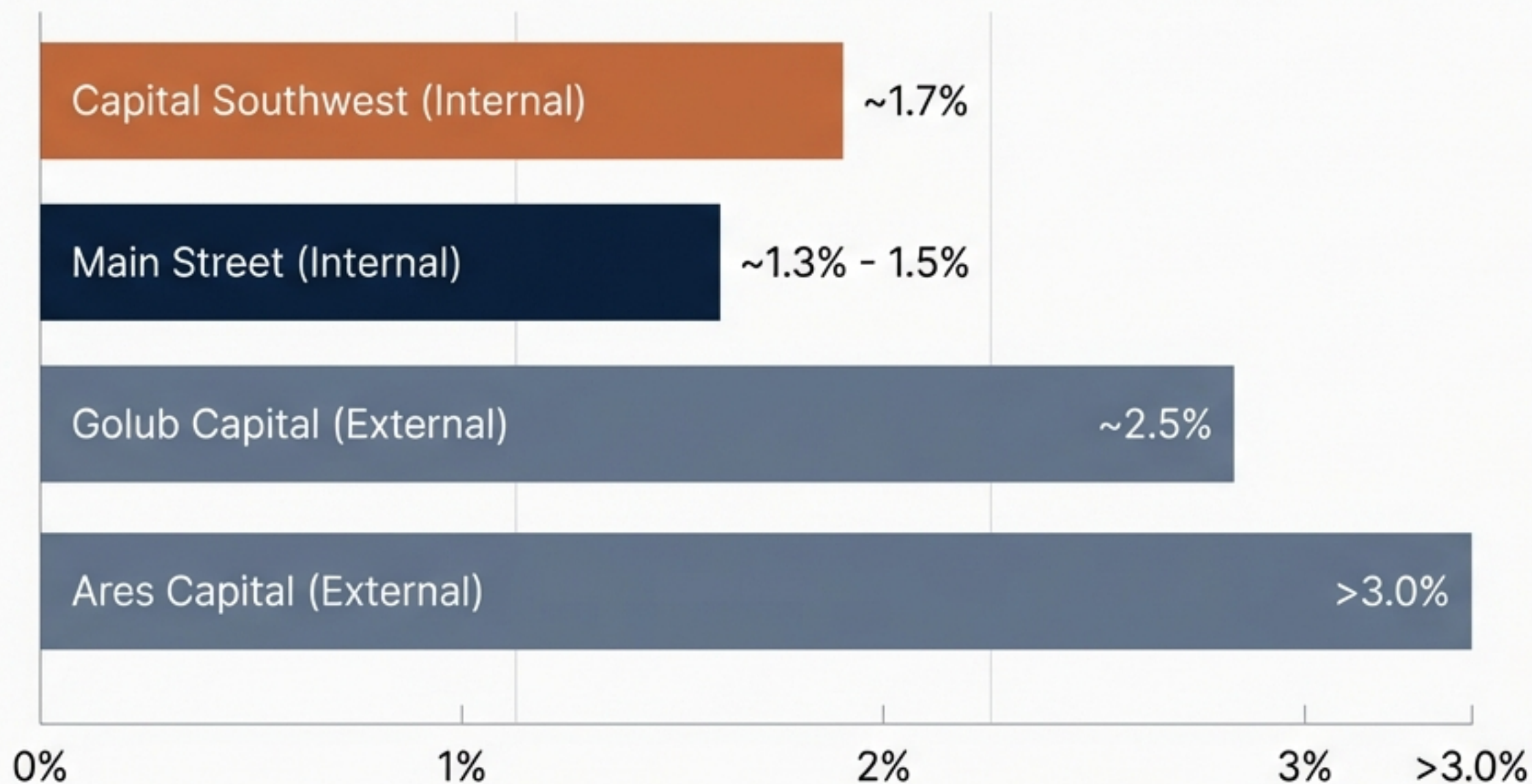
- Non-Accruals rising: Now **1.5%** of Fair Value (up from 0.8%).
- Interest rate cuts threaten **Net Investment Income** (99% floating rate assets).

