Stellus Capital Investment Corp
Form 497
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PROSPECTUS SUPPLEMENT
(to Prospectus dated June 29, 2018)

2,750,000 Shares

Stellus Capital Investment Corporation

Common Stock

We are offering for sale 2,750,000 shares of our common stock. The underwriters have agreed to purchase shares of our common stock from us at a price of $14.43 per share which will result in approximately $38.6 million of net proceeds, after deducting estimated offering expenses, to us, or $44.4 million assuming full exercise of the underwriters option to purchase additional shares described below. We expect that our expenses for this offering will be approximately $135,000.

The underwriters may also exercise their option to purchase up to an additional 412,500 shares of common stock from us, at the price per share set forth above, for 30 days after the date of this prospectus supplement.

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company, or BDC, under the Investment Company Act of 1940, as amended, or the 1940 Act. Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation through debt and related equity investments in middle-market companies. The companies in which we invest are typically highly leveraged, and, in most cases, our investments in such companies will not be rated by national rating agencies. If such investments were rated, we believe that they would likely receive a rating below investment grade (i.e., below BBB or Baa), which are often referred to as junk.

Our common stock is listed on the New York Stock Exchange, or NYSE, under the trading symbol SCM. The last sale price, as reported on NYSE on March 13, 2019, was $14.68 per share. The net asset value per share of our common stock at December 31, 2018 (the last date prior to the date of this prospectus supplement on which we determined net asset value) was $14.09.

Shares of closed-end investment companies, including BDCs, frequently trade at a discount to their net asset value. If our shares trade at a discount to our net asset value, it will likely increase the risk of loss for purchasers in this offering.

This prospectus supplement and the accompanying prospectus, contain important information about us that a prospective investor should know before investing in our common stock. Please read this prospectus supplement and the accompanying prospectus before you invest and keep it for future reference. We file annual, quarterly and current reports, proxy statements and other information about us with the Securities and Exchange Commission, or the SEC. The SEC also maintains a website at *http://www.sec.gov* that contains such information. This information is also available free of charge by contacting us at 4400 Post Oak Parkway, Suite 2200, Houston, Texas 77027, Attention: Investor Relations, or by calling us collect at (713) 292-5400 or on our website at *www.stelluscapital.com.* Information contained on our website is not incorporated by reference into this prospectus, and you should not consider that information to be part of this prospectus supplement and the accompanying prospectus.

Investing in our common stock involves a high degree of risk. Before buying any shares, you should read the discussion of the material risks of investing in our common stock in Risk Factors beginning on page 17 of the accompanying prospectus.

Neither the SEC nor any state securities commission has approved or disapproved of these securities, or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Per Share	Per Share	Total
Public offering price	$14.43	$39,682,500
Sales load to be paid by us (1)	$0.34	$935,000
Proceeds to us before expenses (2)	$14.09	$38,747,500

(1) Stellus Capital Management, LLC has agreed to bear $652,300, or $0.2372 per share, of the sales load in connection with the shares of our common stock sold in this offering, which is not reflected in the above table. If the underwriters exercise their option to purchase additional shares in full, Stellus Capital Management, LLC will bear $750,145, or $0.2372 per share.

(2) Before deducting estimated offering expenses payable by us of approximately $135,000.

The underwriters have the option to purchase up to an additional 412,500 shares of common stock at the public offering price, less the underwriting discount, within 30 days from the date of this prospectus supplement. If the option is exercised in full, the total public offering price will be $45,634,875, and the sales load paid by us will be $1,075,250. The proceeds to us would be $44,559,625, before deducting estimated expenses payable by us of $135,000.

Joint Bookrunning Managers

RAYMOND JAMES | **Keefe, Bruyette & Woods** ***A Stifel Company*** | **Goldman Sachs & Co. LLC**

Co-Managers

Ladenburg Thalmann | **BB&T Capital Markets** | **Janney Montgomery Scott**

The date of this prospectus supplement is March 15, 2019

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YOU SHOULD RELY ONLY ON THE INFORMATION CONTAINED IN THIS PROSPECTUS SUPPLEMENT AND THE ACCOMPANYING PROSPECTUS. WE HAVE NOT, AND THE UNDERWRITERS HAVE NOT, AUTHORIZED ANY OTHER PERSON TO PROVIDE YOU WITH DIFFERENT OR ADDITIONAL INFORMATION. IF ANYONE PROVIDES YOU WITH DIFFERENT OR ADDITIONAL INFORMATION, YOU SHOULD NOT RELY ON IT. WE ARE NOT, AND THE UNDERWRITERS ARE NOT, MAKING AN OFFER TO SELL THESE SECURITIES IN ANY JURISDICTION WHERE THE OFFER OR SALE IS NOT PERMITTED. YOU SHOULD ASSUME THAT THE INFORMATION APPEARING IN THIS PROSPECTUS SUPPLEMENT AND THE ACCOMPANYING PROSPECTUS IS ACCURATE ONLY AS OF THEIR RESPECTIVE DATES, REGARDLESS OF THE TIME OF DELIVERY OF THIS PROSPECTUS SUPPLEMENT AND THE ACCOMPANYING PROSPECTUS OR ANY SALES OF THE SECURITIES. OUR BUSINESS, FINANCIAL CONDITION, RESULTS OF OPERATIONS AND PROSPECTS MAY HAVE CHANGED SINCE THOSE DATES.

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ABOUT THIS PROSPECTUS SUPPLEMENT

This document is in two parts. The first part is this prospectus supplement, which describes the specific terms of this offering and certain matters relating to us. The second part, the accompanying prospectus, gives more general information about the securities that we may offer from time to time, some of which may not apply to the common stock offered by this prospectus supplement. For information about our common stock, see Description of Our Common Stock in the accompanying prospectus.

If information varies between this prospectus supplement and the accompanying prospectus, you should rely only on such information in this prospectus supplement. The information contained in this prospectus supplement supersedes any inconsistent information included in the accompanying prospectus. In various places in this prospectus supplement and the accompanying prospectus, we refer you to other sections of such documents for additional information by indicating the caption heading of such other sections. The page on which each principal caption included in this prospectus supplement and the accompanying prospectus can be found is listed in the table of contents above. All such cross references in this prospectus supplement are to captions contained in this prospectus supplement and not in the accompanying prospectus, unless otherwise stated.

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PROSPECTUS SUPPLEMENT SUMMARY

This summary highlights some of the information in this prospectus supplement and the accompanying prospectus. It is not complete and may not contain all of the information that you may want to consider. You should read the more detailed information set forth under Risk Factors and the other information included in this prospectus supplement and the accompanying prospectus carefully. Except as otherwise indicated, the terms we, us, our, and the Company refer to Stellus Capital Investment Corporation; and Stellus Capital Management refers to our investment adviser and administrator, Stellus Capital Management, LLC.

Stellus Capital Investment Corporation

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a BDC under the 1940 Act. We originate and invest primarily in private middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA (earnings before interest, taxes, depreciation and amortization)) through first lien (including unitranche), second lien and unsecured debt financing, with corresponding equity co-investments. Unitranche debt is typically structured as first lien loans with certain risk characteristics of unsecured debt. Unsecured debt includes senior unsecured and subordinated loans.

Our investment activities are managed by our investment adviser, Stellus Capital Management, an investment advisory firm led by Robert T. Ladd and its other senior investment professionals. We source investments primarily through the extensive network of relationships that the senior investment professionals of Stellus Capital Management have developed with financial sponsor firms, financial institutions, middle-market companies, management teams and other professional intermediaries. The companies in which we invest are typically highly leveraged, and, in most cases, our investments in such companies will not be rated by national rating agencies. If such investments were rated, we believe that they would likely receive a rating that is often referred to as junk.

Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation. We seek to achieve our investment objective by:

accessing the extensive origination channels that have been developed and established by the Stellus Capital Management senior investment professionals that include long-standing relationships with private equity firms, commercial banks, investment banks and other financial services firms;
investing in what we believe to be companies with strong business fundamentals, generally within our core middle-market company focus;
focusing on a variety of industry sectors, including business services, energy, general industrial, government services, healthcare, software and specialty finance;
focusing primarily on directly originated transactions;
applying the disciplined underwriting standards that the Stellus Capital Management senior investment professionals have developed over their extensive investing careers; and
capitalizing upon the experience and resources of the Stellus Capital Management investment team to monitor our investments.

In addition, on October 23, 2013, we received an exemptive order (the Prior Order) from the SEC to co-invest with private funds managed by Stellus Capital Management where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). On December 18, 2018, we received a new exemptive order (the Order) that supersedes the Prior Order and permits us greater flexibility to enter into co-investment transactions. The Order expands on the Prior Order and allows us to co-invest with additional types of private funds, other BDCs, and registered investment companies

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managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management, subject to the conditions included therein. Pursuant to the Order, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is consistent with our investment objectives and strategies. We co-invest, subject to the conditions included in the Order, with private credit funds managed by Stellus Capital Management that have an investment strategy that is similar to or identical to our investment strategy, and we may co-invest with other BDCs and registered investment companies managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management in the future. We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification.

As a BDC, we are required to comply with certain regulatory requirements. Prior to June 28, 2018, we were only allowed to employ leverage to the extent that our asset coverage, as defined in the 1940 Act, was equal to at least 200% after giving effect to such leverage. On March 23, 2018, the Small Business Credit Availability Act (the SBCAA) was signed into law, which included various changes to regulations under the federal securities laws that impact BDCs. The SBCAA included changes to the 1940 Act to allow BDCs to decrease their asset coverage requirement to 150% from 200% under certain circumstances. On April 4, 2018, our board of directors, or the Board , including a required majority (as such term is defined in Section 57(o) of the 1940 Act) of the Board, approved the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act. The Board also approved the submission of a proposal to approve the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act, which was approved by stockholders at our 2018 annual meeting of stockholders. As a result, the asset coverage ratio applicable to the Company was decreased from 200% to 150%, effective as of June 28, 2018. In other words, prior to the enactment of the SBCAA, a BDC could borrow $1.00 for investment purposes for every $1.00 of investor equity. Now, for those BDCs, like the Company, that satisfy the SBCAA s approval and disclosure requirements, the BDC can borrow $2.00 for investment purposes for every $1.00 of investor equity. As of December 31, 2018, our asset coverage ratio was 251%. The amount of leverage that we employ at any time depends on our assessment of the market and other factors at the time of any proposed borrowing.

We have elected and intend to qualify annually to be treated for federal income tax purposes as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code, or the Code. As a RIC, we generally will not have to pay corporate-level federal income taxes on any net ordinary income or capital gains that we distribute to our stockholders as dividends if we meet certain source-of-income, distribution and asset diversification requirements.

SBIC License

Our wholly owned subsidiary holds a license from the Small Business Administration, or SBA, to operate as a small business investment company, or SBIC. Current SBA regulations allow an SBIC to obtain leverage by issuing SBA-guaranteed debentures up to a maximum of $175 million under current SBIC regulations, subject to required capitalization of the SBIC subsidiary, SBA approval, and other requirements. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. The interest rate of SBA-guaranteed debentures is fixed at the time of issuance at a market-driven spread over U.S. Treasury Notes with ten-year maturities. We believe that the SBA-guaranteed debentures are an attractive source of debt capital.

We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the 200% asset coverage ratio we are required to maintain under the 1940 Act. The exemptive relief provides us

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with increased flexibility under the asset coverage test by permitting us to borrow up to $175.0 million more than we would otherwise be able to absent the receipt of this exemptive relief.

Portfolio Composition

Our investments generally range in size from $5.0 million to $30.0 million, and we may also selectively invest in larger positions. We generally expect that the size of our positions will increase in proportion to the size of our capital base. Pending such investments, we may reduce our outstanding indebtedness or invest in cash, cash equivalents, U.S. government securities and other high-quality debt investments with a maturity of one year or less. In the future, we may adjust opportunistically the percentage of our assets held in various types of loans, our principal loan sources and the industries to which we have greatest exposure, based on market conditions, the credit cycle, available financing and our desired risk/return profile.

The following table provides a summary of our portfolio investments as of December 31, 2018:

		As of December 31, 2018 ($ in millions)
Number of investments		57
Fair value (a)		$ 504.5
Cost		$ 502.7
% of portfolio at fair value	first lien debt (b)	57.9 %
% of portfolio at fair value	second lien debt	29.7 %
% of portfolio at fair value	unsecured debt	5.0 %
% of portfolio at fair value	equity	7.4 %
Weighted-average annual yield (c)		10.9 %

(a) As of December 31, 2018, $422.3 million of our debt investments at fair value were at floating interest rates, which represented approximately 91% of our total portfolio of debt investments at fair value. As of December 31, 2018, $43.0 million of our debt investments at fair value were at fixed interest rates, which represented approximately 9% of our total portfolio of debt investments at fair value.

(b) Includes unitranche investments, which account for 20.6% of our investment portfolio at fair value.

(c) The weighted average yield on all of our debt investments as of December 31, 2018, was approximately 10.9%, of which approximately 10.2% was current cash interest. The weighted average yield of our debt investments is not the same as a return on investment for our stockholders but, rather, relates to a portion of our investment portfolio and is calculated before the payment of all of our and our subsidiaries fees and expenses. The weighted average yield was computed using the effective interest rates for all of our debt investments, which represents the interest rate on our debt investment restated as an interest rate payable annually in arrears and is computed including cash and payment in kind, or PIK interest, as well as accretion of original issue discount. There can be no assurance that the weighted average yield will remain at its current level.

Leverage

Credit Facility. We have entered into a senior secured revolving credit agreement, dated as of October 10, 2017, with ZB, N.A., dba Amegy Bank and various other leaders (the Credit Facility). The Credit Facility provides for borrowings up to a maximum of $180.0 million on a committed basis with an accordion feature that allows us to increase the aggregate commitments up to $195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. Borrowings under the Credit Facility bear interest, subject to our election, on a per annum basis equal to (i) LIBOR plus 2.50% with no LIBOR floor or (ii) 1.50% plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%. We pay unused commitment fees of 0.50% per annum on the unused lender commitments. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 1, 2021. Our obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. As of December 31, 2018, we had approximately $99.6 million outstanding under the Credit Facility.

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2022 Notes. On August 21, 2017, we issued $42.5 million in aggregate principal amount of 5.75% notes due 2022, or the 2022 Notes, and received net proceeds of approximately $41.0 million. We issued an additional $6.375 million in aggregate principal amount of the 2022 Notes on September 8, 2017 pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at our option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. The 2022 Notes bear interest at a rate of 5.75% per year payable quarterly on March 15, June 15, September 15 and December 15 of each year. The Notes are listed on the NYSE under the trading symbol SCA with a par value of $25.00 per share.

SBA guaranteed debentures. Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. As of December 31, 2018, the SBIC subsidiary had $150.0 million of SBA guaranteed debentures outstanding.

Stellus Capital Management

Stellus Capital Management manages our investment activities and is responsible for analyzing investment opportunities, conducting research and performing due diligence on potential investments, negotiating and structuring our investments, originating prospective investments and monitoring our investments and portfolio companies on an ongoing basis.

The senior investment professionals of Stellus Capital Management have an average of over 29 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management senior investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing loans and debt securities through market cycles. The Stellus Capital Management senior investment professionals continue to provide investment sub-advisory services to the D. E. Shaw & Co., L.P. and its associated investment funds, or the D. E. Shaw group, with respect to an approximately $17.0 million investment portfolio at fair value (as of December 31, 2018) in middle-market companies pursuant to sub-advisory arrangements.

In addition to serving as our investment adviser and the sub-advisor to the D. E. Shaw group as noted above, Stellus Capital Management currently manages a private credit funds, some of which have an investment strategy that is similar or identical to our investment strategy and energy private equity funds. We received the Order from the SEC, which permits us to to co-invest with investment funds managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management, where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification. We will not co-invest with the energy private equity funds, as the energy private equity funds focus on predominantly equity-related investments and we focus on predominantly credit-related investments. In addition, we will not co-invest with the D. E. Shaw group funds,

Stellus Capital Management is headquartered in Houston, Texas, and also maintains offices in the Washington, D.C. area and Charlotte, North Carolina.

Market Opportunity

We originate and invest primarily in private middle-market companies through first lien (including unitranche), second lien and unsecured debt financing, often with a corresponding equity co-investment. We believe the environment for investing in middle-market companies is attractive for several reasons, including:

Robust Demand for Debt Capital. We believe that private equity firms have significant committed but uncalled capital, a large portion of which is still available for investment in the United States. We expect the large amount of uninvested capital commitments will drive buyout

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activity over the next several years, which should, in turn, create lending opportunities for us. In addition to increased buyout activity, a high volume of senior secured and high yield debt was originated in the calendar years 2011 through 2013 and will come due in the near term and, accordingly, we believe that new financing opportunities will increase as many companies seek to refinance this indebtedness.

Attractive Environment to Lend To Middle-Market Companies. We believe the current strength of the U.S. economy provides an attractive environment to lend to middle-market companies. The U.S. services and manufacturing sector continues to show strong growth and profitability, allowing middle market companies to continue to service their debt and prudently borrow to support growth initiatives and mergers and acquisitions activity. This dynamism, coupled with ample capital from private equity firms to support middle market companies, is creating a large population of credit worthy companies looking for debt capital.

Attractive Deal Pricing and Structures. We believe that the pricing of middle-market debt investments is higher, and the terms of such investments are more conservative, compared to larger liquid, public debt financings, due to the more limited universe of lenders as well as the highly negotiated nature of these financings. These transactions tend to offer stronger covenant packages, higher interest rates, lower leverage levels and better call protection compared to larger financings. In addition, middle-market loans typically offer other investor protections such as default penalties, lien protection, change of control provisions and information rights for lenders.

Specialized Lending Requirements. Lending to middle-market companies requires in-depth diligence, credit expertise, restructuring experience and active portfolio management. We believe that several factors render many U.S. financial institutions ill-suited to lend to middle-market companies. For example, based on the experience of Stellus Capital Management s senior investment professionals, lending to middle-market companies in the United States (a) is generally more labor intensive than lending to larger companies due to the smaller size of each investment and the fragmented nature of the information available with respect to such companies, (b) requires specialized due diligence and underwriting capabilities, and (c) may also require more extensive ongoing monitoring by the lender. We believe that, through Stellus Capital Management, we have the experience and expertise to meet these specialized lending requirements.

Competitive Strengths

We believe that the following competitive strengths will allow us to achieve positive returns for our investors:

Experienced Investment Team. Through our investment adviser, Stellus Capital Management, we have access to the experience and expertise of the Stellus Capital Management senior investment professionals, including its senior investment professionals who have an average of over 29 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing debt and equity securities through market cycles. We believe the members of Stellus Capital Management s senior investment professionals are proven and experienced, with extensive capabilities in credit investing, having participated in these markets for the predominant portion of their careers. We believe that these characteristics enhance the quantity and quality of investment opportunities available to us.

Established, Rigorous Investment and Monitoring Process. The Stellus Capital Management senior investment professionals have developed an extensive review and credit analysis process. Each investment that is reviewed by Stellus Capital Management is brought through a structured, multi-stage approval process. In addition, Stellus Capital Management takes an active approach in monitoring all investments, including reviews of financial performance on at least a quarterly basis and regular discussions with management. Stellus Capital Management s

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investment and monitoring process and the depth and experience of its investment professionals should allow it to conduct the type of due diligence and monitoring that enables it to identify and evaluate risks and opportunities.

Demonstrated Ability to Structure Investments Creatively. Stellus Capital Management has the expertise and ability to structure investments across all levels of a company s capital structure. Furthermore, we believe that current market conditions will allow us to structure attractively priced debt investments and may allow us to incorporate other return-enhancing mechanisms such as commitment fees, original issue discounts, early redemption premiums, PIK, interest and various forms of equity securities.

Resources of Stellus Capital Management Platform. We have access to the resources and capabilities of Stellus Capital Management, which has 17 investment professionals, including Robert T. Ladd, Dean D Angelo, Joshua T. Davis and Todd A. Overbergen, who are supported by eight managing directors, two vice presidents and three analysts. These individuals have developed long-term relationships with middle-market companies, management teams, financial sponsors, lending institutions and deal intermediaries by providing flexible financing throughout the capital structure. We believe that these relationships provide us with a competitive advantage in identifying investment opportunities in our target market. We also expect to benefit from Stellus Capital Management s due diligence, credit analysis, origination and transaction execution experience and capabilities, including the support provided with respect to those functions by Mr. Huskinson, who serves as our chief financial officer and chief compliance officer, and his staff of ten finance and operations professionals.

Risk Factors

An investment in our securities is subject to risks. The following is a summary of the principal risks that you should carefully consider before investing in our securities. In addition, see Risk Factors beginning on page 17 of the accompanying prospectus to read about factors you should consider before deciding to invest in our securities.

