



Capital Southwest Corporation (CSWC)

Updated February 4th, 2025 by Nikolaos Sismanis

Key Metrics

Current Price:	\$22.96	5 Year CAGR Estimate:	9.9%	Market Cap:	\$1.06 B
Fair Value Price:	\$23.70	5 Year Growth Estimate:	1.0%	Ex-Dividend Date:	03/14/2025
% Fair Value:	97%	5 Year Valuation Multiple Estimate:	0.6%	Dividend Payment Date:	03/31/2025
Dividend Yield:	10.1%	5 Year Price Target	\$25	Years Of Dividend Growth:	8 ¹
Dividend Risk Score:	F	Retirement Suitability Score:	C	Rating:	Buy

Overview & Current Events

Capital Southwest Corporation is an internally managed investment company that has elected to be regulated as a BDC (Business Development Company). The company specializes in providing customized debt and equity financing to lower middle market (LMM) companies and debt capital to upper-middle market (UMM) companies located primarily in the United States. Capital Southwest generates around \$82 million in annual revenues and is based in Dallas, Texas.

On February 3rd, 2025, Capital Southwest declared a base quarterly dividend of \$0.58 per share, and a supplemental dividend of \$0.06 per share. The base annualized dividend remains at \$2.32, which we have utilized in our estimates. Supplemental dividends are not included in our fiscal 2025 entry in the table below.

On the same day, Capital Southwest reported its fiscal Q3-2025 results for the period ending December 31st, 2024. Note that the company's fiscal year ends on March 31st. This applies to the figures depicted in our tables. Capital Southwest's total investment income was \$52.0 million, up from \$48.7 million in the prior quarter. The growth in investment income was primarily attributable to an increase in prepayment and other fees received during Q3. Still, the weighted average yield on debt declined sequentially, falling from 12.9% to 12.1%.

Pre-tax net investment income (NII) came in at \$30.7 million, up from \$30.0 million in Q2-2025. On a per-share basis, pre-tax net investment income fell from \$0.64 to \$0.67, however, due to a higher share count.

CSWC's credit portfolio currently consists of 125 lower and upper-middle-market companies. Most of its \$1.7 billion portfolio is allocated in 1st Lien secured debt. CSWC's investment portfolio is well-diversified and exposed to over 20 industries. Healthcare Services, Media & Marketing, and Food/Agriculture & Beverage, account for 13%, 8%, and 7% of the total holdings, respectively. For FY2025, we expect NII/share of \$2.37.

Growth on a Per-Share Basis

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030
NII	\$3.44	-\$0.76	\$0.61	\$1.02	\$1.48	\$1.68	\$1.79	\$1.90	\$2.30	\$2.72	\$2.37	\$2.49
DPS	\$0.20	\$0.14	\$0.79	\$0.99	\$2.27	\$2.75	\$2.05	\$2.52	\$2.28	\$2.47	\$2.32	\$2.44
Shares²	15.5	15.6	15.9	16.1	16.7	18	19	22.8	30	40.7	48.3	60.0

On September 30th, 2015, Capital Southwest completed the spin-off of CSW Industrials (CSWI). This explains the stock price's sudden "nosedive" around this period and the higher financials before the spin-off, as depicted in the table. The company's prolonged history as a BDC company and experienced management team have allowed it to sustain a double-digit investment yield most of the time. The company has refinanced its own loans at lower rates over time, resulting in higher net investment income. Additionally, with only 27 employees, operating expenses as a percentage of total assets have also been declining. They were 4.9% in FY2016, but are currently less than half this amount at 1.6%. In terms of the dividend, the company has been growing its base DPS annually since the spin-off in 2015. The higher dividends seen over the past few years are due to special dividends that the company can afford from additional gains (e.g., equity sales), which are not recorded as investment income. Hence, both the supplemental and special dividends

¹ Refers to the base dividend rate which excludes supplemental payouts.

² Share count is 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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are technically covered. We expect both NII/share and the base DPS to grow by around 1% in the medium-term. Higher interest rates currently benefit the company. Total dividends are likely to be higher amid one-off additional gains from equities, though since they are impossible to predict, we are not speculating higher figures.

Valuation Analysis

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Now	2030
Avg. P/E	14.5	---	26.6	18.9	14.4	12.5	12.8	12.1	8.3	7.6	9.7	10.0
Avg. Yld.	0.4%	1.0%	4.9%	5.1%	10.7%	13.1%	9.0%	10.9%	11.9%	12.0%	10.1%	9.8%

Capital Southwest is now trading at 9.7x our expected net investment income year. We believe this is a more-or-less fair multiple and it accounts for its operating excellence and resilient, cash-flow-producing investments, especially in today's market environment. At the current base DPS, the stock yields 10.1%, excluding any supplemental/special dividends. The actual yield should be higher when accounting for these additional payouts.