Capturing the 'Complexity Premium' in the Lower Middle Market



The Crown Jewel: Internal Management Creates Operating Leverage

Operating Expense Ratios



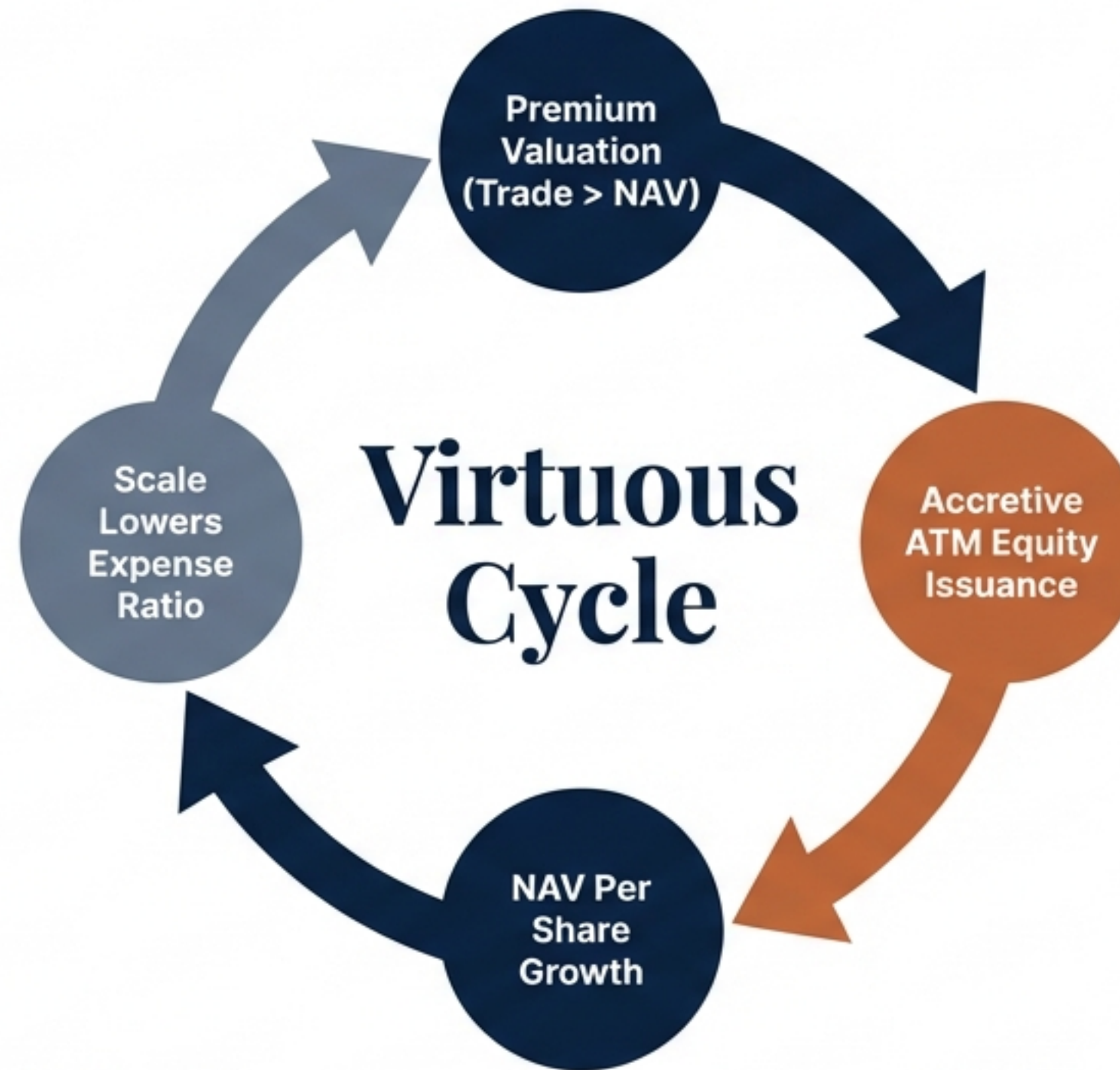
The 200bps Advantage

External managers charge 1.5% base fees + 20% incentive fees.

CSWC pays only actual overhead (salaries/rent).

This savings flows directly to shareholders.