We are dependent upon key personnel of Stellus Capital Management for our future success. If Stellus Capital Management were to lose any of its key personnel, our ability to achieve our investment objective could be significantly harmed.
Our business model depends to a significant extent upon strong referral relationships. Any inability of Stellus Capital Management to maintain or develop these relationships, or the failure of these relationships to generate investment opportunities, could adversely affect our business.
Our financial condition, results of operations and cash flows will depend on our ability to manage our business effectively.
There are significant potential conflicts of interest that could negatively affect our investment returns.
The incentive fee structure we have with Stellus Capital Management may create incentives that are not fully aligned with the interests of our stockholders.
We will be subject to corporate-level income tax and may default under the Credit Facility if we are unable to maintain our qualification as a RIC under Subchapter M of the Code.
Regulations governing our operation as a BDC affect our ability to and the way in which we raise additional capital and, as a BDC, the necessity of raising additional capital may expose us to risks, including the typical risks associated with leverage.
Because we finance our investments with borrowed money, the potential for gain or loss on amounts invested in us is magnified and may increase the risk of investing in us.
Because we use debt to finance our investments, changes in interest rates will affect our cost of capital and net investment income.

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Adverse developments in the credit markets may impair our ability to borrow money.
Most of our portfolio investments are recorded at fair value as determined in good faith by our board of directors and, as a result, there may be uncertainty as to the value of our portfolio investments.
Our ability to enter into transactions with our affiliates will be restricted, which may limit the scope of investments available to us.
The involvement of our interested directors in the valuation process may create conflicts of interest.
There are conflicts related to other arrangements with Stellus Capital Management.
If we fail to maintain our status as a BDC, our business and operating flexibility could be significantly reduced.
Because we have received Board and stockholder approval, we are subject to 150% Asset Coverage. This approval allows us to incur twice as much debt as we could have without such approval, potentially heightening the risks associated with leverage described above.
The effect of global climate change may impact the operations of our portfolio companies.
Existing stockholders may incur dilution if, in the future, we sell shares of our common stock in one or more offerings at prices below the then current net asset value per share of our common stock.

Conflicts of Interests

We may have conflicts of interest arising out of the investment advisory activities of Stellus Capital Management, including those described below.

Our investment strategy includes investments in secured debt (including first lien, second lien and unitranche) and mezzanine debt (including senior unsecured and subordinated debt), as well as related equity securities of private middle-market companies. Stellus Capital Management also manages, and in the future may manage, other investment funds, accounts or investment vehicles that invest or may invest in assets eligible for purchase by us. For example, Stellus Capital Management currently manages private credit funds that have an investment strategy that is identical to our investment strategy. Stellus Capital Management also provides non-discretionary advisory services to the D. E. Shaw group, pursuant to sub-advisory arrangements, with respect to a private investment fund and a strategy of a private multi-strategy investment fund (collectively with the D. E. Shaw group fund, the D. E. Shaw group funds) to which the D. E. Shaw group serves as investment adviser that have an investment strategy similar to our investment strategy. Our investment policies, fee arrangements and other circumstances may vary from those of other investment funds, accounts or investment vehicles managed by Stellus Capital Management.

In addition, on October 23, 2013, we received the Prior Order from the SEC to co-invest with private funds managed by Stellus Capital Management where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). On December 18, 2018, we received the Order that supersedes the Prior Order and permits us greater flexibility to enter into co-investment transactions. The Order expands on the Prior Order and allows us to co-invest with additional types of private funds, other BDCs, and registered investment companies managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management, subject to the conditions included therein. Pursuant to the Order, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is

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consistent with our investment objectives and strategies. We co-invest, subject to the conditions included in the Order, with private credit funds managed by Stellus Capital Management that have an investment strategy that is similar to or identical to our investment strategy, and we may co-invest with other BDCs and registered investment companies managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management in the future. We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification.

In the course of our investing activities, we pay management and incentive fees to Stellus Capital Management. We have entered into an investment advisory agreement with Stellus Capital Management that provides that these fees are based on the value of our gross assets. Because these fees are based on the value of our gross assets, Stellus Capital Management will benefit when we incur debt or use leverage. This fee structure may encourage Stellus Capital Management to cause us to borrow money to finance additional investments. Our board of directors is charged with protecting our interests by monitoring how Stellus Capital Management addresses these and other conflicts of interests associated with its management services and compensation. While our board of directors is not expected to review or approve each investment decision, borrowing or incurrence of leverage, our independent directors will periodically review Stellus Capital Management s services and fees as well as its portfolio management decisions and portfolio performance. See Risk Factors The incentive fee structure we have with Stellus Capital Management may create incentives that are not fully aligned with the interests of our stockholders in the accompanying prospectus.

Stellus Capital Management may from time to time incur expenses in connection with investments to be made on our behalf and on behalf of other investment funds, accounts and investment vehicles managed by Stellus Capital Management. Stellus Capital Management will allocate such expenses on a pro rata basis according to the participation in a transaction, subject to oversight by our board of directors.

Corporate Information

Our principal executive offices are located at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, and our telephone number is (713) 292-5400. We maintain a website located at *www.stelluscapital.com* (under the Public Investors section). Information on our website is not incorporated into or a part of this prospectus or any accompanying prospectus supplement and you should not consider information on our website to be part of this prospectus or any accompanying prospectus.

Recent Developments

Investment Portfolio

On January 4, 2019, we received full repayment on our first lien term loan to EOS Fitness OPCO Holdings, LLC for total proceeds of $3.1 million. We also received a distribution related to our equity position of $0.1 million.

On January 7, 2019, we received $0.3 million in full realization on the equity of OGS Holdings, Inc., resulting in a realized gain of $0.2 million.

On February 4, 2019, we invested $8.5 million in a first lien term loan to ASC Communications, LLC, an existing portfolio company.

On February 8, 2019, we invested $12.3 million in a first lien term loan to Exacta Land Surveyors LLC, a provider of land surveys and field management services used to facilitate the purchasing, selling, and development of residential real estate in the United States. Additionally, we committed $1.5 million in the unfunded revolver, $4.0 million in the unfunded delayed draw term loan, and we invested $1.0 million in the equity of the company.

On February 15, 2019, we received $0.05 million in full realization on the equity of Glori Energy Production, LLC.

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On February 28, 2019, we invested $1.4 million in a first lien term loan to Convergence Technologies, Inc., an existing portfolio company. Additionally, we funded $5.4 million under the existing delayed draw term loan and an additional $0.1 million in the equity of the company.

Credit Facility

The outstanding balance under the Credit Facility as of March 13, 2019 was $115.1 million.

SBA-guaranteed Debentures

The total balance of SBA-guaranteed debentures outstanding as of March 13, 2019 was $150.0 million.

Dividend Declared

On January 11, 2019, the Board declared a regular monthly dividend for each of January, February and March 2019.

Declared	Ex-Dividend Date	Record Date	Payment Date	Amount per Share
1/11/2019	1/30/2019	1/31/2019	2/15/2019	$ 0.1133
1/11/2019	2/27/2019	2/28/2019	3/15/2019	$ 0.1133
1/11/2019	3/28/2019	3/29/2019	4/15/2019	$ 0.1133

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THE OFFERING

Common stock offered by us	2,750,000 shares
Common stock outstanding prior to this offering	15,953,810 shares
Common stock to be outstanding after this offering	18,703,810 shares (assuming no exercise of the underwriters option to purchase additional shares)
Use of proceeds	The net proceeds from this offering (without exercise of the option to purchase additional shares and after deducting estimated expenses payable by us of approximately $135,000) will be $38.6 million. See Use of Proceeds in this prospectus supplement for more information.
Distributions	We pay monthly distributions to our stockholders out of assets legally available for distribution. Our monthly distributions, if any, will be determined by our board of directors. Our board of directors has declared a regular monthly dividend of $0.1133 per share payable on April 15, 2019, May 15, 2019 and June 14, 2019 to common stockholders of record on March 29, 2019, April 30, 2019 and May 31, 2019, respectively.
Taxation	We have elected to be treated for U.S. federal income tax purposes as a RIC. As a RIC, we generally will not have to pay corporate-level U.S. federal income taxes on any net ordinary income or capital gains that we distribute to our stockholders. To maintain our qualification as a RIC and the associated tax benefits, we must meet specified source-of-income and asset diversification requirements and distribute annually at least 90% of our net ordinary income and net short-term capital gains, if any, in excess of our net long-term capital losses. See Distributions and Material U.S. Federal Income Tax Considerations in the accompanying prospectus.
New York Stock Exchange symbol	SCM
Trading at a discount	Shares of closed-end investment companies, including BDCs, frequently trade in the secondary market at a discount to their net asset values. The risk that our shares may trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline. We cannot predict whether our shares will trade above, at or below net asset value. See Risk Factors beginning on page 17 of the accompanying prospectus for a discussion of risks you should carefully consider before deciding to invest in shares of our common stock.
Leverage	We expect to continue to use borrowed funds in order to make additional investments. We expect to use this practice, which is known as leverage, when the terms and conditions are favorable to long-term investing and well aligned with our investment strategy and portfolio composition in an effort to

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increase returns to our stockholders, but this strategy involves significant risks. See Risk Factors beginning on page 17 of the accompanying prospectus. At our 2018 annual meeting on June 28, 2018, our stockholders approved a proposal to permit the Company to be subject to 150% Asset Coverage with immediate effect. This approval allows us to incur twice as much debt as we could have without such approval. The amount of leverage that we employ will depend on Stellus Capital Management s and our Board s assessment of market and other factors at the time of any proposed borrowing.

Our current borrowings include:

Our $195.0 million Credit Facility, of which $115.1 million was outstanding as of March 13, 2019;

Our SBA Debentures, of which $150.0 million were outstanding as of March 13, 2019; and

Our 2022 Notes, of which $48.9 million were outstanding as of March 13, 2019.

Risk Factors

See Risk Factors beginning on page 17 of the accompanying prospectus for a discussion of risks you should carefully consider before deciding to invest in shares of our common stock.

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FEES AND EXPENSES

The following table is intended to assist you in understanding the costs and expenses that an investor in our common stock will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. Moreover, the information set forth below does not include any transaction costs and expenses that investors will incur in connection with each offering of our securities pursuant to this prospectus supplement. Except where the context suggests otherwise, whenever this prospectus supplement contains a reference to fees or expenses paid by us or that we will pay fees or expenses, common stockholders will indirectly bear such fees or expenses.

Stockholder Transaction Expenses:	
Sales load (as a percentage of offering price)	2.36% (1)
Offering expenses (as a percentage of offering price)	0.34% (2)
Dividend reinvestment plan expenses	(3)
Total Stockholder Transaction Expenses (as a percentage of offering price)	2.70 %
Annual Expenses (as percentage of net assets attributable to common stock):	
Base management fees	3.89% (4)
Incentive fees payable under the investment advisory agreement	2.99% (5)
Interest payments on borrowed funds	5.44% (6)
Other expenses	2.83% (7)
Total annual expenses	15.15 %

(1) Represents the commission with respect to the shares of common stock being sold in this offering not including the portion of the commission borne by Stellus Capital Management. There is no guarantee that there will be any sales of our common stock pursuant to this prospectus supplement and the accompanying prospectus.

(2) The percentage reflects estimated offering expenses of approximately $135,000.

(3) The expenses of the dividend reinvestment plan are included in Other expenses.

(4) Our base management fee, payable quarterly in arrears, is 1.75% of our gross assets, including assets purchased with borrowed amounts or other forms of leverage (including traditional and effective leverage such as preferred stock, public and private debt issuances, derivative instruments, repurchase agreements and other similar instruments or arrangements) and excluding cash and cash equivalents and is based on the base management fee incurred for the year ended December 31, 2018.

(5) This item represents the incentive fee payable to Stellus Capital Management based on the actual amounts earned on our pre-incentive fee net investment income for the year ended December 31, 2018.

For purposes of this table, we have assumed that these fees will be payable (in the case of the capital gains incentive fee) and that they will remain constant, although they are based on our performance and will not be paid unless we achieve certain goals.

The incentive fee consists of two components, ordinary income and capital gains:

The ordinary income component, which is payable quarterly in arrears, equals 20.0% of the excess, if any, of our pre-incentive fee net investment income over a 2.0% quarterly (8.0% annualized) hurdle rate, expressed as a rate of return on the value of our net assets attributable to our common stock, and a catch-up provision, measured as of the end of each calendar quarter. Under this provision, in any calendar quarter, our investment adviser receives no incentive fee until our net investment income equals the hurdle rate of 2.0% but then receives, as a catch-up, 100% of our pre-incentive fee net investment income with respect to that portion of such pre-incentive fee net investment income, if any, that exceeds the hurdle rate but is less than 2.5% subject to a total return requirement and deferral of non-cash amounts. The effect of the catch-up provision is that, subject to the total return and deferral provisions discussed below, if pre-incentive fee net investment income exceeds 2.5% in any calendar quarter, Stellus Capital Management will receive 20.0% of our pre-incentive fee net investment income as if a hurdle rate did not apply. The ordinary income component of the incentive fee is computed on income that may include interest that is accrued but not yet received in cash. The foregoing ordinary income component of the incentive fee is subject to a total return requirement, which provides that no incentive fee in respect of the Company s pre-incentive fee net investment income is payable except to the extent 20.0% of the cumulative net increase in net assets resulting from operations (as defined below) over the then current and 11 preceding calendar quarters exceeds the cumulative incentive fees

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accrued and/or paid for the 11 preceding calendar quarters. In other words, any ordinary income incentive fee that is payable in a calendar quarter will be limited to the lesser of (i) 20.0% of the amount by which our pre-incentive fee net investment income for such calendar quarter exceeds the 2.0% hurdle, subject to the catch-up provision, and (ii) (x) 20.0% of the cumulative net increase in net assets resulting from operations for the then current and 11 preceding calendar quarters *minus* (y) the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. For the foregoing purpose, the cumulative net increase in net assets resulting from operations is the sum of pre-incentive fee net investment income, realized gains and losses and unrealized appreciation and depreciation of the Company for the then current and 11 preceding calendar quarters. In addition, the portion of such incentive fee that is attributable to deferred interest (sometimes referred to as PIK or original issue discount, or OID) will be paid to Stellus Capital Management, together with interest thereon from the date of deferral to the date of payment, only if and to the extent we actually receive such interest in cash, and any accrual thereof will be reversed if and to the extent such interest is reversed in connection with any write-off or similar treatment of the investment giving rise to any deferred interest accrual. Any reversal of such accounts would reduce net income for the quarter by the net amount of the reversal (after taking into account the reversal of incentive fees payable) and would result in a reduction and possibly elimination of the incentive fees for such quarter. There is no accumulation of amounts on the hurdle rate from quarter to quarter, and accordingly, there is no clawback of amounts previously paid if subsequent quarters are below the quarterly hurdle, and there is no delay of payment if prior quarters are below the quarterly hurdle.

The capital gains component of the incentive fee equals 20.0% of our Incentive Fee Capital Gains, if any, which equals our aggregate cumulative realized capital gains from inception through the end of each calendar year, computed net of our aggregate cumulative realized capital losses and our aggregate cumulative unrealized capital depreciation, less the aggregate amount of any previously paid capital gain incentive fees. The second component of the incentive fee is payable, in arrears, at the end of each calendar year (or upon termination of the investment advisory agreement, as of the termination date). We will record an expense accrual relating to the capital gains component of the incentive fee payable by us to Stellus Capital Management when the net unrealized gains on our investments exceed all realized capital losses on our investments given the fact that a capital gains incentive fee would be owed to Stellus Capital Management if we were to liquidate our investment portfolio at such time. The actual incentive fee payable to our investment adviser related to capital gains is determined and payable in arrears at the end of each fiscal year and includes only realized capital gains for the period. See Management Agreements Management Fee and Incentive Fee in the accompanying prospectus.

Stellus Capital Management has agreed to permanently waive any interest accrued on the portion of the incentive fee attributable to deferred interest (such as PIK interest or OID).

(6) In addition to our existing SBA guaranteed debentures, the 2022 Notes and the Credit Facility, we may borrow funds from time to time to make investments to the extent we determine that additional capital would allow us to take advantage of additional investment opportunities or if the economic situation is otherwise conducive to doing so. The costs associated with any borrowings are indirectly borne by our stockholders. As of December 31, 2018, we had $150.0 million of SBA guaranteed debentures outstanding, $48.9 million in aggregate principal amount of 5.75% Notes outstanding, plus accrued interest and approximately $99.6 million outstanding under the Credit Facility. For purposes of this calculation, we have assumed that the December 31, 2018 amounts of SBA Debentures remain outstanding and have computed interest expense using the weighted average interest rate as of December 31, 2018 of 3.20%. For the 2022 Notes, we have used the fixed interest rate of 5.75%. We have also assumed borrowings under the Credit Facility incur interest at a rate equal to 4.70% per annum the weighted average interest rate as of December 31, 2018. We expect our borrowings over the 12 months following the offering will be consistent with the amounts outstanding as of December 31, 2018. See Senior Securities in this prospectus supplement.

(7)

Includes our overhead expenses, including payments under the administration agreement based on our allocable portion of overhead and other expenses incurred by Stellus Capital Management. See Management Agreements Administration Agreement in the accompanying prospectus.

Example

The following example demonstrates the projected dollar amount of total cumulative expenses over various periods with respect to a hypothetical investment in us. In calculating the following expense amounts, we have assumed that our annual operating expenses would remain at the levels set forth in the table above.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return (excluding incentive fees)	$ 141	$ 383	$ 579	$ 924

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While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. The incentive fee under the investment management agreement, which, assuming a 5% annual return, would either not be payable or would have a de minimis effect, is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our expenses, and returns to our investors, would be higher. For example, if we assumed that we received our 5.0% annual return completely in the form of net realized capital gains on our investments, which results in a capital gains incentive fee earned, the projected dollar amount of total cumulative expenses set forth in the above illustration and the capital gains incentive fee would be as follows:

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$ 167	$ 439	$ 645	$ 970

While the examples assume reinvestment of all distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the distribution payable to a participant by (a) 95% of the market price per share of our common stock at the close of trading on the payment date fixed by our board of directors or (b) the average purchase price of all shares of common stock purchased by the administrator of the dividend reinvestment plan in the event shares are purchased in the open market to satisfy the share requirements of the dividend reinvestment plan, which may be at, above or below net asset value.

This example and the expenses in the table above should not be considered a representation of our future expenses, and actual expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements in this prospectus supplement and the accompanying prospectus constitute forward-looking statements, which relate to future events or our future performance or financial condition. The forward-looking statements contained in this prospectus supplement and the accompanying prospectus may include, but are not limited to, statements as to:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the effect of investments that we expect to make;
- our contractual arrangements and relationships with third parties;
- actual and potential conflicts of interest with Stellus Capital Management;
- the dependence of our future success on the general economy and its effect on the industries in which we invest;
- the ability of our portfolio companies to achieve their objectives;
- the use of borrowed money to finance a portion of our investments;
- the adequacy of our financing sources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies;
- the ability of Stellus Capital Management to locate suitable investments for us and to monitor and administer our investments;
- the ability of Stellus Capital Management to attract and retain highly talented professionals;
- our ability to qualify and maintain our qualification as a RIC and as a BDC; and
- the effect of future changes in laws or regulations (including the interpretation of these laws and regulations by regulatory authorities) and conditions in our operating areas, particularly with respect to BDCs or RICs.

Such forward-looking statements may include statements preceded by, followed by or that otherwise include the words may, might, will, intend, should, could, can, would, expect, believe, estimate, anticipa or similar words.

We have based the forward-looking statements included in this prospectus supplement and the accompanying prospectus on information available to us on the date of this prospectus supplement and the accompanying prospectus and we assume no obligation to update any such forward-looking statements. Actual results could differ materially from those anticipated in our forward-looking statements, and future results could differ materially from historical performance. We undertake no obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by law or SEC rule or regulation. You are advised to consult any additional disclosures that we may make directly to you, including in the form of a prospectus supplement or post-effective amendment to the registration statement to which this prospectus relates, or through reports that we in the future may file with the SEC, including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K.

You should understand that, under Sections 27A(b)(2)(B) of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E(b)(2)B of the Securities Exchange Act of 1934, the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 do not apply to statements made in connection with any offering of securities pursuant to this prospectus supplement and the accompanying prospectus, if any.

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USE OF PROCEEDS

The net proceeds from the sale of the 2,750,000 shares of common stock in this offering are $38.6 million, and $44.4 million if the underwriter s option to purchase additional shares is exercised in full, after deducting the underwriting discount and estimated offering expenses payable by us.

We intend to use the net proceeds from this offering to repay a portion of the amount outstanding under the Credit Facility, for general corporate purposes, which may include investing in debt or equity securities, and other general corporate purposes, including working capital requirements.

As of March 13, 2019, we had $115.1 million outstanding under the Credit Facility. The Credit Facility has a maturity date of October 10, 2021. Borrowings under the Credit Facility bear interest, subject to our election, on a per annum basis equal to (i) LIBOR plus 2.50% (or 2.75% during certain periods in which our asset coverage ratio is equal to or below 1.90 to 1.00) with no LIBOR floor or (ii) 1.50% (or 1.75% during certain periods in which our asset coverage ratio is equal to or below 1.90 to 1.00) plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%.

We intend to seek to invest the net proceeds received in this offering as promptly as practicable after receipt thereof consistent with our investment objective. We anticipate that substantially all of the net proceeds from this offering of our securities will be used as described above within three to six months, depending on market conditions. We anticipate that the remainder will be used for working capital and general corporate purposes, including potential payments or distributions to stockholders. Pending such use, we will invest a portion of the net proceeds of this offering in short-term investments, such as cash and cash equivalents, which we expect will earn yields substantially lower than the interest income that we anticipate receiving in respect of investments in accordance with our investment objective.