Safety, Quality, Competitive Advantage, & Recession Resiliency

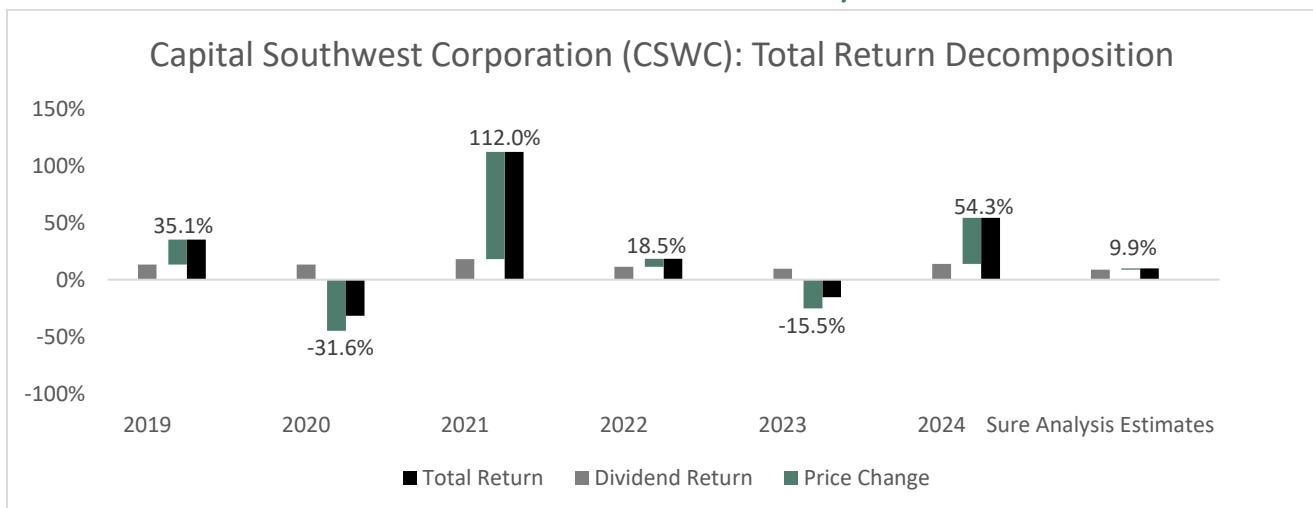
Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030
Payout	6%	---	130%	97%	153%	164%	115%	133%	99%	91%	98%	98%

Capital Southwest's dividend should be considered safer than its 98% payout ratio implies, considering the supplemental payouts, the special payouts, and the latest quarterly dividend increase. The payout ratio does not include the realized gains that are in the form of non-investment income, hence the abnormally high figures. Overall, the BDC's diversified portfolio has proven very resilient, even during COVID-19, when interest income remained robust. Considering 2015's spin-off transformed the company, this is the closest we can get to measure the company's recession resiliency, which could prove to be quite strong based on its 2020-2021 results. Being an investment company, Capital Southwest does not have a distinct competitive advantage compared to its peers other than management's experience.

Final Thoughts & Recommendation

Capital Southwest is a well-diversified business development company and one of the oldest ones in the market, having prospered through numerous cycles. Its financials have been growing fast following the 2015 spinoff, and its optimal financing costs have resulted in a prudent portfolio expansion. We forecast annualized returns of 9.9% in the medium-term, excluding any supplementary dividends, powered primarily by the stock's hefty dividend yield and our growth rates. We rate the stock as a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Revenue	119.7	65.8	14.4	38.4	53.2	48.9	-0.2	71.6	78.9	109.1
SG&A Exp.	2.8	5.8	11.4	4.4	4.4	4.8	5.6	5.2	2.5	9
D&A Exp.	0.0	0.1	0.1	0.5	0.9	1.4	2.4	2.0	2.2	---
Net Profit	112.0	53.4	-5.4	23.5	39.3	33.1	-22.4	50.9	42.8	83.4
Net Margin	93.6%	81.2%	N/A	61.1%	73.9%	67.6%	N/A	71.1%	54.2%	76.4%
Free Cash Flow	8.4	194.3	-111.5	-89.6	-63.9	-94.7	-47.9	-68.3	-184.7	---
Income Tax	-0.7	0.3	-1.3	2.1	0.1	0.9	6.2	4.7	4.0	1.2

Balance Sheet Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Total Assets	778.7	776.9	284.5	325.8	417.5	551.8	585.0	735.6	974	1,557
Cash & Equivalents	88.2	225.8	96.0	22.4	7.9	9.9	13.7	31.6	11.4	32.3
Total Liabilities	8.3	9.5	11.9	40.7	109.2	225.9	312.7	399.3	553	801
Long-Term Debt	0.0	0.0	0.0	25.0	95.3	216.1	303.3	381.3	529	771
Shareholder's Equity	770.4	767.4	272.6	285.1	308.3	326.0	272.2	336.3	421	756
LTD/E Ratio	0.0	0.0	0.0	0.1	0.3	0.7	1.1	1.1	1.27	1.02

Profitability & Per Share Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Return on Assets	15.5%	6.9%	-1.0%	7.7%	10.6%	6.8%	-3.9%	7.7%	5.0%	5.9%
Return on Equity	15.7%	7.0%	-1.0%	8.4%	13.2%	10.4%	-7.5%	16.7%	11.3%	12.4%
ROIC	15.7%	7.0%	-1.0%	8.1%	11.0%	7.0%	-4.0%	7.9%	5.1%	6.1%
Shares Out.	15.3	15.5	15.7	15.9	16.1	16.7	18.0	19.1	22.84	40.73
Revenue/Share	7.83	4.24	0.92	2.42	3.30	2.92	-0.01	3.76	3.46	2.68
FCF/Share	0.55	12.51	-7.09	-5.64	-3.96	-5.66	-2.66	-3.6	-8.09	---

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

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