The Valuation Flywheel: How Premium Valuation Drives NAV

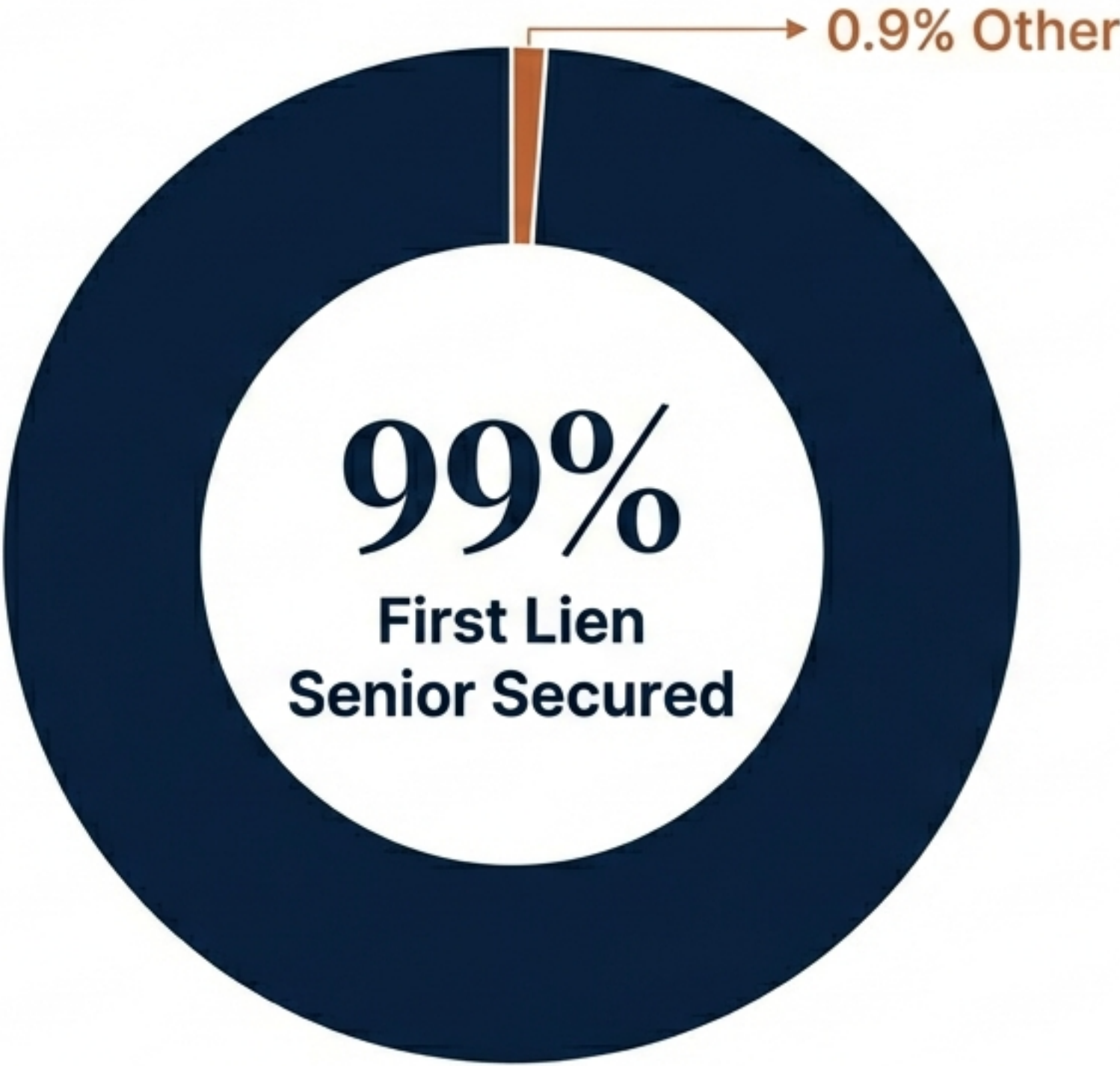


Q3 FY2026 Execution: Raised \$52.6M at ~127% of NAV.

Long Term Result: 5-Year NAV Growth from \$15.13 to \$16.75.