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CAPITALIZATION

The following table sets forth our capitalization as of December 31, 2018:

on an actual basis; and

on an as further adjusted basis giving effect to the assumed sale of 2,750,000 shares of our common stock at a price of $14.43 per share, less commissions and expenses, and the application of the proceeds to repay a portion of the amount outstanding under the Credit Facility.

This table should be read in conjunction with our Management s Discussion and Analysis of Financial Condition and Results of Operations and our financial statements and notes thereto included in this prospectus supplement and the accompanying prospectus.

	As of December 31, 2018	
	Actual	As Adjusted (1) (Unaudited)
Assets		
Cash and cash equivalents	$17,467,146	$17,467,146
Investments, at fair value	$504,483,668	$504,483,668
Other assets	$4,336,437	$4,336,437
Total assets	$526,287,251	$526,287,251
Liabilities:		
5.75% Notes due 2022	$47,641,797	$47,641,797
Credit Facility (1)	$98,237,227	$59,624,727
SBA-Guaranteed debentures	$146,387,802	$146,387,802
Other liabilities	$9,175,418	$9,175,418
Total liabilities	$301,442,244	$262,829,744
Stockholder s equity:		
Common stock, par value $0.001 per share (100,000,000 shares authorized; 15,953,810 shares issued and outstanding, actual; 18,703,810[(2)] shares issued and outstanding, as adjusted)	$15,954	$18,704
Paid-in capital in excess of par value	$228,160,491	$266,770,241
Accumulated net realized loss	$(10,786,240)	$(10,786,240)
Accumulated undistributed net investment income	$5,782,736	$5,782,736
Net unrealized appreciation (depreciation) on investments and cash equivalents	$1,672,066	$1,672,066
Total stockholders equity	$224,845,007	$263,457,507
Total liabilities and stockholders equity	$526,287,251	$526,287,251

(1) As of March 13, 2019, we had approximately $115.1 million outstanding under our Credit Facility outstanding. This table has not been adjusted to reflect the changes in our outstanding borrowings under the Credit Facility subsequent to December 31, 2018.

(2) Excludes up to 412,500 shares of our common stock issuable upon exercise of the underwriters option to purchase additional shares.

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SELECTED FINANCIAL AND OTHER DATA

The following selected financial data for the years ended December 31, 2018, 2017, 2016, 2015 and 2014 was derived from our financial statements which have been audited by Grant Thornton, LLP, our independent registered public accounting firm. The data should be read in conjunction with our financial statements and related notes thereto and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this prospectus supplement and the accompanying prospectus.

Statement of Operations Data	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Total investment income	$53,266,338	$39,648,193	$39,490,197	$35,158,559	$32,324,847
Total expenses, net of fee waiver	$30,629,801	$21,677,433	$22,177,996	$18,611,431	$15,812,750
Net investment income	$22,636,537	$17,970,760	$17,312,201	$16,547,128	$16,512,097
Net increase in net assets resulting from operations	$26,194,578	$22,613,257	$23,199,062	$7,670,536	$10,179,142
Per Share Data:					
Net asset value	$14.09	$13.81	$13.69	$13.19	$13.94
Net investment income	$1.42	$1.21	$1.39	$1.33	$1.34
Net increase in net assets resulting from operations	$1.64	$1.52	$1.86	$0.61	$0.83
Distributions declared	$1.36	$1.36	$1.36	$1.36	$1.36

Balance Sheet Data	As of December 31, 2018	As of December 31, 2017	As of December 31, 2016	As of December 31, 2015	As of December 31, 2014
Investments at fair value	$504,483,668	$371,839,772	$365,625,891	$349,017,697	$315,965,434
Cash and cash equivalents	$17,467,146	$25,110,718	$9,194,129	$10,875,790	$2,046,563
Total assets(2)	$526,287,251	$400,260,855	$379,878,729	$365,368,412	$323,776,402
Total liabilities(2)	$301,442,244	$180,013,613	$208,996,944	$200,717,308	$149,826,950
Total net assets	$224,845,007	$220,247,242	$170,881,785	$164,651,104	$173,949,452
Other Data:					
Number of portfolio companies at period end	57	48	45	39	32
Weighted average yield on debt investments at period end(1)(3)	10.9%	10.8%	11.0%	10.6%	10.9%

(1) Computed using the effective interest rates for all of our debt investments, including accretion of original issue discount.

(2) ASU No. 2015-03 Simplifying the Presentation of Debt Issuance Costs was effective for the quarter ended March 31, 2016. Total assets and total liabilities for the periods prior to the effective date have been modified from their respective filings to conform to this presentation.

(3) The weighted average yield of our debt investments is not the same as a return on investment for our stockholders, rather, relates to a portion of our investment portfolio and is calculated before the payment of all of our subsidiaries fees and expenses. The weighted average yield was computed using the effective interest rates for all of our debt investment restated as an interest rate payable annually in arrears and is computed including cash and payment in kind, or PIK interest, as well as accretion of original issue discount.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our financial statements and notes thereto contained elsewhere in this prospectus supplement.

Statements we make in the following discussion which express a belief, expectation or intention, as well as those that are not historical fact, are forward-looking statements that are subject to risks, uncertainties and assumptions. Our actual results, performance or achievements, or industry results, could differ materially from those we express in the following discussion as a result of a variety of factors, including the risks and uncertainties we have referred to under the headings Special Note Regarding Forward-Looking Statements in this prospectus supplement and Risk Factors in the accompanying prospectus.

Overview

We were organized as a Maryland corporation on May 18, 2012 and formally commenced operations on November 7, 2012. Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation through debt and related equity investments in middle-market companies.

We are an externally managed, non-diversified, closed-end investment company that has elected to be regulated as a BDC under the 1940 Act. Our investment activities are managed by our investment adviser, Stellus Capital Management.

As a BDC, we are required to comply with certain regulatory requirements. For instance, as a BDC, we must not acquire any assets other than qualifying assets specified in the 1940 Act unless, at the time the acquisition is made, at least 70% of our total assets are qualifying assets. Qualifying assets include investments in eligible portfolio companies. Under the relevant SEC rules, the term eligible portfolio company includes all private operating companies, operating companies whose securities are not listed on a national securities exchange, and certain public operating companies that have listed their securities on a national securities exchange and have a market capitalization of less than $250 million, in each case organized and with their principal of business in the United States.

We have elected to be treated for tax purposes as a RIC under Subchapter M of the Code. To maintain our qualification as a RIC, we must, among other things, meet certain source-of-income and asset diversification requirements. As of December 31, 2018, we were in compliance with the RIC requirements. As a RIC, we generally will not have to pay corporate-level U.S. federal income taxes on any income we distribute to our stockholders.

As a BDC, we are required to comply with certain regulatory requirements. Prior to June 28, 2018, we were only allowed to employ leverage to the extent that our asset coverage, as defined in the 1940 Act, was equal to at least 200% after giving effect to such leverage. On March 23, 2018, the Small Business Credit Availability Act (the SBCAA) was signed into law, which included various changes to regulations under the federal securities laws that impact BDCs. The SBCAA included changes to the 1940 Act to allow BDCs to decrease their asset coverage requirement to 150% from 200% under certain circumstances.

On April 4, 2018, the Board, including a required majority (as such term is defined in Section 57(o) of the Investment Company Act of 1940, as amended (the 1940 Act)) of the Board, approved the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act. The Board also approved the submission of a proposal to approve the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act, which was approved by shareholders at the Company s 2018 annual meeting of stockholders. As a result, the asset coverage ratio applicable to the Company was decreased from 200% to 150%, effective June 28, 2018. The amount of leverage that we employ at any time depends on our assessment of the market and other factors at the time of any proposed borrowing.

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Portfolio Composition and Investment Activity

Portfolio Composition

We originate and invest primarily in privately-held middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA) through first lien (including unitranche), second lien, and unsecured debt financing, often times with a corresponding equity investment.

As of December 31, 2018, we had $504.5 million (at fair value) invested in 57 companies. As of December 31, 2018, our portfolio included approximately 58% of first lien debt, 30% of second lien debt, 5% of unsecured debt and 7% of equity investments at fair value. The composition of our investments at cost and fair value as of December 31, 2018 was as follows:

	Cost	Fair Value
Senior Secured First Lien (1)	$ 297,965,589	$ 292,004,982
Senior Secured Second Lien	155,382,612	149,661,220
Unsecured Debt	25,436,237	23,697,466
Equity	23,959,211	39,120,000
Total Investments	$ 502,743,649	$ 504,483,668

(1) Includes unitranche investments, which account for 20.6% of our portfolio at fair value. Unitranche structures may combine characteristics of first lien senior secured as well as second lien and/or subordinated loans and our unitranche loans will expose us to the risks associated with the second lien and subordinated loans to the extent we invest in the last-out tranche.

As of December 31, 2017, we had $371.8 million (at fair value) invested in 48 companies. As of December 31, 2017, our portfolio included approximately 38% of first lien debt, 48% of second lien debt, 7% of unsecured debt and 7% of equity investments at fair value. The composition of our investments at cost and fair value as of December 31, 2017 was as follows:

	Cost	Fair Value
Senior Secured First Lien (1)	$ 140,915,106	$ 141,006,923
Senior Secured Second Lien	181,164,730	178,432,850
Unsecured Debt	27,903,141	27,430,000
Equity	18,470,229	24,969,999
Total Investments	$ 368,453,206	$ 371,839,772

(1) Includes unitranche investments, which account for 13.2% of our portfolio at fair value. Unitranche structures may combine characteristics of first lien senior secured as well as second lien and/or subordinated loans and our unitranche loans will expose us to the risks associated with the second lien and subordinated loans to the extent we invest in the last-out tranche.

Our investment portfolio may contain loans that are in the form of lines of credit or revolving credit facilities, which require us to provide funding when requested by portfolio companies in accordance with the terms and conditions of the underlying loan agreements. As of December 31, 2018 and December 31, 2017, we had unfunded commitments of $21.2 million and $8.7 million, respectively, to provide debt financing for eleven and four portfolio companies, respectively. As of December 31, 2018, the Company had sufficient liquidity to fund such unfunded commitments should the need arise.

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The following is a summary of geographical concentration of our investment portfolio as of December 31, 2018:

	Cost	Fair Value	% of Total Investments at fair value	
Texas	$ 100,229,354	$ 97,474,226	19.32	%
California	86,550,134	85,880,918	17.03	%
New Jersey	43,513,698	41,473,072	8.22	%
Ohio	36,209,514	36,273,224	7.19	%
Illinois	19,941,053	29,880,018	5.92	%
Canada	27,902,537	27,935,931	5.54	%
Arizona	21,682,522	21,603,741	4.28	%
South Carolina	20,871,587	20,385,325	4.04	%
New York	20,446,690	20,287,086	4.02	%
Tennessee	20,117,218	19,381,134	3.84	%
Arkansas	17,696,537	18,013,941	3.57	%
Pennsylvania	17,732,831	17,824,372	3.53	%
Maryland	17,237,500	17,237,500	3.42	%
Wisconsin	11,437,711	10,869,000	2.15	%
Colorado	10,777,822	10,777,822	2.14	%
Georgia	5,988,728	9,820,000	1.95	%
Indiana	7,363,628	7,087,500	1.40	%
Puerto Rico	8,797,954	5,029,913	1.00	%
North Carolina	4,946,554	4,425,000	0.88	%
Massachusetts	1,317,406	1,670,000	0.33	%
Missouri	139,656	670,000	0.13	%
Virginia	50,001	280,000	0.06	%
Florida	242,304	110,000	0.02	%
Utah	1,550,710	93,945	0.02	%
	$ 502,743,649	$ 504,483,668	100.00	%

The following is a summary of geographical concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Texas	$ 109,043,496	$ 108,445,000	29.16	%
New Jersey	34,531,876	34,595,527	9.30	%
New York	28,939,268	29,365,000	7.90	%
Canada	26,315,677	26,440,000	7.11	%
California	25,519,753	25,930,000	6.97	%
Illinois	24,250,169	25,700,000	6.91	%
Massachusetts	22,534,191	22,247,850	5.98	%
Arizona	13,565,958	13,840,000	3.72	%
North Carolina	12,248,770	12,499,167	3.36	%
Ohio	10,112,627	9,990,000	2.69	%
Tennessee	9,848,614	9,950,000	2.68	%
Missouri	9,152,087	9,530,000	2.56	%

Georgia	5,929,223	8,329,998	2.24	%
Pennsylvania	7,848,470	8,058,746	2.17	%
Arkansas	7,397,881	7,618,484	2.05	%
Minnesota	5,421,770	5,420,000	1.46	%
Puerto Rico	8,827,864	5,080,000	1.37	%
Washington	4,172,743	4,520,000	1.22	%
Alabama	1,206,682	2,880,000	0.77	%
Utah	1,293,782	880,000	0.24	%
Florida	242,304	420,000	0.11	%
Virginia	50,001	100,000	0.03	%
	$ 368,453,206	$ 371,839,772	100.00	%

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The following is a summary of industry concentration of our investment portfolio as of December 31, 2018:

	Cost	Fair Value	% of Total Investments at fair value	
Services: Business	$ 60,784,467	$ 63,810,643	12.65	%
Healthcare & Pharmaceuticals	58,682,811	54,785,327	10.86	%
Consumer Goods: Durable	44,218,515	44,049,052	8.73	%
Finance	34,208,412	41,910,000	8.30	%
Software	37,427,547	38,026,250	7.54	%
Media: Broadcasting & Subscription	38,137,844	37,733,004	7.48	%
Retail	28,764,221	27,525,897	5.45	%
Education	26,562,249	25,325,000	5.02	%
High Tech Industries	21,094,192	21,094,192	4.18	%
Beverage, Food, & Tobacco	20,709,134	18,213,945	3.61	%
Services: Consumer	17,952,663	17,640,255	3.50	%
Automotive	17,457,259	17,282,187	3.43	%
Energy: Oil & Gas	14,312,328	15,542,102	3.08	%
Consumer goods: non-durable	14,994,980	14,579,375	2.89	%
Chemicals, Plastics, & Rubber	11,835,100	11,707,835	2.32	%
Containers, Packaging, & Glass	11,437,711	10,869,000	2.15	%
Construction & Building	10,374,827	10,280,000	2.04	%
Utilities: Oil & Gas	9,853,435	9,853,435	1.95	%
Capital Equipment	7,535,876	7,929,775	1.57	%
Transportation: Cargo	6,808,345	6,841,739	1.36	%
Insurance	5,425,301	5,460,000	1.08	%
Hotel, Gaming, & Leisure	3,170,307	3,414,655	0.68	%
Environmental Industries	946,124	330,000	0.07	%
Services: Government	50,001	280,000	0.06	%
	$ 502,743,649	$ 504,483,668	100.00	%

The following is a summary of industry concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Software	$ 48,560,675	$ 48,997,850	13.18	%
Healthcare & Pharmaceuticals	41,192,879	37,829,167	10.17	%
High Tech Industries	36,058,477	35,460,000	9.54	%
Finance	26,500,097	28,330,000	7.62	%
Services: Business	23,386,714	25,749,999	6.93	%
Capital Equipment	24,300,027	24,170,000	6.50	%
Media: Broadcasting & Subscription	21,680,239	23,665,000	6.36	%
Chemicals, Plastics, & Rubber	20,825,458	21,145,000	5.69	%
Services: Consumer	17,862,616	18,070,000	4.86	%
Construction & Building	17,913,413	17,980,000	4.84	%
Education	17,197,396	17,335,526	4.66	%
Consumer Goods: Durable	16,559,947	16,798,484	4.52	%

Consumer goods: non-durable	13,250,000	13,250,000	3.56	%
Retail	8,288,083	8,280,000	2.23	%
Automotive	7,848,470	8,058,746	2.17	%
Transportation: Cargo	6,785,894	6,840,000	1.84	%
Energy: Oil & Gas	6,766,968	6,700,000	1.80	%
Insurance	5,410,226	5,500,000	1.48	%
Beverage, Food, & Tobacco	3,964,242	3,580,000	0.96	%
Hotel, Gaming, & Leisure	3,284,942	3,420,000	0.92	%
Environmental Industries	766,442	580,000	0.16	%
Services: Government	50,001	100,000	0.03	%
	$ 368,453,206	$ 371,839,772	100.00	%

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At December 31, 2018, our average portfolio company investment at amortized cost and fair value was approximately $8.9 million and $8.9 million, respectively, and our largest portfolio company investment at amortized cost and fair value was approximately $21.6 million and $22.3 million, respectively. At December 31, 2017, our average portfolio company investment at amortized cost and fair value was approximately $7.7 million and $7.4 million, respectively, and our largest portfolio company investment at amortized cost and fair value was approximately $22.5 million and $22.2 million, respectively.

At December 31, 2018, 91% of our debt investments bore interest based on floating rates (subject to interest rate floors), such as LIBOR, and 9% bore interest at fixed rates. At December 31, 2017, 87% of our debt investments bore interest based on floating rates (subject to interest rate floors), such as LIBOR, and 13% bore interest at fixed rates.

The weighted average yield on all of our debt investments as of December 31, 2018 and December 31, 2017 was approximately 10.9% and 10.8%, respectively. The weighted average yield was computed using the effective interest rates for all of our debt investments, including accretion of original issue discount. The weighted average yield of our debt investments is not the same as a return on investment for our stockholders, but, rather relates to a portion of our investment portfolio and is calculated before the payment of all of our subsidiaries fees and expenses.

As of December 31, 2018 and December 31, 2017, we had cash and cash equivalents of $17.5 million and $25.1 million, respectively.

Investment Activity

During the year ended December 31, 2018, we made $272.9 million of investments in seventeen new portfolio companies and twelve existing portfolio companies. During the year ended December 31, 2018, we received $147.6 million in proceeds principally from prepayments of our investments, including $22.9 million from amortization of certain other investments.

During the year ended December 31, 2017, we made $172.2 million of investments in fourteen new portfolio companies and two existing portfolio companies. During the year ended December 31, 2017, we received $172.3 million in proceeds principally from prepayments of our investments, including $7.2 million from amortization of certain other investments.

Our level of investment activity can vary substantially from period to period depending on many factors, including the amount of debt and equity capital to middle market companies, the level of merger and acquisition activity, the general economic environment and the competitive environment for the types of investments we make.

Asset Quality

In addition to various risk management and monitoring tools, Stellus Capital Management uses an investment rating system to characterize and monitor the credit profile and expected level of returns on each investment in our portfolio. This investment rating system uses a five-level numeric scale. The following is a description of the conditions associated with each investment category:

Investment Category 1 is used for investments that are performing above expectations, and whose risks remain favorable compared to the expected risk at the time of the original investment.
Investment Category 2 is used for investments that are performing within expectations and whose risks remain neutral compared to the expected risk at the time of the original investment. All new loans are initially rated 2.

Investment Category 3 is used for investments that are performing below expectations and that require closer monitoring, but where no loss of return or principal is expected. Portfolio companies with a rating of 3 may be out of compliance with financial covenants.

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Investment Category 4 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are often in work out. Investments with a rating of 4 are those for which some loss of return but no loss of principal is expected.
Investment Category 5 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are almost always in work out. Investments with a rating of 5 are those for which some loss of return and principal is expected.

	As of December 31, 2018 (dollars in millions)			As of December 31, 2017		
Investment Category	Fair Value	% of Total Portfolio	Number of Portfolio Companies(1)	Fair Value	% of Total Portfolio	Number of Portfolio Companies(1)
1	$ 92.5	18 %	13	$ 25.9	7 %	5
2	372.3	74 %	37	306.7	82 %	36
3	26.8	5 %	3	37.0	10 %	5
4	12.8	3 %	4	1.9	1 %	2
5	0.1	%	1	0.4	%	1
Total	$ 504.5	100 %	58	$ 371.9	100 %	49

(1) One portfolio company appears in two categories as of December 31, 2018 and December 31, 2017.

Loans and Debt Securities on Non-Accrual Status

We will not accrue interest on loans and debt securities if we have reason to doubt our ability to collect such interest. As of December 31, 2018, we had four loans on non-accrual status, which represented approximately 3.9% of our loan portfolio at cost and 2.8% at fair value. As of December 31, 2017, we had two loans on non-accrual status, which represented approximately 1.2% of our loan portfolio at cost and 0.3% at fair value.

Results of Operations

An important measure of our financial performance is net increase (decrease) in net assets resulting from operations, which includes net investment income (loss), net realized gain (loss) and net unrealized appreciation (depreciation). Net investment income (loss) is the difference between our income from interest, dividends, fees and other investment income and our operating expenses including interest on borrowed funds. Net realized gain (loss) on investments is the difference between the proceeds received from dispositions of portfolio investments and their amortized cost. Net unrealized appreciation (depreciation) on investments is the net change in the fair value of our investment portfolio.