Defensive Architecture: Seniority with Granularity

Portfolio Composition



Diversity Metrics

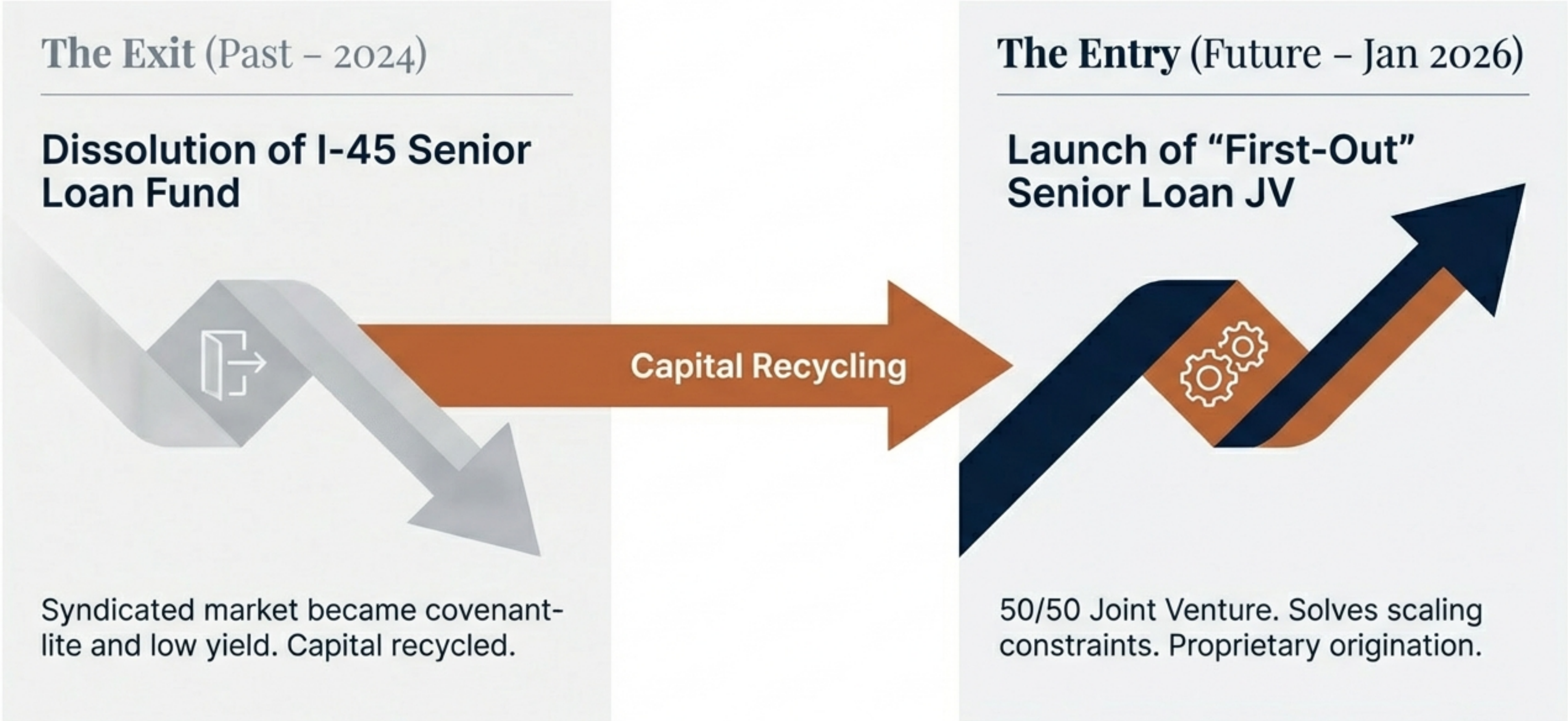
132
Portfolio Companies

0.9%
Average Position Size

11.3%
Weighted Average Yield

3.6x
Borrower Debt-to-EBITDA

Strategic Rotation: Exiting Commoditized Syndication for Proprietary Control



The New JV: Engineering Returns via Structural Leverage

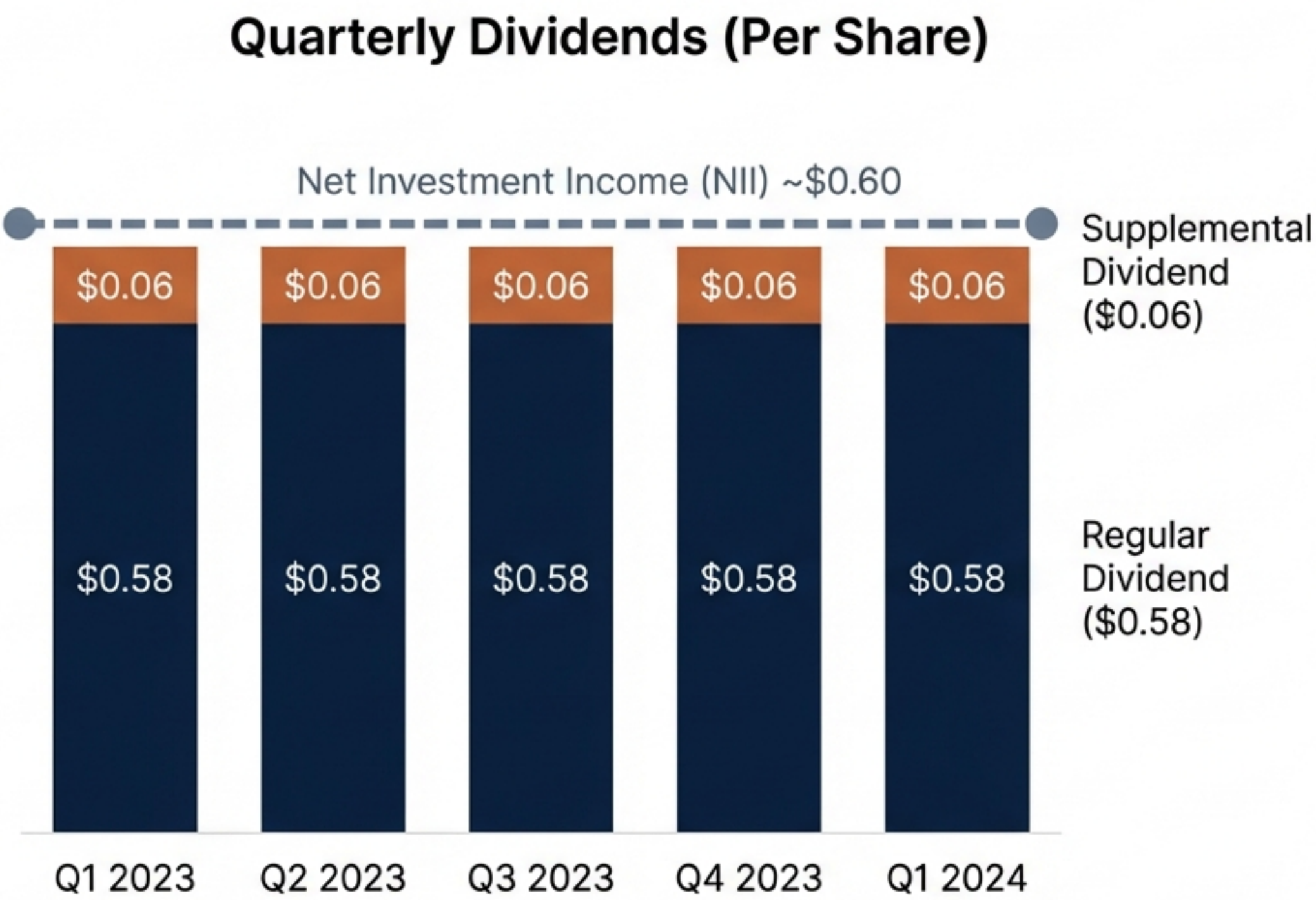
Capital Stack



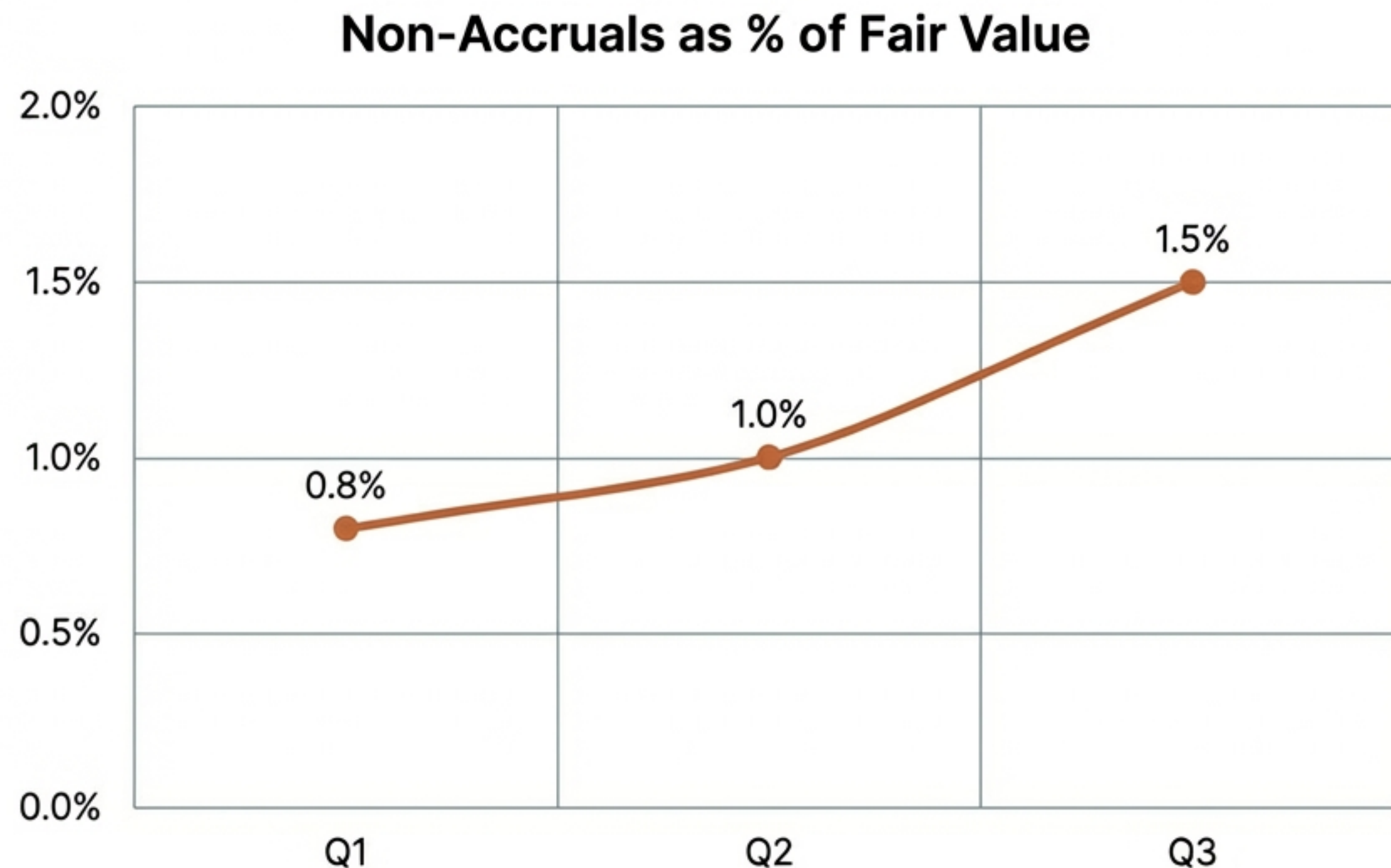
$$\text{Safe Assets} + 2.5x \text{ Fund Leverage} = \text{High Yield Equity} \text{ (~13-15\% ROE)}$$

Risk Note: Leverage transforms low-risk assets into high-beta equity. Asset impairments are magnified.

The Income Engine: Covered Dividends & The UTI Fortress



Credit Monitor: The 'Rate Hike Hangover' Emerges



The Trend: Borrowers stressed by prolonged high rates.

Analysis: 1.5% is manageable, but the velocity of increase is the primary risk.

Context: Portfolio Leverage at 3.6x Debt-to-EBITDA leaves little room for margin compression.

The Bear Case: Three Converging Headwinds

Rate Normalization



99% Floating Rate Assets.
As Fed cuts rates, interest income falls immediately.