Comparison of the Years ended December 31, 2018, 2017, and 2016

Revenues

We generate revenue in the form of interest income on debt investments and capital gains and distributions, if any, on investment securities that we may acquire in portfolio companies. Our debt investments typically have a term of five to seven years and bear interest at a fixed or floating rate. Interest on our debt securities is generally payable quarterly. Payments of principal on our debt investments may be amortized over the stated term of the investment, deferred for several years or due entirely at maturity. In some cases, our debt investments may pay interest in-kind, or PIK. Any outstanding principal amount of our debt securities and any accrued but unpaid interest will generally become due at the maturity date. The level of interest income we receive is directly related to the balance of interest-bearing investments multiplied by the weighted average yield of our investments. We expect that the total dollar amount of interest and any dividend income that we earn to increase as the size of our investment portfolio increases. In addition, we may generate revenue in the form of prepayment fees, commitment, loan origination, structuring or due diligence fees, fees for providing significant managerial assistance and consulting fees.

The following shows the breakdown of investment income for the years ended December 31, 2018, 2017, and 2016 (in millions).

	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
Interest Income[(1)]	$ 49.6	$ 37.6	$ 38.0
PIK Income	1.9	0.5	0.2
Miscellaneous fees[(1)]	1.8	1.6	1.3
Total	$ 53.3	$ 39.7	$ 39.5

(1) For the years ended December 31, 2018, 2017 and 2016, we recognized $3.4 million, $2.5 million and $1.6 million of non-recurring income, respectively. Non-recurring income was mostly related to early repayments and amendments to specific loan positions with the exception of the year ended December 31, 2018 which includes recognition of prior period interest reserve.

The increase in interest income from the respective periods were due primarily to growth in the overall investment portfolio and increased interest rates.

Expenses

Our primary operating expenses include the payment of fees to Stellus Capital Management under the investment advisory agreement, our allocable portion of overhead expenses under the administration agreement and other operating costs described below. We bear all other out-of-pocket costs and expenses of our operations and transactions, which may include:

- organization and offering;
- calculating our net asset value (including the cost and expenses of any independent valuation firm);
- fees and expenses payable to third parties, including agents, consultants or other advisors, in monitoring financial and legal affairs for us and in monitoring our investments and performing due diligence on our prospective portfolio companies or otherwise relating to, or associated with, evaluating and making investments;
- interest payable on debt, if any, incurred to finance our investments and expenses related to unsuccessful portfolio acquisition efforts;
- offerings of our common stock and other securities;
- base management and incentive fees;
- administration fees and expenses, if any, payable under the administration agreement (including our allocable portion of Stellus Capital Management s overhead in performing its obligations under the administration agreement, including rent and the allocable portion of the cost of our chief compliance officer and chief financial officer and his staff);
- transfer agent, dividend agent and custodial fees and expenses;
- U.S. federal and state registration fees;
- all costs of registration and listing our shares on any securities exchange;
- U.S. federal, state and local taxes;
- independent directors fees and expenses;

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costs of preparing and filing reports or other documents required by the SEC or other regulators;
costs of any reports, proxy statements or other notices to stockholders, including printing costs;
costs and fees associated with any fidelity bond, directors and officers/errors and omissions liability insurance, and any other insurance premiums;
direct costs and expenses of administration, including printing, mailing, long distance telephone, copying, secretarial and other staff, independent auditors and outside legal costs;
proxy voting expenses; and
all other expenses incurred by us or Stellus Capital Management in connection with administering our business.

The following shows the breakdown of operating expenses for the years ended December 31, 2018, 2017 and 2016 (in millions).

	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
Operating Expenses			
Management Fees	$ 8.2	$ 6.3	$ 6.3
Valuation Fees	0.3	0.3	0.4
Administrative services expenses	1.4	1.3	1.0
Income incentive fees	5.5	2.9	4.3
Capital gain incentive fees	0.1		
Professional fees	1.2	1.3	0.7
Directors fees	0.3	0.3	0.3
Insurance expense	0.3	0.4	0.5
Interest expense and other fees	12.3	7.9	8.0
Income tax expense	0.3		
Deferred offering costs			0.3
Other general and administrative	0.7	0.6	0.4
Total Operating Expenses	$ 30.6	$ 21.3	$ 22.2
Loss on extinguishment of debt		0.4	
Total Expenses	$ 30.6	$ 21.7	$ 22.2

The increase in operating expenses for the respective periods was primarily due to 1) an increase in management fees directly related to the growth of our portfolio, 2) increased interest expense due to the greater principal amount of the additional 2022 Notes, despite their lower annual interest rate as compared to the 2019 Notes, the higher balance and increased rates on the Credit Facility and SBA-guaranteed debentures outstanding during the period, and 3) higher income incentive fees and capital gains incentive fees due to performance of the portfolio.

Net Investment Income

Net investment income was $22.6 million, or $1.42 per common share based on 15,953,571 weighted-average common shares outstanding at December 31, 2018. Net investment income was $18.0 million, or $1.21 per common share based on 14,870,981 weighted-average common shares outstanding at December 31, 2017. Net investment income was $17.3 million, or $1.39 per common share based on 12,479,959 weighted-average common shares outstanding at December 31, 2016.

Net investment income for the year ended December 31, 2018 increased compared to the year ended December 31, 2017 as a result of an increase in interest income due to growth in the overall

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investment portfolio and increased interest rates, offset by an increase in management and incentive fees and interest expense incurred related to the portfolio growth.

Net Realized Gains and Losses

We measure realized gains or losses by the difference between the net proceeds from the repayment, sale or other disposition and the amortized cost basis of the investment, using the specific identification method, without regard to unrealized appreciation or depreciation previously recognized.

Proceeds from repayments of investments and amortization of certain other investments for the year ended December 31, 2018 totaled $147.5 million and net realized gains totaled $5.5 million from the realization of our equity investments in certain portfolio companies. Proceeds from repayments of investments and amortization of certain other investments for the year ended December 31, 2017 totaled $172.3 million and net realized gain totaled $4.7 million from the realization of our equity investments in certain portfolio companies. Proceeds from the sales and repayments of investments and amortization of certain other investments for the year ended December 31, 2016 totaled $55.9 million and net realized loss totaled $13.1 million, $12.2 million of which is related to the realized loss of our term loan to Binder and Binder.

Provision for Taxes on Realized Gains

In connection with the gain realized from the exit of its equity investment in Eating Recovery Center, LLC, the Company recorded an income tax provision on realized gains of $0.3 million for the year ended December 31, 2018. No income tax provision was recorded on realized gains for the years ended December 31, 2017 and 2016. As of December 31, 2018 and 2017, no tax liability related to the taxes on realized gains were included on the Consolidated Statement of Assets and Liabilities.

Net Change in Unrealized Appreciation (Depreciation) of Investments

Net change in unrealized appreciation primarily reflects the change in portfolio investment values during the reporting period, including the reversal of previously recorded appreciation or depreciation when gains or losses are realized.

Net change in unrealized appreciation (depreciation) on investments and cash equivalents for the year ended December 31, 2018, 2017 and 2016 totaled ($1.6) million, $22.0 thousand, and $18.6 million, respectively.

The change in unrealized depreciation in 2018 was due to a significant widening of spreads right at year end, offset by the write up of a specific equity investment. There was relatively no change in unrealized appreciation in 2017. The change in unrealized appreciation in 2016 was due primarily to two factors: a) the reversal of $8.3 million of unrealized depreciation accrued in prior years resulting from realized losses and b) $10.3 million from tightening interest rate spreads in 2016.

Provision for Taxes on Unrealized Appreciation on Investments

We have direct wholly owned subsidiaries that have elected to be taxable entities (the Taxable Subsidiaries). The Taxable Subsidiaries permit us to hold equity investments in portfolio companies which are pass through entities for tax purposes and continue to comply with the source-of-income requirements contained in RIC tax provisions of the Code. The Taxable Subsidiaries are not consolidated with us for income tax filing purposes and may generate income tax expense, benefit, and the related tax assets and liabilities, as a result of their ownership of certain portfolio investments. The income tax expense, or benefit, if any, and related tax assets and liabilities are reflected in our consolidated financial statements.

For the year ended December 31, 2018, 2017 and 2016, we recognized a deferred tax benefit (provision) related to unrealized appreciation on certain equity investments for income tax at our Taxable Subsidiaries of $(67.0) thousand, $9.0 thousand and $0.4 million, respectively. As of

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December 31, 2018 and 2017, a deferred tax liability of $67.0 thousand and $0, respectively, were included on the Consolidated Statement of Assets and Liabilities.

Net Increase in Net Assets Resulting from Operations

Net increase in net assets resulting from operations totaled $26.2 million, or $1.64 per common share based on weighted-average shares of 15,953,571 for the year ended December 31, 2018, as compared to $22.6 million, or $1.52 per common share based on weighted-average shares of 14,870,981 common shares outstanding for the year ended December 31, 2017, as compared to $23.2 million, or $1.86 per common share based on weighted-average shares of 12,479,959 common shares outstanding for the year ended December 31, 2016.

The increase in net assets resulting from operations for the year ended December 31, 2018 as compared to the year ended December 31, 2017 was higher due primarily to a higher net investment income due to the growth of the portfolio, as well as a larger amount of realized gains. The increase in net assets resulting from operations for the year ended December 31, 2017 as compared to the year ended December 31, 2016 was lower due to higher net unrealized gains on the portfolio in 2016, offset by net realized gains and a higher net investment income in 2017.

Financial Condition, Liquidity and Capital Resources

Cash Flows from Operating and Financing Activities

Our operating activities used net cash of $102.4 million for the year ended December 31, 2018, primarily in connection with the purchase of portfolio investments, offset by sales and repayments of portfolio investments. Our financing activities for the year ended December 31, 2018 provided cash of $94.8 million primarily from proceeds from SBA-guaranteed debentures and net borrowings on our credit facility.

Our operating activities provided net cash of $18.9 million for the year ended December 31, 2017, primarily in connection with the income earned on portfolio investments, offset by the purchase and origination of portfolio investments. Our financing activities for the year ended December 31, 2017 used cash of $2.9 million primarily from net repayments on our credit facility.

Our operating activities provided net cash of $8.8 million for the year ended December 31, 2016, primarily in connection with the sale and repayment of portfolio investments, offset by the purchase and origination of portfolio investments. Our financing activities for the year ended December 31, 2016 used cash of $10.5 million, primarily from repayments on our credit facility.

Liquidity and Capital Resources

Our liquidity and capital resources are derived from the Credit Facility, the 2022 Notes, SBA-guaranteed debentures and cash flows from operations, including investment sales and repayments, and income earned. Our primary use of funds from operations includes investments in portfolio companies and other operating expenses we incur, as well as the payment of dividends to the holders of our common stock. We used, and expect to continue to use, these capital resources as well as proceeds from turnover within our portfolio and from public and private offerings of securities to finance our investment activities.

Although we expect to fund the growth of our investment portfolio through the net proceeds from future public and private equity offerings and issuances of senior securities or future borrowings to the extent permitted by the 1940 Act, our plans to raise capital may not be successful. In this regard, if our common stock trades at a price below our then-current net asset value per share, we may be limited in our ability to raise equity capital given that we cannot sell our common stock at a price below net asset value per share unless our stockholders approve such a sale and our board of directors makes certain determinations in connection therewith. A proposal, approved by our stockholders at our 2018 annual stockholders meeting, authorizes us to sell shares equal to up to 25% of our outstanding common stock of our common stock below the then current net asset value per share of our common stock in one or more offerings. This authorization will expire on June 28, 2019, the one year anniversary of our 2018 annual stockholders meeting. We would need similar future approval from our stockholders to issue shares below the then current net asset value per share any time after the expiration of the current approval. In addition, we intend to distribute between 90% and 100% of our taxable income to our stockholders in order to satisfy the requirements applicable to RICs under Subchapter M of the Code. Consequently, we may not have the funds or the ability to fund new investments, to make additional investments in our portfolio companies, to fund our unfunded commitments to portfolio companies or to repay borrowings. In addition, the illiquidity of our portfolio investments may make it difficult for us to sell these investments when desired and, if we are required to sell these investments, we may realize significantly less than their recorded value.

Also, as a BDC, we generally are required to meet a coverage ratio of total assets, less liabilities and indebtedness not represented by senior securities, to total senior securities, which include all of our borrowings and any outstanding preferred stock, of at least 150% effective June 28, 2018 (at least 200% prior to June 28, 2018). This requirement limits the amount that we may borrow. We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the asset coverage test under the 1940 Act. We were in compliance with the asset coverage ratios at all times. As of December 31, 2018 and December 31, 2017, our asset coverage ratio was 251% and 346%, respectively. The amount of leverage that we employ will depend on our assessment of market conditions and other factors at the time of any proposed borrowing, such as the maturity, covenant package and rate structure of the proposed borrowings, our ability to raise funds through the issuance of shares of our common stock and the risks of such borrowings within the context of our investment outlook. Ultimately, we only intend to use leverage if the expected returns from borrowing to make investments will exceed the cost of such borrowing. As of December 31, 2018 and December 31, 2017, we had cash and cash equivalents of $17.5 million and $25.1 million, respectively.

Credit Facility

On November 7, 2012, the Company entered into a revolving credit facility (the Original Facility) with various lenders. SunTrust Bank, one of the lenders, served as administrative agent under the Original Facility. The Original Facility, as amended on November 21, 2014 and August 31, 2016, provided for borrowings in an aggregate amount of $120.0 million on a committed basis with an accordion feature that allowed the Company to increase the aggregate commitments up to $195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. The Company terminated the Original Facility on October 11, 2017, in conjunction with securing and entering into a new senior secured revolving credit agreement, dated as of October 10, 2017, as amended on March 28, 2018 and August 2, 2018, with ZB, N.A., dba Amegy Bank and various other lenders (the Credit Facility).

The Credit Facility, as amended, provides for borrowings up to a maximum of $180.0 million on a committed basis with an accordion feature that allows the Company to increase the aggregate commitments up to $195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions.

Borrowings under the Credit Facility bear interest, subject to the Company s election, on a per annum basis equal to (i) LIBOR plus 2.50% (or 2.75% during certain periods in which the Company s asset coverage ratio is equal to or below 1.90 to 1.00) with no LIBOR floor, or (ii) 1.50% (or 1.75% during certain periods in which the Company s asset coverage ratio is equal to or below 1.90 to 1.00) plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%. The Company pays unused commitment fees of 0.50% per annum on the unused lender commitments under the Credit Facility. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 10, 2021.

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The Company s obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. The Credit Facility contains certain covenants, including but not limited to: (i) maintaining a minimum liquidity test of at least $10.0 million, including cash, liquid investments and undrawn availability, (ii) maintaining an asset coverage ratio of at least 1.75 to 1.0, and (iii) maintaining a minimum stockholder s equity. As of December 31, 2018, the Company was in compliance with these covenants.

As of December 31, 2018 and December 31, 2017, the outstanding balance under the Credit Facility was $99.6 million and $40.8 million, respectively. The carrying amount of the amount outstanding under the Credit Facility approximates its fair value. The fair values of the Credit Facility is determined in accordance with ASC 820, which defines fair value in terms of the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of the Credit Facility is estimated based upon market interest rates for our own borrowings or entities with similar credit risk, adjusted for nonperformance risk, if any. The Company had previously incurred total costs of $3.1 million in connection with obtaining, amending, and maintaining the Original Facility. The Company incurred additional costs of $1.5 million in connection with the current Credit Facility, which are being amortized over the life of the facility. Additionally, $0.3 million of costs from the Original Facility will continue to be amortized over the remaining life of the Credit Facility. As of December 31, 2018 and 2017, $1.3 million and $1.4 million of such prepaid loan structure fees and administration fees had yet to be amortized, respectively. These prepaid loan fees are presented on our consolidated statement of assets and liabilities as a deduction from the debt liability attributable to the Credit Facility as required by ASU No. 2015-3.

Interest is paid quarterly in arrears. The following table summarizes the interest expense and amortized loan fees on the Credit Facility for the years ended December 31, 2018, 2017, and 2016 (dollars in millions):

	For the years ended		
	December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$ 3.7	$ 2.2	$ 3.4
Loan fee amortization	0.4	0.4	0.5
Commitment fees on unused portion	0.4	0.3	0.1
Administration fees	0.1	0.1	
Total interest and financing expenses	$ 4.6	$ 3.0	$ 4.0
Loss on extinguishment of debt	$	$ 0.1	$
Weighted average interest rate	4.7 %	3.7 %	3.2 %
Effective interest rate (including fee amortization)	5.7 %	5.0 %	3.7 %
Average debt outstanding	$ 79.8	$ 60.1	$ 106.6
Cash paid for interest and unused fees	$ 4.2	$ 2.5	$ 3.4

SBA-guaranteed debentures

Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. Under the regulations applicable to SBIC funds, a single licensee can have outstanding debentures guaranteed by the SBA subject to a regulatory leverage limit, up to two times the amount of regulatory capital. As of December 31, 2018 and 2017, the SBIC subsidiary had $75.0 million and $67.5 million, respectively, in regulatory capital, as such term is defined by the SBA.

On August 12, 2014, we obtained exemptive relief from the SEC to permit us to exclude the debt of the SBIC subsidiary guaranteed by the SBA from our asset coverage test under the 1940

Act. The exemptive relief provides us with increased flexibility under the asset coverage test by permitting us to borrow up to $150.0 million more than we would otherwise be able to absent the receipt of this exemptive relief.

On a stand-alone basis, the SBIC subsidiary held $225.5 million and $162.0 million in assets at December 31, 2018 and 2017, respectively, which accounted for approximately 42.9% and 40.4% of our total consolidated assets at December 31, 2018 and 2017, respectively.

Debentures guaranteed by the SBA have fixed interest rates that equal prevailing 10-year Treasury Note rates plus a market spread and have a maturity of ten years with interest payable semi-annually. The principal amount of the debentures is not required to be paid before maturity, but may be pre-paid at any time with no prepayment penalty. As of December 31, 2018 and 2017, the SBIC subsidiary had $150.0 million and $90.0 million of the SBA-guaranteed debentures outstanding, respectively. SBA-guaranteed debentures incur upfront fees of 3.425%, which consists of a 1.00% commitment fee and a 2.425% issuance discount, which are amortized over the life of the SBA-guaranteed debentures. Once pooled, which occurs in March and September each year, the SBA-guaranteed debentures bear interest at a fixed rate that is set to the current 10-year treasury rate plus a spread at each pooling date.

As of December 31, 2018 and 2017, the carrying amount of the SBA-guaranteed debentures approximated their fair value. The fair values of the SBA-guaranteed debentures are determined in accordance with ASC 820, which defines fair value in terms of the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of the SBA-guaranteed debentures are estimated based upon market interest rates for our own borrowings or entities with similar credit risk, adjusted for nonperformance risk, if any. At December 31, 2018 and 2017, the SBA-guaranteed debentures would be deemed to be Level 3, as defined in Note 6.

As of December 31, 2018, the Company has incurred $5.1 million in financing costs related to the SBA-guaranteed debentures since receiving our SBIC license, which were recorded as prepaid loan fees. As of December 31, 2018 and 2017, $3.6 million and $2.2 million of prepaid financing costs had yet to be amortized, respectively. These prepaid loan fees are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3. See Note 1 for further discussion.

The following table summarizes the interest expense and amortized fees on the SBA-guaranteed debentures for the years ended December 31, 2018, 2017 and 2016 (dollars in millions):

	For the years ended		
	December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$ 4.0	$ 2.1	$ 1.9
Debenture fee amortization	0.6	0.3	0.3
Total interest and financing expenses	$ 4.6	$ 2.4	$ 2.2
Weighted average interest rate	3.2 %	3.1 %	2.9 %
Effective interest rate (including fee amortization)	3.7 %	3.6 %	3.4 %
Average debt outstanding	$ 125.4	$ 67.3	$ 65.0
Cash paid for interest	$ 3.1	$ 2.0	$ 1.5

Notes

On May 5, 2014, the Company closed a public offering of $25.0 million aggregate principal amount of 6.50% notes (the 2019 Notes) due April 30, 2019. On August 21, 2017, the Company caused notices to be issued to the holders of its 2019 Notes regarding the Company s exercise of its option to redeem all of the issued and outstanding 2019 Notes, pursuant to Section 1101 of the Base Indenture dated as of May 5, 2014, between the Company and U.S. Bank National Association, as trustee, and Section 1.01(h)(i) of the First Supplemental Indenture dated as of May 5, 2014. The

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Company redeemed all $25.0 million in aggregate principal amount of the 2019 Notes on September 20, 2017. The 2019 Notes were redeemed at 100% of their principal amount, plus the accrued and unpaid interest thereon through the redemption date. As a result of the redemption, the Company recognized a loss on the extinguishment of debt of $0.3 million for the year ended December 31, 2017, due to the write off of the remaining deferred financing costs on the 2019 Notes.

The following table summarizes the interest expense and deferred financing costs on the 2019 Notes for the years ended December 31, 2018, 2017, and 2016 (dollars in millions):

	For the years ended December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$	$ 1.2	$ 1.6
Deferred financing costs		0.1	0.2
Total interest and financing expenses	$	$ 1.3	$ 1.8
Loss on extinguishment of debt		0.3	
Cash paid for interest	$	$ 1.4	$ 1.6

On August 21, 2017, the Company issued $42.5 million in aggregate principal amount of 5.75% fixed-rate notes due 2022 (the 2022 Notes). On September 8, 2017, the Company issued an additional $6.4 million in aggregate principal amount of the 2022 Notes pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at the Company s option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. Interest is payable quarterly beginning December 15, 2017.

The Company used all of the net proceeds from the 2022 Notes offering to fully redeem the 2019 Notes and a portion of the amount outstanding under the Original Facility. As of both December 31, 2018 and 2017, the aggregate carrying amount of all Notes was $48.9 million and the fair value of the Notes was approximately $47.6 million and $49.5 million, respectively. The 2022 Notes are listed on New York Stock Exchange under the trading symbol SCA . The fair value of the Notes is based on the closing price of the security, which is a Level 2 input under ASC 820 due to sufficient trading volume.

In connection with the issuance and maintenance of the 2022 Notes, we have incurred $1.7 million of fees that are being amortized over the term of the 2022 Notes, of which $1.2 million and $1.6 million remained to be amortized as of December 31, 2018 and 2017, respectively. These financing costs are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3.

The following table summarizes the interest expense and deferred financing costs on the 2022 Notes for the years ended December 31, 2018, 2017, 2016 (in millions):

	For the years ended December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$ 2.8	$ 1.0	$
Deferred financing costs	0.3	0.1	

Total interest and financing expenses	$ 3.1	$ 1.1	$
Cash paid for interest	$ 2.8	$ 0.9	$

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Contractual Obligations

As of December 31, 2018, our future fixed commitments for cash payments on contractual obligations for each of the next five years and thereafter are as follows:

	Total	2019	2020	2021	2022	2023	2024 and thereafter
	(dollars in thousands)						
Credit facility payable	$99,550			$99,550			
Notes payable	$48,875				$48,875		
SBA-guaranteed debentures	$150,000						$150,000
Total	$298,425	$	$	$99,550	$48,875	$	$150,000

Off-Balance Sheet Arrangements

We may be a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financial needs of our portfolio companies. As of December 31, 2018, our only off-balance sheet arrangements consisted of $21.2 million of unfunded commitments to provide debt financing to eleven of our portfolio companies. As of December 31, 2017, our only off-balance sheet arrangements consisted of a $8.7 million unfunded commitments to provide debt financing to four of our portfolio companies.

Regulated Investment Company Status and Dividends

We have elected to be treated as a RIC under Subchapter M of the Code. So long as we maintain our qualification as a RIC, we will not be taxed on our investment company taxable income or realized net capital gains, to the extent that such taxable income or gains are distributed, or deemed to be distributed, to stockholders as dividends on a timely basis.

Taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses, and generally excludes net unrealized appreciation or depreciation until realized. Distributions declared and paid by us in a year may differ from taxable income for that year as such dividends may include the distribution of current year taxable income or the distribution of prior year taxable income carried forward into and distributed in the current year. Distributions also may include returns of capital.

To qualify for RIC tax treatment, we must, among other things, distribute, with respect to each taxable year, at least 90% of our investment company net taxable income (i.e., our net ordinary income and our realized net short-term capital gains in excess of realized net long-term capital losses, if any). If we maintain our qualification as a RIC, we must also satisfy certain distribution requirements each calendar year in order to avoid a federal excise tax on our undistributed earnings of a RIC.

We intend to distribute to our stockholders between 90% and 100% of our annual taxable income (which includes our taxable interest and fee income). However, the covenants contained in the Credit Facility may prohibit us from making distributions to our stockholders, and, as a result, could hinder our ability to satisfy the distribution requirement. In addition, we may retain for investment some or all of our net taxable capital gains (i.e., realized net long-term capital gains in excess of realized net short-term capital losses) and treat such amounts as deemed distributions to our stockholders. If we do this, our stockholders will be treated as if they received actual distributions of the capital gains we retained and then reinvested the net after-tax proceeds in our common stock. Our stockholders also may be eligible to claim tax credits (or, in certain circumstances, tax refunds) equal to their allocable share of the tax we paid on the capital gains deemed distributed to them. To the extent our taxable earnings for a fiscal taxable year fall below the total amount of our dividends for that fiscal year, a portion of those dividend distributions may be deemed a return of capital to our stockholders.

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We may not be able to achieve operating results that will allow us to make distributions at a specific level or to increase the amount of these distributions from time to time. In addition, we may be limited in our ability to make distributions due to the asset coverage test for borrowings applicable to us as a business development company under the 1940 Act and due to provisions in Credit Facility. We cannot assure stockholders that they will receive any distributions or distributions at a particular level.

In accordance with certain applicable Treasury regulations and private letter rulings issued by the Internal Revenue Service, a RIC may treat a distribution of its own stock as fulfilling its RIC distribution requirements if each stockholder may elect to receive his or her entire distribution in either cash or stock of the RIC, subject to a limitation that the aggregate amount of cash to be distributed to all stockholders must be at least 20% of the aggregate declared distribution. If too many stockholders elect to receive cash, each stockholder electing to receive cash must receive a pro rata amount of cash (with the balance of the distribution paid in stock). In no event will any stockholder, electing to receive cash, receive less than 20% of his or her entire distribution in cash. If these and certain other requirements are met, for U.S. federal income tax purposes, the amount of the dividend paid in stock will be equal to the amount of cash that could have been received instead of stock. We have no current intention of paying dividends in shares of our stock in accordance with these Treasury regulations or private letter rulings.

Recent Accounting Pronouncements

See Note 1 to the financial statements for a description of recent accounting pronouncements, if any, including the expected dates of adoption and the anticipated impact on the financial statements.

Critical Accounting Policies

The preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Changes in the economic environment, financial markets and any other parameters used in determining such estimates could cause actual results to differ. In addition to the discussion below, our significant accounting policies are further described in the notes to the financial statements.

Valuation of portfolio investments

As a business development company, we generally invest in illiquid loans and securities including debt and equity securities of middle-market companies. Under procedures established by our Board, we value investments for which market quotations are readily available at such market quotations. We obtain these market values from an independent pricing service or at the mean between the bid and ask prices obtained from at least two brokers or dealers (if available, otherwise by a principal market maker or a primary market dealer). Debt and equity securities that are not publicly traded or whose market prices are not readily available are valued at fair value as determined in good faith by our Board. Such determination of fair values may involve subjective judgments and estimates, although we engage independent valuation providers to review the valuation of each portfolio investment that does not have a readily available market quotation at least once each quarter. Investments purchased within 90 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates value. With respect to unquoted securities, our Board, together with our independent valuation advisors, values each investment considering, among other measures, discounted cash flow models, comparisons of financial ratios of peer companies that are public and other factors.

When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, our Board uses the pricing indicated by the external event to corroborate and/or assist us in our valuation. Because there is not a readily available market for substantially all of the investments in our portfolio, we value most of our portfolio investments at fair value as determined in good faith by our Board using a documented valuation policy and a consistently applied valuation process. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material.

With respect to investments for which market quotations are not readily available, our Board undertakes a multi-step valuation process each quarter, as described below:

Our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals of Stellus Capital Management responsible for the portfolio investment;
Preliminary valuation conclusions are then documented and discussed with our senior investment professionals and Stellus Capital Management;
At least twice annually, the valuation for each portfolio investment is reviewed by an independent valuation firm;
The audit committee of our Board then reviews these preliminary valuations and makes a recommendation to our Board; and
The Board then discusses valuations and determines the fair value of each investment in our portfolio in good faith, based on the input of Stellus Capital Management, the independent valuation firm and the audit committee.

Revenue recognition

We record interest income on an accrual basis to the extent that we expect to collect such amounts. For loans and debt securities with contractual PIK interest, which represents contractual interest accrued and added to the loan balance that generally becomes due at maturity, we do not accrue PIK interest if the portfolio company valuation indicates that such PIK interest is not collectible. We will not accrue interest on loans and debt securities if we have reason to doubt our ability to collect such interest. Loan origination fees, original issue discount and market discount or premium are capitalized, and we then accrete or amortize such amounts using the effective interest method as interest income. Upon the prepayment of a loan or debt security, any unamortized loan origination is recorded as interest income. We record prepayment premiums on loans and debt securities as interest income. Dividend income, if any, will be recognized on the ex-dividend date.

We have investments in our portfolio that contain a PIK interest provision. Any PIK interest is added to the principal balance of such investments and is recorded as income, if the portfolio company valuation indicates that such PIK interest is collectible. In order to maintain our status as a RIC, substantially all of this income must be paid out to stockholders in the form of dividends, even if we have not collected any cash.

Net realized gains or losses and net change in unrealized appreciation or depreciation

We measure realized gains or losses by the difference between the net proceeds from the repayment, sale, or other disposition and the amortized cost basis of the investment, without regard to unrealized appreciation or depreciation previously recognized. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment values during the reporting period, including any reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

Capital Gains Incentive Fee

Under GAAP, we calculate the capital gains incentive fee payable to Stellus Capital Management as if we had realized all investments at their fair values as of the reporting date. Accordingly, we accrue a provisional capital gains incentive fee taking into account any unrealized gains or losses. As the provisional incentive fee is subject to the performance of investments until

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there is a realization event, the amount of provisional capital gains incentive fee accrued at a reporting date may vary from the incentive fee that is ultimately realized and the differences could be material.

Recent Developments

Investment Portfolio

On January 4, 2019, we received full repayment on the first lien term loan of EOS Fitness OPCO Holdings, LLC for total proceeds of $3.1 million. We also received a distribution related to our equity of $0.1 million.

On January 7, 2019, we received 0.3 million in full realization on the equity of OGS Holdings, Inc., resulting in a realized gain $0.2 million.

On February 4, 2019, we invested $8.5 million in the first lien term loan of ASC Communications, LLC, an existing portfolio company.

On February 8, 2019, we invested $12.3 million in the first lien term loan of Exacta Land Surveyors LLC, a provider of land surveys and field management services used to facilitate the purchasing, selling, and development of residential real estate in the U.S. Additionally, we committed $1.5 million in the unfunded revolver, $4.0 million in the unfunded delayed draw term loan, and we invested $1.0 million in the equity of the company.

On February 15, 2019, we received $0.05 million in full realization on the equity of Glori Energy Production, LLC.

On February 28, 2019, we invested $1.4 million in the first lien term loan of Convergence Technologies, Inc., an existing portfolio company. Additionally, we funded $5.4 million under the existing delayed draw term loan and an additional $0.1 million in the equity of the company.

Credit Facility

The outstanding balance under the Credit Facility as of March 4, 2019 was $112.8 million.

SBA-guaranteed Debentures

The total balance of SBA-guaranteed debentures outstanding as of March 4, 2019 was $150.0 million.

Dividend Declared

On January 11, 2019, the Company s Board declared a regular monthly dividend for each of January, February and March 2019.

Declared	Ex-Dividend Date	Record Date	Payment Date	Amount per Share
1/11/2019	1/30/2019	1/31/2019	2/15/2019	$ 0.1133
1/11/2019	2/27/2019	2/28/2019	3/15/2019	$ 0.1133
1/11/2019	3/28/2019	3/29/2019	4/15/2019	$ 0.1133

Quantitative and Qualitative Disclosures About Market Risk

We are subject to financial market risks, including changes in interest rates. For the year ended December 31, 2018 and 2017, 91% and 87% of the loans in our portfolio bore interest at floating rates, respectively. These floating rate loans typically bear interest in reference to LIBOR, which are indexed to 30-day or 90-day LIBOR rates, subject to an interest rate floor. December 31, 2018 and 2017, the weighted average interest rate floor on our floating rate loans was 0.94% and 0.92%, respectively.

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Assuming that the Statement of Assets and Liabilities as of December 31, 2018 were to remain constant and no actions were taken to alter the existing interest rate sensitivity, the following table shows the annual impact on net income of changes in interest rates:

	($ in millions)		
Change in Basis Points	Interest Income	Interest Expense	Net Interest Income[1]
Up 300 basis points	$ 13.2	$ (2.5)	$ 10.7
Up 200 basis points	9.0	(1.7)	7.3
Up 100 basis points	4.8	(0.8)	4.0
Down 100 basis points	(3.5)	0.8	(2.7)
Down 200 basis points	(6.6)	1.7	(4.9)
Down 300 basis points	(7.8)	2.5	(5.3)

(1) Excludes the impact of incentive fees based on pre-incentive fee net investment income. See Note 2 for more information on the incentive fee.

Although we believe that this measure is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in credit quality, size and composition of the assets on the balance sheet and other business developments that could affect net increase in net assets resulting from operations. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by this estimate. We may hedge against interest rate fluctuations by using standard hedging instruments such as futures, options and forward contacts subject to the requirements of the 1940 Act. While hedging activities may insulate us against adverse changes in interest rates, they may also limit our ability to participate in the benefits of lower interest rates with respect to our portfolio of investments. For the years ended December 31, 2018 and 2017, we did not engage in hedging activities.

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SENIOR SECURITIES

Information about our senior securities is shown in the following table for the fiscal years ended December 31, 2018, 2017, 2016, 2015, 2014, 2013 and 2012. The report of Grant Thornton LLP, our independent registered public accounting firm, on the senior securities table as of December 31, 2018, is attached as an exhibit to the registration statement of which this supplement prospectus is a part.

Class and Year	Total Amount Outstanding Exclusive of Treasury Securities[1] (Dollars in thousands)	Asset Coverage per Unit[2]	Involuntary Liquidating Preference per Unit[3]	Average Market Value per Unit[4]
SBA Debentures				
Fiscal 2014	$ 16,250	N/A [6]		N/A
Fiscal 2015	$ 65,000	N/A [6]		N/A
Fiscal 2016	$ 65,000	N/A [6]		N/A
Fiscal 2017	$ 90,000	N/A [6]		N/A
Fiscal 2018	$ 150,000	N/A [6]		N/A
Original Credit Facility[7]				
Fiscal 2012	$ 38,000	$ 3,090		N/A
Fiscal 2013	$ 110,000	$ 2,470		N/A
Fiscal 2014	$ 106,500	$ 2,320 [6]		N/A
Fiscal 2015	$ 109,500	$ 2,220 [6]		N/A
Fiscal 2016	$ 116,000	$ 2,210 [6]		N/A
Credit Facility				
Fiscal 2017	$ 40,750	$ 3,460 [6]		N/A
Fiscal 2018	$ 99,550	$ 2,520 [6]		N/A
5.75% Notes due 2022				
Fiscal 2017	$ 48,875	$ 3,460 [6]		$ 25.34
Fiscal 2018	$ 48,875	$ 2,520 [6]		$ 25.18
6.50% Notes due 2019[7]				
Fiscal 2014	$ 25,000	$ 2,320 [6]		$ 25.41
Fiscal 2015	$ 25,000	$ 2,220 [6]		$ 25.27
Fiscal 2016	$ 25,000	$ 2,210 [6]		$ 25.11
Short-Term Loan[5]				
Fiscal 2012	$ 45,000	$ 3,090		N/A
Fiscal 2013	$ 9,000	$ 2,470		N/A

(1) Total amount of senior securities outstanding at the end of the period presented.

(2) Asset coverage per unit is the ratio of the carrying value of our total assets, less all liabilities and indebtedness not represented by senior securities, in relation to the aggregate amount of senior securities representing indebtedness. Asset coverage per unit is expressed in terms of dollar amounts per $1,000 of indebtedness.

(3)

The amount to which such class of senior security would be entitled upon the involuntary liquidation of the issuer in preference to any security junior to it. The indicates information which the SEC expressly does not require to be disclosed for certain types of senior securities.

(4) Average market value per unit for the Notes represents the average of the daily closing prices as reported on the NYSE during the period presented. Average market value per unit for our SBA Debentures and Credit Facility are not applicable because these are not registered for public trading.

(5) Refers to short-term loans that the Company obtained from Raymond James and repaid in full on January 2, 2013 and January 2, 2014, respectively.

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(6) We have excluded our SBA-guaranteed debentures from the asset coverage calculation as of December 31, 2018, 2017, 2016, 2015 and 2014 pursuant to the exemptive relief granted by the SEC in August 2014 that permits us to exclude such debentures from the definition of senior securities in the 200% asset coverage ratio we are required to maintain under the 1940 Act.

(7) Such senior securities were retired during the 2017 fiscal year.

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PRICE RANGE OF COMMON STOCK AND DISTRIBUTIONS

Our common stock is traded on the NYSE under the symbol SCM. In connection with our initial public offering, our shares of common stock began trading on November 8, 2012, and before that date, there was no established trading market for our common stock.

The following table sets forth, for each fiscal quarter during the last two most recently completed fiscal years and the current fiscal year to date, the range of high and low closing prices of our common stock as reported on the NYSE, the sales price as a percentage of our net asset value.

Fiscal Year Ended	NAV Per Share(1)	Closing Sales Price(2) High	Closing Sales Price(2) Low	Premium or Discount of High Sales to NAV(3)	Premium or Discount of Low Sales to NAV(3)
December 31, 2019					
First Quarter (through March 13, 2019)	*	$ 15.20	$ 13.27	*	*
December 31, 2018					
Fourth Quarter	$ 14.09	$ 13.65	$ 11.91	-3.12 %	-15.47 %
Third Quarter	$ 14.29	$ 13.98	$ 12.79	-2.17 %	-10.50 %
Second Quarter	$ 14.07	$ 13.60	$ 11.56	-3.34 %	-17.84 %
First Quarter	$ 13.93	$ 13.00	$ 11.34	-6.67 %	-18.59 %
December 31, 2017					
Fourth Quarter	$ 13.81	$ 14.29	$ 12.19	3.48 %	-11.73 %
Third Quarter	$ 13.85	$ 13.85	$ 13.30		-3.97 %
Second Quarter	$ 13.84	$ 14.55	$ 13.25	5.13 %	-4.26 %
First Quarter	$ 13.84	$ 14.57	$ 12.09	5.27 %	-12.64 %

(1) Net asset value is determined as of the last date in the relevant quarter and therefore may not reflect the net asset value per share on the date of the high and low sales prices. The net asset values shown are based on outstanding shares at the end of each period.

(2) Closing sales price is determined as the high or low closing sales price noted within the respective quarter, not adjusted for dividends.

(3) Calculated as of the respective high or low sales price divided by the quarter end net asset value.

* Not determinable at the time of filing.

On March 13, 2019, the last reported sales price of our common stock was $14.68 per share. As of March 13, 2019, we had 8 stockholders of record, which did not include stockholders for whom shares are held in nominee or street name.

Shares of BDCs may trade at a market price that is less than the value of the net assets attributable to those shares. The possibility that our shares of common stock will trade at a discount from net asset value or at premiums that are unsustainable over the long term are separate and distinct from the risk that our net asset value will decrease. Since they began trading on November 8, 2012, in connection with our initial public offering, our shares of common stock have traded at times at a discount to the net assets attributable to those shares.

To the extent that we have income available, we intend to make monthly distributions to our stockholders. Our monthly stockholder distributions, if any, will be determined by our board of directors. Any stockholder distribution to our stockholders will be declared out of assets legally available for distribution.

We have elected to be treated as a RIC under the Code. To maintain RIC tax treatment, we must distribute at least 90% of our net ordinary income and net short-term capital gains in excess of our net long-term capital losses, if any, to our stockholders. In order to avoid certain excise taxes imposed on RICs, we currently intend to distribute during each calendar year an amount at least equal to the sum of: (a) 98% of our net ordinary income for such calendar year; (b) 98.2% of our capital gain net income for the one-year period ending on October 31 of the calendar year; and (c) any net ordinary income and capital gain net income for preceding years that were not distributed during such years and on which we previously paid no U.S. federal income tax.

We currently intend to distribute net capital gains (*i.e.*, net long-term capital gains in excess of net short-term capital losses), if any, at least annually out of the assets legally available for such distributions. However, we may decide in the future to retain such capital gains for investment and elect to treat such gains as deemed distributions to you. If this happens, you will be treated for U.S. federal income tax purposes as if you had received an actual distribution of the capital gains that we retain and reinvested the net after tax proceeds in us. In this situation, you would be eligible to claim a tax credit (or in certain circumstances a tax refund) equal to your allocable share of the tax we paid on the capital gains deemed distributed to you. See Material U.S. Federal Income Tax Considerations in this prospectus supplement. We cannot assure you that we will achieve results that will permit us to pay any cash distributions, and if we issue senior securities, we may be prohibited from making distributions if doing so would cause us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or if such distributions are limited by the terms of any of our borrowings.

We have adopted an opt out dividend reinvestment plan for our common stockholders. Unless you elect to receive your distributions in cash, we intend to make such distributions in additional shares of our common stock under our dividend reinvestment plan. Although distributions paid in the form of additional shares of our common stock will generally be subject to U.S. federal, state and local taxes in the same manner as cash distributions, investors participating in our dividend reinvestment plan will not receive any corresponding cash distributions with which to pay any such applicable taxes. If you hold shares of our common stock in the name of a broker or financial intermediary, you should contact such broker or financial intermediary regarding your election to receive distributions in cash in lieu of shares of our common stock. Any distributions reinvested through the issuance of shares through our dividend reinvestment plan will increase our gross assets on which the base management fee and the incentive fee are determined and paid to Stellus Capital Management. See Dividend Reinvestment Plan beginning on page 127 of the accompanying prospectus.