Spread Compression



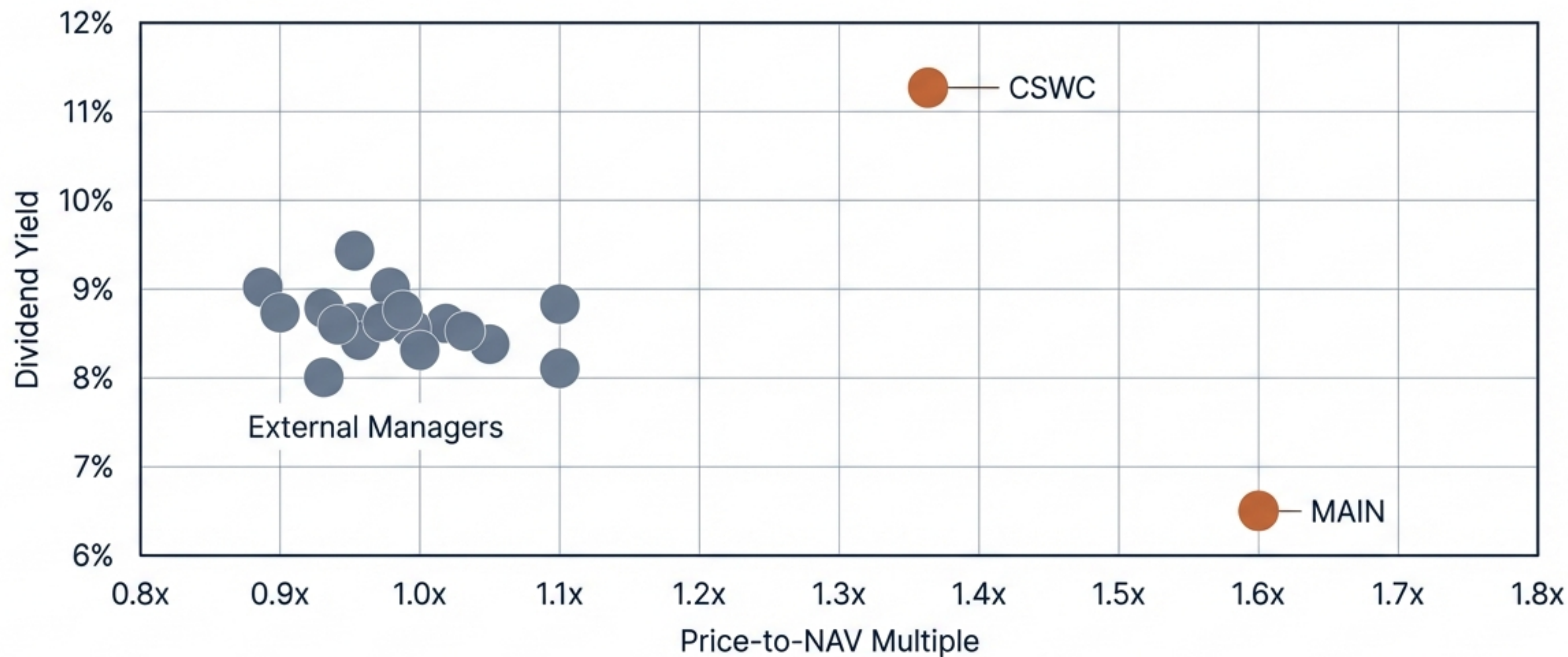
Too much dry powder (\$3T global private credit).
New commitment spreads compressed to ~6.4%.

Valuation Risk



Priced for perfection at 1.36x NAV. No margin of safety for execution errors.

Valuation Context: The 'Internal Management' Premium



Market prices the fee savings efficiently. Regression to the mean (1.15x) implies 15% downside risk.

Scenario Analysis: Navigating FY2027

Soft Landing (Base Case)	Hard Landing (Bear Case)	Status Quo
↓ Rates fall slowly. Credit holds.	⚡ Rates slashed. Spreads blow out. Non-accruals >3%.	— Rates higher for longer.
↓ Impact: NII covers Regular Dividend (\$0.58). Supplemental fades.	⚡ Impact: NAV erosion. Dividend cut likely. Multiple compression.	— Impact: Continued NII outperformance, but higher borrower stress.

Final Verdict: A Quality Hold Requiring Vigilance

The Bull View

- Structural cost advantage is permanent.
- UTI Reserve (\$1.02) protects the dividend.
- Proven capital allocators (exited I-45, accretive ATM use).

The Bear View

- Cycle has peaked (NII declining).
- Credit stress is rising (Non-accruals at 1.5%).
- Valuation offers no buffer.

**Bottom Line: Best-in-Class Structure, Priced for Perfection.
Monitor credit metrics closely in 2026.**

Appendix: Key Definitions & Terminology

NII (Net Investment Income): Core earnings from interest/fees, excluding capital gains.

RIC (Regulated Investment Company): Tax structure requiring 90% income distribution.

UTI (Undistributed Taxable Income): Spillover income kept in reserve to smooth dividends.

ATM (At-The-Market) Program: Method of issuing stock directly into the market at current prices.

First-Out / Last-Out: Tranches of senior debt; "First-Out" gets paid first (lower risk/yield).