The following table summarizes our distributions per share that our board of directors has declared on our common stock since January 1, 2018:

Date Declared	Record Date	Payment Date	Per Share
Fiscal 2018			
January 11, 2018	January 31, 2018	February 15, 2018	$ 0.1133
January 11, 2018	February 28, 2018	March 15, 2018	$ 0.1133
January 11, 2018	March 29, 2018	April 13, 2018	$ 0.1133
April 16, 2018	April 30, 2018	May 15, 2018	$ 0.1133
April 16, 2018	May 31, 2018	June 15, 2018	$ 0.1133
April 16, 2018	June 29, 2018	July 13, 2018	$ 0.1133
July 12, 2018	July 31, 2018	August 15, 2018	$ 0.1133
July 12, 2018	August 31, 2018	September 14, 2018	$ 0.1133
July 12, 2018	September 28, 2018	October 15, 2018	$ 0.1133
October 16, 2018	October 31, 2018	November 15, 2018	$ 0.1133
October 16, 2018	November 29, 2018	December 14, 2018	$ 0.1133
October 16, 2018	December 31, 2018	January 15, 2019	$ 0.1133
Total			$ 1.3596

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UNDERWRITING

Under the terms and subject to the conditions contained in an underwriting agreement dated March 15, 2019, the underwriters named below, for whom Raymond James and Keefe, Bruyette & Woods, Inc. are acting as representatives, have severally agreed to purchase, and we have agreed to sell to them, the number of shares of common stock indicated below:

Underwriter	Number of Shares
Raymond James & Associates, Inc.	976,250
Keefe, Bruyette & Woods, Inc.	838,750
Goldman Sachs & Co. LLC	412,500
Ladenburg Thalmann & Co. Inc.	220,000
Janney Montgomery Scott LLC	192,500
BB&T Capital Markets, a division of BB&T Securities, LLC	110,000
Total	**2,750,000**

The underwriting agreement provides that the obligations of the underwriters to pay for and accept delivery of the shares of common stock offered hereby are subject to the approval of certain legal matters by their counsel and to certain other conditions. The underwriters are severally obligated to take and pay for all shares of common stock offered hereby (other than those covered by the underwriters option to purchase additional shares described below) if any such shares are taken. The offering of the common stock by the underwriters is subject to receipt and acceptance and subject to the underwriters right to reject any order in whole or in part. We have agreed to indemnify the several underwriters against certain liabilities, including liabilities under the Securities Act.

Our common stock is listed on the NYSE under the symbol SCM.

The underwriters are purchasing the shares of common stock from us at $14.09 per share (representing approximately $38.7 million aggregate proceeds to us, before we deduct our aggregate out-of-pocket expenses of approximately $135,000, or approximately $44.6 million if the underwriters option to purchase additional shares described below is exercised in full). Stellus Capital Management had agreed to bear $652,300, or $0.2372 per share, of the commissions (sales load) to be paid to the underwriters in connection with this offering, or $750,145 if the underwriters option to purchase additional shares is exercised in full.

Option to Purchase Additional Shares

We have granted to the underwriters an option, exercisable for 30 days from the date of this prospectus supplement, to purchase up to an aggregate of 412,500 additional shares of common stock at the price set forth on the cover page of this prospectus supplement. To the extent such option is exercised, each underwriter will become obligated, subject to certain conditions, to purchase approximately the same percentage of such additional shares of common stock as the number set forth next to such underwriter s name in the preceding table bears to the total number of shares set forth next to the names of all underwriters in the preceding table.

Lock-Up Agreements

We, and our executive officers and directors, have agreed, subject to certain exceptions, not to issue, sell, offer to sell, contract or agree to sell, hypothecate, pledge, transfer, grant any option to purchase, establish an open put equivalent position or otherwise dispose of or agree to dispose of directly or indirectly, any shares of our common stock, or any securities convertible into or exercisable or exchangeable for any shares of our common stock or any right to acquire shares of our common stock, for 90 days from the date of this prospectus supplement, subject to extension upon material announcements or earnings releases. The representatives, at any time and without notice, may release all or any portion of the common stock subject to the foregoing lock-up agreements.

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Price Stabilization, Short Positions and Penalty Bids

In connection with this offering, the underwriters may purchase and sell shares of our common stock in the open market. These transactions may include over-allotment, syndicate covering transactions and stabilizing transactions. An over-allotment involves syndicate sales of shares in excess of the number of shares to be purchased by the underwriters in the offering, which creates a syndicate short position. Syndicate covering transactions involve purchases of shares in the open market after the distribution has been completed in order to cover syndicate short positions.

Stabilizing transactions consist of some bids or purchases of shares of our common stock made for the purpose of preventing or slowing a decline in the market price of the shares while the offering is in progress.

In addition, the underwriters may impose penalty bids, under which they may reclaim the selling concession from a syndicate member when the shares of our common stock originally sold by that syndicate member are purchased in a stabilizing transaction or syndicate covering transaction to cover syndicate short positions.

Similar to other purchase transactions, these activities may have the effect of raising or maintaining the market price of the common stock or preventing or slowing a decline in the market price of the common stock. As a result, the price of the common stock may be higher than the price that might otherwise exist in the open market. Except for the sale of shares of our common stock in this offering, the underwriters may carry out these transactions on the NYSE, in the over-the-counter market or otherwise.

Neither the underwriters nor we make any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the price of the shares. In addition, neither the underwriters nor we make any representation that the underwriters will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

Conflicts of Interest

An affiliate of Keefe, Bruyette & Woods, Inc., an underwriter in this offering, acts as a lender and/or agent under the Credit Facility. Certain of the net proceeds from the sale of our common stock, not including underwriting compensation, may be paid to such affiliate of Keefe, Bruyette & Woods, Inc. in connection with the repayment of debt owed under the Credit Facility. As a result, Keefe, Bruyette & Woods, Inc. and/or its affiliate may receive more than 5% of the net proceeds of this offering, not including underwriting compensation.

The underwriters and their respective affiliates are full service financial institutions engaged in various activities, which may include sales and trading, commercial and investment banking, advisory, investment management, investment research, principal investment, hedging, market making, brokerage and other financial and non-financial activities and services. The underwriters and/or their affiliates from time to time provide and may in the future provide investment banking, commercial banking and financial advisory services to us, for which they have received and may receive customary compensation.

In the ordinary course of their various business activities, the underwriters and their respective affiliates, officers, directors and employees may purchase, sell or hold a broad array of investments and actively trade securities, derivatives, loans, commodities, currencies, credit default swaps and other financial instruments for their own account and for the accounts of their customers, and such investment and trading activities may involve or relate to our assets, securities and/or instruments (directly, as collateral securing other obligations or otherwise) and/or persons and entities with relationships with us. The underwriters and their respective affiliates may also communicate independent investment recommendations, market color or trading ideas and/or publish or express independent research views in respect of such assets, securities or instruments and may at any time hold, or recommend to clients that they should acquire, long

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and/or short positions in such assets, securities and instruments. In addition, the underwriters and/or their affiliates may from time to time refer investment banking clients to us as potential portfolio investments. If we invest in those clients, we may utilize net proceeds from this offering to fund such investments, and the referring underwriter or its affiliate may receive placement fees from its client in connection with such financing, which placement fees may be paid out of the amount funded by us.

The addresses of the underwriters are: Raymond James & Associates, Inc., 880 Carillon Parkway, St. Petersburg, Florida 33716 and Keefe, Bruyette & Woods, Inc. 787 7th Avenue, 4th Floor, New York, NY 10019.

Selling Restrictions

European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a Relevant Member State) with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the Relevant Implementation Date) an offer of shares may not be made to the public in that Relevant Member State other than:

(a) to any legal entity which is a qualified investor as defined in the Prospectus Directive;

(b) to fewer than 100 or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, 150, natural or legal persons (other than qualified investors as defined in the Prospectus Directive), as permitted under the Prospectus Directive, subject to obtaining the prior consent of the representative of the several underwriters; or

(c) in any other circumstances falling within Article 3(2) of the Prospectus Directive,

provided that no such offer of shares of our common stock shall require us or any underwriter to publish a prospectus pursuant to Article 3 of the Prospectus Directive or supplement a prospectus pursuant to Article 16 of the Prospectus Directive.

For the purposes of this provision, the expression an offer of shares to the public in relation to any shares of our common stock in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the shares of our common stock to be offered so as to enable an investor to decide to purchase or subscribe for any shares of our common stock, as the same may be varied in that Relevant Member State by any measure implementing the Prospectus Directive in that Relevant Member State. The expression Prospectus Directive means Directive 2003/71/EC (and amendments thereto, including the 2010 PD Amending Directive to the extent implemented in the Relevant Member State) and includes any relevant implementing measure in each Relevant Member State and the expression 2010 PD Amending Directive means Directive 2010/73/EU.

The sellers of shares of our common stock have not authorized and do not authorize the making of any offer of shares of our common stock through any financial intermediary, other than offers made by the underwriters with a view to underwriting the shares of our common stock as contemplated in this prospectus supplement and the accompanying prospectus. Accordingly, no purchaser of shares of our common stock, other than the underwriters, is authorized to make any further offer of shares of our common stock on behalf of the sellers or the underwriters.

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United Kingdom

Each underwriter has represented and agreed that:

(a) it has complied and will comply with all applicable provisions of the Financial Services and Markets Act 2000 (FSMA) with respect to anything done by it in relation to the shares of common stock in, from or otherwise involving the United Kingdom; and

(b) it will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue and sale of such shares of common stock in circumstances in which Section 21(1) of the FSMA does not apply to us.

Japan

The securities have not been and will not be registered under the Financial Instruments and Exchange Law of Japan (the Financial Instruments and Exchange Law) and each underwriter has agreed that it will not offer or sell any securities, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Financial Instruments and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

Hong Kong

The shares may not be offered or sold by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), or (ii) to professional investors within the meaning of the Securities and Futures Ordinance (Cap.571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances which do not result in the document being a prospectus within the meaning of the Companies Ordinance (Cap.32, Laws of Hong Kong), and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to shares which are or are intended to be disposed of only to persons outside Hong Kong or only to professional investors within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Singapore

This prospectus supplement and the accompanying prospectus have not been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, this prospectus and any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the shares may not be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the SFA), (ii) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA. Where the shares are subscribed or purchased under Section 275 of the SFA by a relevant person which is: (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries rights and interest in that trust will not be transferable for

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six months after that corporation or that trust has acquired the shares under Section 275 of the SFA except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A) of the SFA and in accordance with the conditions specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

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LEGAL MATTERS

Certain legal matters regarding the shares of common stock offered by this prospectus will be passed upon for us by Eversheds Sutherland (US) LLP, Washington, DC 20001. Certain legal matters in connection with the offering will be passed upon for the underwriters by Mayer Brown LLP, New York, NY.

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The financial statements, financial highlights and senior securities table of Stellus Capital Investment Corporation included in this prospectus and elsewhere in the registration statement have been so included in reliance upon the reports of Grant Thornton LLP. Grant Thornton LLP, located at 171 N. Clark Street, Chicago, Illinois, 60601, serves as the Company s independent registered public accounting firm, providing audit services and review of certain documents to be filed with the SEC.

AVAILABLE INFORMATION

We have filed with the SEC a registration statement on Form N-2, together with all amendments and related exhibits, under the Securities Act with respect to the shares of common stock offered by this prospectus supplement. The registration statement contains additional information about us and the shares of common stock being offered by this prospectus supplement.

We also file with or submit to the SEC annual, quarterly and current reports, proxy statements and other information meeting the informational requirements of the Exchange Act. You may inspect and copy these reports, proxy statements and other information, as well as the registration statement and related exhibits and schedules, at the SEC s website *www.sec.gov*.

We maintain a website at *www.stelluscapital.com* and make all of our annual, quarterly and current reports, proxy statements and other publicly filed information available, free of charge, on or through our website. Information contained on our website is not incorporated into this prospectus supplement or the accompanying prospectus, and you should not consider information on our website to be part of this prospectus supplement or the accompanying prospectus. You may also obtain such information by contacting us in writing at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, Attention: Investor Relations. The SEC maintains a website that contains reports, proxy and information statements and other information we file with the SEC at *www.sec.gov*. Copies of these reports, proxy and information statements and other information may also be obtained, after paying a duplicating fee, by electronic request at the following e-mail address: *publicinfo@sec.gov*.

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Stellus Capital Investment Corporation

Opinion on the financial statements

We have audited the accompanying consolidated statements of assets and liabilities of Stellus Capital Investment Corporation (a Maryland corporation) and subsidiaries (the Company), including the consolidated schedules of investments, as of December 31, 2018 and 2017, the related consolidated statements of operations, changes in net assets, and cash flows for each of the three years in the period ended December 31, 2018, and the related notes, schedules and financial highlights (collectively referred to as the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, and the financial highlights for each of the five years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company s internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 5, 2019 expressed an unqualified opinion.

Basis for opinion

These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on the Company s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures include examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our procedures included verification by confirmation of securities as of December 31, 2018 and 2017, by correspondence with the portfolio companies and custodians, or by other appropriate auditing procedures where replies were not received. We believe that our audits provide a reasonable basis for our opinion.

/s/ GRANT THORNTON LLP

We have served as the Company s auditor since 2012.
Dallas, Texas

March 5, 2019

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Stellus Capital Investment Corporation

Opinion on internal control over financial reporting

We have audited the internal control over financial reporting of Stellus Capital Investment Corporation (a Maryland corporation) and subsidiaries (the Company) as of December 31, 2018, based on criteria established in the 2013 Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018, based on criteria established in the 2013 Internal Control Integrated Framework issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements of the Company, as of and for the year ended December 31, 2018 and our report dated March 5, 2019, expressed an unqualified opinion on those financial statements.

Basis for opinion

The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and limitations of internal control over financial reporting

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

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Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ GRANT THORNTON LLP

Dallas, Texas
March 5, 2019

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PART I FINANCIAL INFORMATION STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

	December 31, 2018	December 31, 2017
ASSETS		
Non-controlled, affiliated investments, at fair value (amortized cost of $52,185 and $1,052,185, respectively)	$50,000	$990,000
Non-controlled, non-affiliated investments, at fair value (amortized cost of $502,691,464 and $367,401,021, respectively)	504,433,668	370,849,772
Cash and cash equivalents	17,467,146	25,110,718
Receivable for sales and repayments of investments	99,213	26,891
Interest receivable	3,788,684	2,922,204
Other receivables	85,246	
Deferred offering costs	18,673	
Prepaid expenses	344,621	361,270
Total Assets	$526,287,251	$400,260,855
LIABILITIES		
Notes payable	$47,641,797	$47,306,488
Credit facility payable	98,237,227	39,332,479
SBA-guaranteed debentures	146,387,802	87,818,813
Dividends payable	1,807,570	1,806,671
Management fees payable	2,183,975	1,621,592
Income incentive fees payable	1,936,538	371,647
Capital gains incentive fees payable	81,038	
Interest payable	1,863,566	1,021,173
Unearned revenue	410,593	139,304
Administrative services payable	392,191	327,033
Deferred tax liability	67,953	
Income tax payable	316,092	
Other accrued expenses and liabilities	115,902	268,413
Total Liabilities	$301,442,244	$180,013,613
Commitments and contingencies (Note 7)		
Net Assets	$224,845,007	$220,247,242
NET ASSETS		
Common Stock, par value $0.001 per share (200,000,000 shares and 100,000,000 shares authorized; 15,953,810 and 15,945,879 issued and outstanding, respectively)	$15,954	$15,946
Paid-in capital	228,160,491	228,066,762
	(10,786,240)	(10,786,240)

Accumulated net realized loss from investments, net of cumulative dividends of $9,519,362 and $4,246,819, respectively, and tax provision on realized gain of $267,975 and $0, respectively		
Accumulated undistributed net investment income	5,782,736	(435,794)
Net unrealized appreciation on non-controlled, non-affiliated investments and cash equivalents, net of provision for taxes of $67,953 and $0, respectively (Note 13)	1,674,251	3,448,753
Net unrealized depreciation on non-controlled, affiliated investments	(2,185)	(62,185)
Net Assets	$224,845,007	$220,247,242
Total Liabilities and Net Assets	$526,287,251	$400,260,855
Net Asset Value Per Share	$14.09	$13.81

See accompanying notes to these consolidated financial statements.

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
INVESTMENT INCOME			
Interest income	$51,463,033	$38,071,449	$38,176,617
Other income	1,803,305	1,576,744	1,313,580
Total Investment Income	$53,266,338	$39,648,193	$39,490,197
OPERATING EXPENSES			
Management fees	$8,154,842	$6,255,911	$6,281,863
Valuation fees	307,838	336,300	397,330
Administrative services expenses	1,390,375	1,245,727	1,045,648
Income incentive fees	5,529,376	2,911,392	4,275,436
Capital gains incentive fees	81,038		
Professional fees	1,189,071	1,274,066	712,524
Directors fees	317,000	331,000	324,000
Insurance expense	348,500	429,897	471,427
Interest expense and other fees	12,338,755	7,855,211	7,992,185
Income tax expense	275,106		
Deferred offering costs			261,761
Other general and administrative expenses	697,900	621,204	415,822
Total Operating Expenses	$30,629,801	$21,260,708	$22,177,996
Loss on extinguishment of debt		416,725	
Net Investment Income	$22,636,537	$17,970,760	$17,312,201
Net realized gain (loss) on non-controlled, non-affiliated investments and cash equivalents	$5,540,518	$4,655,976	$(13,089,671)
Tax provision on realized gain on investments	(267,975)		
Net change in unrealized appreciation (depreciation) on non-controlled, non-affiliated investments and cash equivalents	$(1,706,549)	$40,113	$18,603,401
Net change in unrealized appreciation (depreciation) on non-controlled, affiliated investments and cash equivalents	60,000	(62,185)	
Benefit (provision) for taxes on net unrealized gain (loss) on investments	$(67,953)	$8,593	$373,131
Net Increase in Net Assets Resulting from Operations	$26,194,578	$22,613,257	$23,199,062
Net Investment Income Per Share	$1.42	$1.21	$1.39
Net Increase in Net Assets Resulting from Operations Per Share	$1.64	$1.52	$1.86

Weighted Average Shares of Common Stock Outstanding	15,953,571	14,870,981	12,479,959
Distributions Per Share	$1.36	$1.36	$1.36

See accompanying notes to these consolidated financial statements.

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Increase in Net Assets Resulting from Operations			
Net investment income	$22,636,537	$17,970,760	$17,312,201
Net realized gain (loss) on investments and cash equivalents	5,540,518	4,655,976	(13,089,671)
Tax provision on realized gain on investments	(267,975)		
Net change in unrealized appreciation (depreciation) on non-controlled, non-affiliated investments and cash equivalents	(1,706,549)	40,113	18,603,401
Net change in unrealized appreciation (depreciation) on non-controlled, affiliated investments and cash equivalents	60,000	(62,185)	
Benefit (provision) for taxes on unrealized appreciation on investments	(67,953)	8,593	373,131
Net Increase in Net Assets Resulting from Operations	$26,194,578	$22,613,257	$23,199,062
Stockholder distributions from:			
Net investment income	(16,418,007)	(17,970,760)	(16,968,350)
Net realized capital gains	(5,272,543)	(2,352,545)	
Total Distributions	$(21,690,550)	$(20,323,305)	$(16,968,350)
Capital Share Transactions			
Issuance of common stock	$94,788	$48,741,549	$
Sales load		(1,358,880)	
Offering costs		(307,022)	
Partial share redemption	(1,051)	(142)	(31)
Net Increase (Decrease) in Net Assets Resulting From Capital Share Transactions	$93,737	$47,075,505	$(31)
Total Increase in Net Assets	$4,597,765	$49,365,457	$6,230,681
Net Assets at Beginning of Period	$220,247,242	$170,881,785	$164,651,104
Net Assets at End of Period (Includes $5,782,736, $(435,794) and $(435,794) of Accumulated Undistributed Net Investment Income (Loss), Respectively)	$224,845,007	$220,247,242	$170,881,785

See accompanying notes to these consolidated financial statements.

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Cash flows from operating activities			
Net Increase in net assets resulting from operations	$26,194,578	$22,613,257	$23,199,062
Adjustments to reconcile net increase in net assets resulting from operations to net cash provided by (used in) operating activities:			
Purchases of investments	(272,927,459)	(172,171,246)	(65,661,034)
Proceeds from sales and repayments of investments	147,528,448	172,260,541	55,949,177
Net change in unrealized depreciation (appreciation) on investments	1,646,549	22,072	(18,603,401)
Increase in investments due to PIK	(1,869,905)	(499,595)	(243,766)
Amortization of premium and accretion of discount, net	(1,553,333)	(1,196,566)	(1,128,511)
Deferred tax provision (benefit)	67,953	(8,593)	(373,130)
Amortization of loan structure fees	456,151	455,893	523,835
Amortization of deferred financing costs	335,309	251,826	326,190
Amortization of loan fees on SBA-guaranteed debentures	623,989	333,027	184,783
Net realized (gain) loss on investments	(5,540,518)	(4,655,976)	13,089,341
Loss on extinguishment of debt		416,725	
Deferred offering costs			261,761
Changes in other assets and liabilities			
Decrease (increase) in interest receivable	(866,480)	1,679,538	118,289
Decrease (increase) in other receivable	(85,246)	748	6,936
Decrease in prepaid expenses	16,649	94,949	19,230
Increase in management fees payable	562,383	13,297	89,516
Increase (decrease) in incentive fees payable	1,564,891	(981,624)	745,315
Increase in capital gains incentive fees payable	81,038		
Increase (decrease) in administrative services payable	65,158	54,522	(125,288)
Increase in interest payable	842,393	47,361	403,623
Increase (decrease) in unearned revenue	271,289	119,349	(16,922)
Increase in income tax payable	316,092		
Increase (decrease) in other accrued expenses and liabilities	(152,511)	1,022	71,714
	$(102,422,582)	$18,850,527	$8,836,720

Net Cash Provided by (Used in) Operating Activities

See accompanying notes to these consolidated financial statements.

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Cash flows from financing activities			
Proceeds from the issuance of common stock	$	$48,741,549	$
Sales load for common stock issued		(1,358,880)	
Offering costs paid for common stock	(18,673)	(307,022)	
Proceeds from notes issued		48,875,000	
Financing costs paid for Notes issued		(1,688,961)	
Repayments on Notes issued		(25,000,000)	
Stockholder distributions paid	(21,594,863)	(19,930,616)	(16,968,350)
Proceeds from SBA Debentures	60,000,000	25,000,000	
Financing costs paid on SBA Debentures	(2,055,000)	(856,250)	
Borrowings under Credit Facility	246,300,000	194,250,000	56,500,000
Repayments of Credit Facility	(187,500,000)	(269,500,000)	(50,000,000)
Financing costs paid on Credit facility	(351,403)	(1,158,616)	(50,000)
Partial Share Redemption	(1,051)	(142)	(31)
Net Cash Provided by (Used in) Financing Activities	$94,779,010	$(2,933,938)	$(10,518,381)
Net Increase (Decrease) in Cash and Cash Equivalents	$(7,643,572)	$15,916,589	$(1,681,661)
Cash and cash equivalents balance at beginning of period	25,110,718	9,194,129	10,875,790
Cash and Cash Equivalents Balance at End of Period	$17,467,146	$25,110,718	$9,194,129
Supplemental and Non-Cash Activities			
Cash paid for interest expense	$10,075,913	$6,762,104	$6,548,754
Excise tax paid	27,717	37,648	
Shares issued pursuant to Dividend Reinvestment Plan	94,788		
Conversion from debt to equity		864,101	
Increase in Distribution Payable	899	392,689	

See accompanying notes to these consolidated financial statements.

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments
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Consolidated Schedule of Investments (continued) December 31, 2018

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Consolidated Schedule of Investments (continued) December 31, 2018

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2018

(1) See Note 1 of the Notes to the Consolidated Financial Statements for a discussion of the methodologies used to value securities in the portfolio.

(2) Investments held by the SBIC subsidiary, which include $13,410,706 of cash and $214,114,498 of investments (at cost) are excluded from the obligations to the lenders of the Credit Facility. The Company s obligations to the lenders of the Credit Facility, as defined in Note 9, are secured by a first priority security interest in all investments and cash and cash equivalents, except for investments held by the SBIC Subsidiary.

(3) Excluded from the investment is an undrawn delayed draw term loan commitment in an amount not to exceed $865,385, with an interest rate of LIBOR plus 7.50% and a maturity of June 30, 2023. This investment is accruing an unused commitment fee of 0.375% per annum.

(4) Security is non-income producing.

(5) The investment is not a qualifying asset under the Investment Company Act of 1940, as amended. The Company may not acquire any non-qualifying assets unless, at the time of the acquisition, qualifying assets represent at least 70% of the Company s total assets. Qualifying assets represent approximately 87% of the Company s total assets as of December 31, 2018.

(6) Represents a PIK interest security. At the option of the issuer, interest can be paid in cash or cash and PIK interest. The percentage of PIK interest shown is the maximum PIK interest that can be elected by the issuer.

(7) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $666,666, with an interest rate of LIBOR plus 5.75% and a maturity of June 29, 2022. This investment is accruing an unused commitment fee of 0.50% per annum.

(8) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $2,000,000, with an interest rate of LIBOR plus 5.75% and a maturity of August 8, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(9) Investment has been on non-accrual since November 30, 2018.

(10) Excluded from the investment is an undrawn delayed draw term loan commitment in an amount not to exceed $3,669,681 with an interest rate of LIBOR plus 5.50% and a maturity of October 18, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(11) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $520,000, with an interest rate of LIBOR plus 8.00% and a maturity of September 30, 2018. This investment is not accruing an unused commitment fee.

(12) These loans have LIBOR floors that are lower than the applicable LIBOR rates; therefore, the floors are not in effect.

See accompanying notes to these consolidated financial statements.

Stellus Capital Investment Corporation Consolidated Schedule of Investments (continued) December 31, 2018

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2018

(13) These loans are last-out term loans with contractual rates higher than the applicable LIBOR rates; therefore, the floors are not in effect.

(14) Excluded from the investment is an undrawn delayed draw term loan commitment in an amount not to exceed $5,357,143, with an interest rate of LIBOR plus 6.75% and a maturity of August 30, 2024. This investment is accruing an unused commitment fee of 0.50% per annum.

(15) Investment has been on non-accrual since November 1, 2017.

(16) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $1,000,000, with an interest rate of LIBOR plus 7.75% and a maturity of February 5, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(17) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $1,500,000, with an interest rate of LIBOR plus 6.50% and a maturity of January 31, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(18) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $750,000, with an interest rate of LIBOR plus 7.50% and a maturity of April 13, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(19) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $1,222,494, with an interest rate of LIBOR plus 6.25% and a maturity of September 26, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(20) Investment has been on non-accrual since March 29, 2018.

(21) Investment has been on non-accrual since October 31, 2018.

(22) This loan is a unitranche investment.

(23) Excluded from the investment is an undrawn delayed draw term loan commitment in an amount not to exceed $1,662,592, with an interest rate of LIBOR plus 6.25% and a maturity of September 26, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

(24) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $2,000,000 with an interest rate of LIBOR plus 6.00% and a maturity of November 15, 2023. This investment is accruing an unused commitment fee of 0.50% per annum.

Abbreviation Legend

PIK	Payment-In-Kind
L	LIBOR
Euro	Euro Dollar

See accompanying notes to these consolidated financial statements.

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Consolidated Schedule of Investments
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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2017

(1) See Note 1 of the Notes to the Consolidated Financial Statements for a discussion of the methodologies used to value securities in the portfolio.

(2) Investments held by the SBIC Subsidiary, which include $5,258,500 of cash and $154,149,450 of investments (at cost) are excluded from the obligations to the lenders of the Credit Facility. The Company s obligations to the lenders of the Credit Facility, as defined in Note 9, are secured by a first priority security interest in all investments and cash and cash equivalents, except for investments held by the SBIC Subsidiary.

See accompanying notes to these consolidated financial statements.

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2017

(3) These loans have LIBOR or Euro Floors that are higher than the current applicable LIBOR or Euro rates; therefore, the floors are in effect.

(4) Security is non-income producing.

(5) The investment is not a qualifying asset under the Investment Company Act of 1940, as amended. The Company may not acquire any non-qualifying assets unless, at the time of the acquisition, qualifying assets represent at least 70% of the Company s total assets. Qualifying assets represent approximately 86% of the Company s total assets as of December 31, 2017.

(6) Represents a PIK security. At the option of the issuer, interest can be paid in cash or cash and PIK. The percentage of PIK shown is the maximum PIK that can be elected by the issuer.

(7) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $666,666, with an interest rate of LIBOR plus 6.25% and a maturity of June 29, 2022. This investment is accruing an unused commitment fee of 0.50% per annum.

(8) In the fourth quarter of 2016, Binder & Binder National Social Security Disability, emerged from Chapter 11 Bankruptcy in the U.S. Bankruptcy Court, Southern District of New York. The investment s fair value has been adjusted to reflect the court-approved unsecured claim distribution proceeds that have been awarded to the Company. As of this time, the Company does not expect to receive any additional repayment other than the court awarded amount.

(9) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed $1,750,000, with an interest rate of LIBOR plus 6.50% and a maturity of December 22, 2022. This investment is accruing an unused commitment fee of 0.50% per annum.

(10) Excluded from the investment is an undrawn commitment in an amount not to exceed $520,000, with an interest rate of LIBOR plus 8.00% and a maturity of September 30, 2018. This investment is accruing an unused commitment fee of 0.50% per annum.

(11) Interest compounds annually on this loan at a rate of 11%. The interest does not increase the principal balance.

(12) These loans have LIBOR floors that are lower than the applicable LIBOR rates; therefore, the floors are not in effect.

(13) These loans are last-out term loans with contractual rates higher than the applicable LIBOR rates; therefore, the floors are not in effect.

(14) Excluded from the investment is an undrawn commitment in an amount not to exceed $5,750,000, with an interest rate of LIBOR plus 7.62% and a maturity of July 26, 2022. This investment is accruing an unused commitment fee of 0.50% per annum.

(15) Investment has been on non-accrual since November 1, 2017.

(16) This loan is a last-out term loan with a set contractual rate that equals the current applicable LIBOR rate.

(17) This loan is a unitranche investment.

Abbreviation Legend

PIK	Payment-In-Kind
L	LIBOR
Euro	Euro Dollar

See accompanying notes to these consolidated financial statements.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Stellus Capital Investment Corporation (we , us , our and the Company) was formed as a Maryland corporation on M 18, 2012 (Inception) and is an externally managed, closed-end, non-diversified investment management company. The Company is applying the guidance of Accounting Standards Codification (ASC) Topic 946, Financial Services Investment Companies. The Company has elected to be regulated as a business development company under the Investment Company Act of 1940, as amended (the 1940 Act) and treated as a regulated investment company (RIC) under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code) for U.S. federal income tax purposes. The Company s investment activities are managed by our investment adviser Stellus Capital Management, LLC (Stellus Capital or the Advisor).

As of December 31, 2018 the Company has issued a total of 15,953,810 shares and raised $235,742,980 in gross proceeds since inception, incurring $7,566,535 in offering expenses and sales load fees for net proceeds from offerings of $228,176,445. The Company s shares are currently listed on the New York Stock Exchange under the symbol SCM . See Note 4 for further details.

The Company has established wholly owned subsidiaries: SCIC Consolidated Blocker 1, Inc., SCIC ICD Blocker 1, Inc., SCIC CC Blocker 1, Inc., SCIC ERC Blocker 1, Inc., SCIC SKP Blocker 1, Inc., SCIC APE Blocker 1, Inc., and SCIC Hollander Blocker 1, Inc., which are structured as Delaware entities, to hold equity or equity-like investments in portfolio companies organized as limited liability companies, or LLCs (or other forms of pass-through entities) (collectively, the Taxable Subsidiaries). The Taxable Subsidiaries are consolidated for U.S. generally accepted accounting principles (U.S GAAP) reporting purposes, and the portfolio investments held by them are included in the consolidated financial statements.

On June 14, 2013, we formed Stellus Capital SBIC LP (the SBIC subsidiary), a Delaware limited partnership, and its general partner, Stellus Capital SBIC GP, LLC., a Delaware limited liability company, as wholly owned subsidiaries of the Company. On June 20, 2014, the SBIC subsidiary received a license from the Small Business Administration (SBA) to operate as a Small Business Investment Company (SBIC) under Section 301(c) of the Small Business Investment Company Act of 1958. The SBIC subsidiary is consolidated for U.S. GAAP reporting purposes, and the portfolio investments held by it are included in the consolidated financial statements.

The SBIC license allows the SBIC subsidiary to obtain leverage by issuing SBA-guaranteed debentures, subject to the issuance of a capital commitment by the SBA and other customary procedures. SBA-guaranteed debentures are non-recourse, interest only debentures with interest payable semi-annually and have a ten year maturity. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. The interest rate of SBA-guaranteed debentures is fixed on a semi-annual basis at a market-driven spread over U.S. Treasury Notes with 10-year maturities. The SBA, as a creditor, will have a superior claim to the SBIC s assets over the Company s stockholders in the event the Company liquidates the SBIC subsidiary or the SBA exercises its remedies under the SBA-guaranteed debentures issued by the SBIC subsidiary upon an event of default. SBA regulations currently limit the amount that a single licensee may borrow to a maximum of $150,000,000 when it has at least $75,000,000 in regulatory capital, as such term is defined by the SBA, receives a capital commitment from the SBA and has been through an examination by the SBA subsequent to licensing. As of December 31, 2018 and 2017, the SBIC subsidiary had $75,000,000 and $67,500,000 of regulatory capital, respectively, as such term is defined by the

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

SBA. As of December 31, 2018 and 2017, the SBIC subsidiary had $150,000,000 and $90,000,000 of SBA-guaranteed debentures outstanding, respectively. See footnote (2) of the Consolidated Schedule of Investments for additional information regarding the treatment of SBIC investments with respect to the Credit Facility.

As a BDC, we are required to comply with certain regulatory requirements. Prior to June 28, 2018, we were only allowed to employ leverage to the extent that our asset coverage, as defined in the 1940 Act, was equal to at least 200% after giving effect to such leverage. On March 23, 2018, the Small Business Credit Availability Act (the SBCAA) was signed into law, which included various changes to regulations under the federal securities laws that impact BDCs. The SBCAA included changes to the 1940 Act to allow BDCs to decrease their asset coverage requirement to 150% from 200% under certain circumstances.

On April 4, 2018, the Company s board of directors (the Board), including a required majority (as such term is defined in Section 57(o) of the Investment Company Act of 1940, as amended (the 1940 Act)) of the Board, approved the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act. The Board also approved the submission of a proposal to approve the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act, which was approved by shareholders at the Company s 2018 annual meeting of stockholders. As a result, the asset coverage ratio test applicable to the Company was decreased from 200% to 150%, effective June 28, 2018. The amount of leverage that we employ at any time depends on our assessment of the market and other factors at the time of any proposed borrowing.

The Company s investment objective is to maximize the total return to its stockholders in the form of current income and capital appreciation through debt and related equity investments in middle-market companies. The Company seeks to achieve its investment objective by originating and investing primarily in private U.S. middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA (earnings before interest, taxes, depreciation and amortization)) through first lien (including unitranche), second lien, and unsecured debt financing, with corresponding equity co-investments. It sources investments primarily through the extensive network of relationships that the principals of Stellus Capital have developed with financial sponsor firms, financial institutions, middle-market companies, management teams and other professional intermediaries.

Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in conformity with U.S. GAAP and pursuant to the requirements for reporting on Form 10-K and Article 10 of regulation

S-X.

In the opinion of management, the consolidated financial results included herein contain all adjustments, consisting solely of normal recurring accruals, considered necessary for the fair presentation of financial statements for the periods included herein. Certain reclassifications have been made to certain prior period balances to conform with current presentation.

In accordance with Regulation S-X under the Securities Act of 1933 and Securities Exchange Act of 1934, as amended (the Exchange Act), the Company does not consolidate portfolio company investments.

The accounting records of the Company are maintained in U.S. dollars.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Portfolio Investment Classification

The Company classifies its portfolio investments in accordance with the requirements of the 1940 Act as follows; (a) Control Investments are defined as investments in which the Company owns more than 25% of the voting securities or has rights to maintain greater than 50% of the board representation, (b) Affiliate Investments are defined as investments in which the Company owns between 5% and 25% of the voting securities and does not have rights to maintain greater than 50% of the board representation, and (c) Non-controlled, non-affiliate investments are defined as investments that are neither Control Investments or Affiliate Investments.

Cash and Cash Equivalents

At December 31, 2018, cash balances totaling $336,243 exceeded FDIC insurance protection levels of $250,000 by $86,243, subjecting the Company to risk related to the uninsured balance. In addition, at December 31, 2018, the Company held $17,130,903 in cash equivalents that were back by the full faith credit of the U.S. government. All of the Company s cash and cash equivalents are held at large established high credit quality financial institutions and management believes that risk of loss associated with any uninsured balances is remote.

Cash consists of bank demand deposits. We deem certain U.S. Treasury Bills and other high-quality, short-term debt securities as cash equivalents. At the end of each fiscal quarter, we may take proactive steps to ensure we are in compliance with the RIC diversification requirements under Subchapter M of the Internal Revenue Code, which are dependent upon the composition of our total assets at quarter end. We may accomplish this in several ways, including purchasing U.S. Treasury Bills and closing out positions after quarter-end or temporarily drawing down on the Credit Facility (see footnote 9). At December 31, 2018 and December 31, 2017, we held no U.S. Treasury Bills.

Fair Value Measurements

We account for substantially all of our financial instruments at fair value in accordance with ASC Topic 820 Fair Value Measurements and Disclosures (ASC Topic 820). ASC Topic 820 defines fair value, establishes a framework used to measure fair value, and requires disclosures for fair value measurements, including the categorization of financial instruments into a three-level hierarchy based on the transparency of valuation inputs. ASC Topic 820 requires disclosure of the fair value of financial instruments for which it is practical to estimate such value. We believe that the carrying amounts of our financial instruments such as cash, receivables and payables approximate the fair value of these items due to the short maturity of these instruments. This is considered a Level 1 valuation technique. The carrying values of our Credit Facility and SBA-guaranteed debentures approximate fair value because the interest rates adjusts to the market interest rates (Level 3 input). The carrying value of our 2022 Notes (as defined in Note 11 below) is based on the closing price of the security (level 2 input). See Note 6 to the consolidated financial statements for further discussion regarding the fair value measurements and hierarchy.

Consolidation

As permitted under Regulation S-X under the Exchange Act and ASC Topic 946, we generally do not consolidate our investment in a portfolio company other than an investment company subsidiary. Accordingly, we consolidated the results of the SBIC subsidiary and the Taxable Subsidiaries. All intercompany balances have been eliminated upon consolidation.

STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of Estimates

The preparation of the statement of assets and liabilities in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Changes in the economic environment, financial markets and any other parameters used in determining these estimates could cause actual results to differ materially.

Deferred Financing Costs

Deferred financing costs, prepaid loan fees on SBA-guaranteed debentures and prepaid loan structure fees consist of fees and expenses paid in connection with the closing of our Credit Facility, notes and SBA-guaranteed debentures and are capitalized at the time of payment. These costs are amortized using the straight line method over the term of the respective instrument and presented as an offset to the corresponding debt on the statement of Assets and Liabilities.

Offering Costs

Deferred offering costs consist of fees and expenses incurred in connection with the offer and sale of the Company s securities, including legal, accounting, printing fees and other related expenses, as well as costs incurred in connection with the filing of a shelf registration statement. These costs are capitalized when incurred and recognized as a reduction of offering proceeds when the offering is consummated and shown on the Consolidated Statement of Changes in Net Assets and Liabilities as a reduction to Paid-in-Capital. During the year ended December 31, 2016, the Company determined that it was no longer likely to issue shares under its current shelf registration statement, as a result, the Company expensed $261,761 of previously capitalized deferred offering costs for the year ended December 31, 2016. During the year ended December 31, 2018, the Company incurred $18,673 of costs related to the preparation of a registration statement, which were capitalized and will be treated as discussed above in the event an offering is consummated.

Investments

As a BDC, the Company will generally invest in illiquid loans and securities including debt and equity securities of private middle-market companies. Under procedures established by our board of directors, the Company intends to value investments for which market quotations are readily available at such market quotations. The Company will obtain these market values from an independent pricing service or at the median between the bid and ask prices obtained from at least two brokers or dealers (if available, otherwise by a principal market maker or a primary market dealer). Debt and equity securities that are not publicly traded or whose market prices are not readily available will be valued at fair value as determined in good faith by our board of directors. Such determination of fair values may involve subjective judgments and estimates. The Company also engages independent valuation providers to review the valuation of each portfolio investment that does not have a readily available market quotation at least twice annually.

Investments purchased within approximately 90 days of the valuation date will be valued at cost plus accreted discount, or minus amortized premium, which approximates fair value. With respect to unquoted securities, our board of directors, will value each investment considering, among other measures, discounted cash flow models, comparisons of financial ratios of peer companies that are public and other factors. When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, the board of directors will use the pricing indicated by the external event to corroborate and/or assist us in our valuation. Because the

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Company expects that there will not be a readily available market for many of the investments in its portfolio, the Company expects to value most of its portfolio investments at fair value as determined in good faith by the board of directors using a documented valuation policy and a consistently applied valuation process. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material.

In following these approaches, the types of factors that will be taken into account in fair value pricing investments will include, as relevant, but not be limited to:

- available current market data, including relevant and applicable market trading and transaction comparables;
- applicable market yields and multiples;
- security covenants;
- call protection provisions;
- information rights;
- the nature and realizable value of any collateral;
- the portfolio company s ability to make payments, its earnings and discounted cash flows and the markets in which it does business;
- comparisons of financial ratios of peer companies that are public;
- comparable merger and acquisition transactions; and
- the principal market and enterprise values.

Revenue Recognition

We record interest income on an accrual basis to the extent such interest is deemed collectible. Payment-in-kind (PIK) interest, represents contractual interest accrued and added to the loan balance that generally becomes due at maturity. Loan origination fees, original issue discount and market discount or premium are capitalized, and we then accrete or amortize such amounts using the effective interest method as interest income. Upon the prepayment of a loan or debt security, any unamortized loan origination fee is recorded as interest income. We record prepayment premiums on loans and debt securities as other income. Dividend income, if any, will be recognized on the ex-dividend date.

A presentation of the interest income we have received from Portfolio Companies for the years ended December 31, 2018, 2017 and 2016 is as follows:

For the years ended

	December 31, 2018	December 31, 2017	December 31, 2016
Loan interest	$ 46,501,235	$ 34,890,298	$ 36,143,335
PIK income	1,869,905	499,595	243,766
Fee amortization income[(1)]	1,636,168	1,235,568	1,145,437
Fee income acceleration[(2)]	1,455,725	1,445,988	644,079
Total Interest Income	$ 51,463,033	$ 38,071,449	$ 38,176,617

(1) Includes amortizations of upfront fees on unfunded commitments.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

(2) Unamortized loan origination fees recognized upon realization.

To maintain our status as a RIC, substantially all of this income must be paid out to stockholders in the form of dividends, even if we have not collected any cash.

We will not accrue any form of interest on loans and debt securities if we have reason to doubt our ability to collect such interest. Management considers portfolio specific circumstances as well as other economic factors in determining collectibility. As of December 31, 2018, we had four loans on non-accrual status, which represented approximately 3.9% of our loan portfolio at cost and 2.8% at fair value. As of December 31, 2017, we had two loans on non-accrual status, which represented approximately 1.2% of our loan portfolio at cost and 0.3% at fair value. As of December 31, 2018 and December 31, 2017, $1,856,272 and $1,145,014 of income from investments on non-accrual has not been accrued. If a loan or debt security's status significantly improves regarding the debtor's ability to service the debt or other obligations, or if a loan or debt security is sold or written off, we remove it from non-accrual status.

Net Realized Gains or Losses and Net Change in Unrealized Appreciation or Depreciation

We measure realized gains or losses by the difference between the net proceeds from the repayment, sale or disposition and the amortized cost basis of the investment, without regard to unrealized appreciation or depreciation previously recognized. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment values during the reporting period, including any reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

Investment Transaction Costs

Costs that are material associated with an investment transaction, including legal expenses, are included in the cost basis of purchases and deducted from the proceeds of sales unless such costs are reimbursed by the borrower.

Receivables and Payables for Unsettled Securities Transaction

The Company records all investments on a trade date basis.

U.S. Federal Income Taxes

The Company has elected to be treated as a RIC under Subchapter M of the Code, and to operate in a manner so as to qualify for the tax treatment applicable to RICs. To qualify for tax treatment as a RIC, among other things, the Company is required to timely distribute to its stockholders at least 90% of investment company taxable income, as defined by the Code, for each year. So long as the Company maintains its status as a RIC, it generally will not pay corporate-level U.S. federal income taxes on any net ordinary income or capital gains that it distributes at least annually to its stockholders as dividends. Rather, any tax liability related to income earned by the Company represents obligations of the Company s investors and will not be reflected in the consolidated financial statements of the Company.

To avoid a 4% U.S federal excise tax on undistributed earnings, the Company is required to distribute each calendar year the sum of (i) 98% of its ordinary income for such calendar year (ii) 98.2% of its net capital gains for the one-year period ending December 31 (iii) any income recognized, but not distributed, in preceding years and on which the Company paid no federal income tax or the Excise Tax Avoidance Requirement. For this purpose, however, any net ordinary income or capital gain net income retained by us that is subject to corporate income tax for the tax

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

year ending in that calendar year will be considered to have been distributed by year end (or earlier if estimated taxes are paid). The Company, at its discretion, may choose not to distribute all of its taxable income for the calendar year and pay a non-deductible 4% excise tax on this income. If the Company chooses to do so, all other things being equal, this would increase expenses and reduce the amount available to be distributed to stockholders. To the extent that the Company determines that its estimated current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable income, the Company accrues excise taxes on estimated excess taxable income as taxable income is earned. Included in income tax expense for the year ended December 31, 2018 is the 2018 excise tax estimate of $316,092, less refunds related to the estimated excise tax paid for the years ended December 31, 2017 and 2016 totaling $63,144. Included in other general and administrative expense for the year ended December 31, 2017 is the 2017 tax estimate of $27,717 and an additional estimate of $14,985 related to the excise tax for the year ended December 31, 2016. Included in other general and administrative expenses for the year ended December 31, 2016 is the 2016 tax estimate of $22,663.

The Company evaluates tax positions taken or expected to be taken in the course of preparing its tax returns to determine whether the tax positions are more-likely-than-not of being sustained by the applicable tax authority. Tax positions deemed to meet a more-likely-than-not threshold would be recorded as a tax provision or expense in the applicable period. As of December 31, 2018 and December 31, 2017, the Company had not recorded a liability for any uncertain tax positions. Management s evaluation of uncertain tax positions may be subject to review and adjustment at a later date based upon factors including, but not limited to, an on-going analysis of tax laws, regulations and interpretations thereof. The Company s policy is to include interest and penalties related to income taxes, if applicable, in income tax expense. Any such expenses for the year ended December 31, 2018 were de minimis.

On December 22, 2017, the Tax Cuts and Jobs Act legislation was signed into law. The Tax Cuts and Jobs Act includes significant changes to the U.S. corporate tax system, including a reduction in the U.S. corporate income tax rate from 35% to 21%. ASC 740, Income Taxes, requires the effect of changes in tax rates and laws on deferred tax balances to be recognized in the period in which the legislation is enacted. As such, we have accounted for the tax effects as a result of the Tax Cuts and Jobs Act beginning with the period ending December 31, 2017.

The Taxable Subsidiaries are direct wholly owned subsidiaries of the Company that have elected to be taxable entities. The Taxable Subsidiaries permit the Company to hold equity investments in portfolio companies which are pass through entities for tax purposes and continue to comply with the source-of-income requirements contained in RIC tax provisions of the Code. The Taxable Subsidiaries are not consolidated with the Company for income tax purposes and may generate income tax expense, benefit, and the related tax assets and liabilities, as a result of their ownership of certain portfolio investments. The income tax expense, or benefit, if any, and related tax assets and liabilities are reflected in the Company s consolidated financial statements.

The Taxable Subsidiaries use the liability method in accounting for income taxes. Deferred tax assets and liabilities are recorded for temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, using statutory tax rates in effect for the year in which the temporary differences are expected to reverse. A valuation allowance is provided against deferred tax assets when it is more likely than not that some portion or all of the deferred tax asset will not be realized.

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NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses. Taxable income generally excludes net unrealized appreciation or depreciation, as investment gains or losses are not included in taxable income until they are realized.

For the years ended December 31, 2018, 2017 and 2016, the Company recorded deferred income tax benefit (expense) of ($67,953), $8,593 and $373,131, respectively, related to the Taxable Subsidiaries. In addition, as of December 31, 2018 and December 31, 2017, the Company had a deferred tax liability of $67,953 and $0, respectively. See Note 13, Income Taxes, for a schedule of the deferred tax asset and valuation allowance reducing the deferred tax asset and the deferred tax liability.

Earnings per Share

Basic per share calculations are computed utilizing the weighted average number of shares of common stock outstanding for the period. The Company has no common stock equivalents. As a result, there is no difference between diluted earnings per share and basic per share amounts.

Paid In Capital

The Company records the proceeds from the sale of its common stock on a net basis to (i) capital stock and (ii) paid in capital in excess of par value, excluding all commissions and marketing support fees.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). The guidance in this ASU supersedes the revenue recognition requirements in Revenue Recognition (Topic 605). Under the new guidance, an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The update is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The guidance was effective for the Company as of January 1, 2018. Note, the guidance exempts interest income from the above guidance, indicating recognition will remain the same. The Company will continue to recognize origination fees over the life of the loan. Repayment penalty fees will be recognized immediately if a repayment is made and miscellaneous fees such as administration fees will be recognized on the contract renewal date or other discrete point in time per the credit agreement. Substantially all of the Company s income is not within the scope of ASU 2014-09. For those income items that are within the scope (primarily fee income), the Company has similar performance obligations as compared with deliverables and separate units of account previously identified. As a result, the Company s timing of its income recognition remains the same and the adoption of the standard was not material.

In November 2015, the FASB issued ASU 2015-17 Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes. ASU 2015-17 requires entities to present deferred tax assets and deferred tax liabilities as noncurrent in a classified balance sheet. It simplifies the current guidance, which requires entities to separately present deferred tax assets and liabilities as current or noncurrent in a classified balance sheet. The guidance was effective for the Company as of January 1, 2017 and there has been no material impact on its consolidated financial statement.

In August 2016, the FASB issued ASU 2016-15 Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. ASU 2016-15 is intended to reduce

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 1 NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (continued)

diversity in practice in how certain transactions are classified in the statement of cash flows. The new guidance addresses the classification of various transactions including debt prepayment or debt extinguishment costs, settlement of zero-coupon debt instruments, contingent consideration payments made after a business combination, distributions received from equity method investments, beneficial interests in securitization transactions, and others. The update is effective for annual periods beginning after December 31, 2017, and interim periods within those annual periods. Early adoption is permitted, including adoption in an interim period. The Company early adopted the guidance as of January 1, 2017 and there is no material impact of this new standard on our consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-13 Changes to the Disclosure Requirements for Fair Value Measurement. ASU 2018-13 is part of the disclosure framework project, which primarily focuses on improving the effectiveness of disclosures in the notes to financial statements. The amendments in this update remove, modify, and add certain disclosure requirements on fair value measurements in Topic 820, Fair Value Measurement. The update is effective for annual periods beginning after December 31, 2019, and interim periods within those annual periods. The Company is currently assessing the impact of the guidance, however it does not expect any impact of this new guidance on its consolidated financial statements to be material.

From time to time, new accounting pronouncements are issued by the Financial Accounting Standards Board (FASB) or other standards setting bodies that are adopted by the Company as of the specified effective date. We believe the impact of the recently issued standards and any that are not yet effective will not have a material impact on our consolidated financial statements upon adoption.

NOTE 2 RELATED PARTY ARRANGEMENTS

Investment Advisory Agreement

The Company has entered into an investment advisory agreement with Stellus Capital pursuant to which Stellus Capital serves as its investment adviser. Pursuant to this agreement, the Company has agreed to pay to Stellus Capital an annual base management fee of 1.75% of gross assets, including assets purchased with borrowed funds or other forms of leverage and excluding cash and cash equivalents, and an incentive fee.

For the years ended December 31, 2018, 2017 and 2016, the Company recorded an expense for base management fees of $8,154,842, $6,255,911, and $6,281,863 respectively. As of December 31, 2018 and December 31, 2017, respectively, $2,183,975 and $1,621,592 was payable to Stellus Capital, respectively.

The incentive fee has two components, investment income and capital gains, as follows:

Investment Income Incentive Fee

The income component (Income Incentive Fee) is calculated, and payable to the Advisor, quarterly in arrears based on the Company s pre-incentive fee net investment income for the immediately preceding calendar quarter, subject to a cumulative total return requirement and to deferral of non-cash amounts. The pre-incentive fee net investment income, which is expressed as a rate of return on the value of the Company s net assets attributable to the Company s common stock, for the immediately preceding calendar quarter, has a 2.0% hurdle rate (also referred to as the Hurdle). Pre-incentive fee net investment income means interest income, dividend income and any other income accrued during the calendar quarter, minus the Company s operating

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 2 RELATED PARTY ARRANGEMENTS (continued)

expenses for the quarter excluding the incentive fee. Pre-incentive fee net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount, debt instruments with PIK interest and zero coupon securities), accrued income that the Company has not yet received in cash. The Advisor receives no incentive fee for any calendar quarter in which the Company s pre-incentive fee net investment income does not exceed the Hurdle. Subject to the cumulative total return requirement described below, the Advisor receives 100% of the Company s pre-incentive fee net investment income for any calendar quarter with respect to that portion of the pre-incentive net investment income for such quarter, if any, that exceeds the Hurdle but is less than 2.5% of net assets (also referred to as the Catch-up) and 20.0% of the Company s pre-incentive fee net investment income for such calendar quarter, if any, greater than 2.5% of net assets.

The foregoing incentive fee is subject to a total return requirement, which provides that no incentive fee in respect of the Company s pre-incentive fee net investment income is payable except to the extent 20.0% of the cumulative net increase in net assets resulting from operations over the then current and 11 preceding calendar quarters exceeds the cumulative incentive fees accrued and/or paid for the 11 preceding quarters. In other words, any Income Incentive Fee that is payable in a calendar quarter is limited to the lesser of (i) 20% of the amount by which the Company s pre-incentive fee net investment income for such calendar quarter exceeds the 2.0% hurdle, subject to the Catch-up, and (ii) (x) 20% of the cumulative net increase in net assets resulting from operations for the then current and 11 preceding quarters minus (y) the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. For the foregoing purpose, the cumulative net increase in net assets resulting from operations is the amount, if positive, of the sum of pre-incentive fee net investment income, realized gains and losses and unrealized appreciation and depreciation of the Company for the then current and 11 preceding calendar quarters. In addition, the Advisor is not paid the portion of such incentive fee that is attributable to deferred interest until the Company actually receives such interest in cash.

For the years ended December 31, 2018, 2017 and 2016, the Company incurred $5,529,376, $2,911,392 and $4,275,436, respectively, of Investment Income Incentive Fees. As of December 31, 2018 and 2017, $1,936,538 and $371,647, respectively, of such incentive fees were payable to the Advisor, of which $1,675,804 and $175,738, respectively, were currently payable (as explained below). As of December 31, 2018 and December 31, 2017, $260,734 and $195,909, respectively, of incentive fees incurred but not paid by the Company were generated from deferred interest (i.e. PIK, certain discount accretion and deferred interest) and are not payable until such amounts are received by the Company in cash.

Capital Gains Incentive Fee

The Company also pays the Advisor an incentive fee based on capital gains (the Capital Gains Incentive Fee). The Capital Gains Incentive Fee is determined and payable in arrears as of the end of each calendar year (or upon termination of the investment management agreement, as of the termination date). The Capital Gains Incentive Fee is equal to 20.0% of the Company s cumulative aggregate realized capital gains from Inception through the end of that calendar year, computed net of the cumulative aggregate realized capital losses and cumulative aggregate unrealized capital depreciation through the end of such year. The aggregate amount of any previously paid Capital Gains Incentive Fees is subtracted from such Capital Gains Incentive Fee calculated.

U.S. GAAP requires that the incentive fee accrual considers the cumulative aggregate realized gains and losses and unrealized capital appreciation and depreciation of investments or other financial instruments in the calculation, as an incentive fee would be payable if such unrealized

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 2 RELATED PARTY ARRANGEMENTS (continued)

capital appreciation or depreciation were realized, even though such unrealized capital appreciation is not permitted to be considered in calculating the fee actually payable under the investment advisory agreement. There can be no assurance that unrealized appreciation or depreciation will be realized in the future. Accordingly, such fees, as calculated and accrued, may not necessarily be payable under the investment advisory agreement, and may never be paid based upon the computation of incentive fees in subsequent periods. For the years ended December 31, 2018, and 2017, the Company incurred $81,038 and $0, respectively. As of December 31, 2018 and December 31, 2017, $81,038 and $0, respectively of Capital Gains Incentive Fees were payable to the Advisor.

The following tables summarize the components of the incentive fees discussed above:

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Investment Income Incentive Fee Incurred	$ 5,529,376	$ 2,911,392	$ 4,275,436
Capital Gains Incentive Fee Incurred	81,038		$
Incentive Fee Expense	$ 5,610,414	$ 2,911,392	$ 4,275,436

	December 31, 2018	December 31, 2017
Investment Income Incentive Fee Currently Payable	$ 1,675,804	$ 175,738
Investment Income Incentive Fee Deferred	260,734	195,909
Capital Gains Incentive Fee Payable	81,038	
Incentive Fee Payable	$ 2,017,576	$ 371,647

Director Fees

For the years ended December 31, 2018, 2017 and 2016, the Company recorded an expense relating to director fees of $317,000, $331,000, and $324,000, respectively. As of December 31, 2018 and 2017, the Company owed its independent directors no unpaid director fees.

Co-Investments

On October 23, 2013, the Company received an exemptive order (the Prior Order) from the SEC to co-invest with private funds managed by Stellus Capital Management where doing so is consistent with the Company s investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). On December 18, 2018, the Company received a new exemptive order (the Order) that supersedes the Prior Order and permits the Company greater flexibility to enter into co-investment transactions. The Order expands on the Prior Order and allows the Company to co-invest with additional types of private funds, other BDCs, and registered investment companies managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management, subject to the conditions included therein. Pursuant to the Order, a required majority (as defined in Section 57(o) of the 1940 Act) of the Company s independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to the Company and its stockholders and do not involve overreaching of the Company or its stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of the Company s stockholders and is consistent with the Company s investment objectives and strategies. The Company co-invests, subject to the conditions included in the Order, with private credit funds managed by Stellus Capital Management that have an investment strategy that is

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NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 2 RELATED PARTY ARRANGEMENTS (continued)

similar to or identical to the Company s investment strategy, and the Company may co-invest with other BDCs and registered investment companies managed by Stellus Capital Management or an adviser that is controlled, controlling, or under common control with Stellus Capital Management in the future. The Company believes that such co-investments may afford additional investment opportunities and an ability to achieve greater diversification.

Administrative Agent

The Company serves as the administrative agent on certain investment transactions, including co-investments with its affiliates under the exemptive relief order. As of December 31, 2018 and December 31, 2017, there was no cash due to other investment funds related to interest paid by a borrower to the Company as administrative agent. Any such amount would be included in Other Accrued Expenses and Liabilities on the Consolidated Statement of Assets and Liabilities.

License Agreement

The Company has entered into a license agreement with Stellus Capital under which Stellus Capital has agreed to grant the Company a non-exclusive, royalty-free license to use the name Stellus Capital. Under this agreement, the Company has a right to use the Stellus Capital name for so long as Stellus Capital or one of its affiliates remains its investment adviser. Other than with respect to this limited license, the Company has no legal right to the Stellus Capital name.

Administration Agreement

The Company entered into an administration agreement with Stellus Capital pursuant to which Stellus Capital will furnish the Company with office facilities and equipment and will provide the Company with the clerical, bookkeeping, recordkeeping and other administrative services necessary to conduct day-to-day operations. Under this administration agreement, Stellus Capital will perform, or oversee the performance of, its required administrative services, which includes, among other things, being responsible for the financial records which it is required to maintain and preparing reports to its stockholders and reports filed with the SEC.

For the years ended December 31, 2018, 2017 and 2016, the Company recorded expenses of $1,195,174, $1,117,011, and $922,531, respectively, related to the administration agreement. As of December 31, 2018 and December 31, 2017, $323,188 and $279,141, respectively, remained payable to Stellus Capital relating to the administration agreement.

Indemnification

The investment advisory agreement provides that, absent willful misfeasance, bad faith or gross negligence in the performance of its duties or by reason of the reckless disregard of its duties and obligations under the investment advisory agreement, Stellus Capital and its officers, managers, partners, agents, employees, controlling persons and members, and any other person or entity affiliated with it, are entitled to indemnification from the Company for any damages, liabilities, costs and expenses (including reasonable attorneys fees and amounts reasonably paid in settlement) arising from the rendering of Stellus Capital s services under the investment advisory agreement or otherwise as our investment adviser.

NOTE 3 DISTRIBUTIONS

Distributions are generally declared by the Company s board of directors each calendar quarter, paid monthly and recognized as distribution liabilities on the ex-dividend date. The Company intends to distribute net realized gains (i.e., net capital gains in excess of net capital

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NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 3 DISTRIBUTIONS (continued)

losses), if any, at least annually. The stockholder distributions, if any, will be determined by the board of directors. Any distribution to stockholders will be declared out of assets legally available for distribution.

The following table reflects the Company s distributions declared and paid or to be paid on its common stock since Inception:

Date Declared	Record Date	Payment Date	Per Share
Fiscal 2012			
December 7, 2012	December 21, 2012	December 27, 2012	$ 0.1812
Fiscal 2013			
March 7, 2013	March 21, 2013	March 28, 2013	$ 0.3400
June 7, 2013	June 21, 2013	June 28, 2013	$ 0.3400
August 21, 2013	September 5, 2013	September 27, 2013	$ 0.3400
November 22, 2013	December 9, 2013	December 23, 2013	$ 0.3400
Fiscal 2014			
December 27, 2013	January 15, 2014	January 24, 2014	$ 0.0650
January 20, 2014	January 31, 2014	February 14, 2014	$ 0.1133
January 20, 2014	February 28, 2014	March 14, 2014	$ 0.1133
January 20, 2014	March 31, 2014	April 15, 2014	$ 0.1133
April 17, 2014	April 30, 2014	May 15, 2014	$ 0.1133
April 17, 2014	May 30, 2014	June 16, 2014	$ 0.1133
April 17, 2014	June 30, 2014	July 15, 2014	$ 0.1133
July 7, 2014	July 31, 2014	August 15, 2014	$ 0.1133
July 7, 2014	August 29, 2014	September 15, 2014	$ 0.1133
July 7, 2014	September 30, 2014	October 15, 2014	$ 0.1133
October 15, 2014	October 31, 2014	November 14, 2014	$ 0.1133
October 15, 2014	November 28, 2014	December 15, 2014	$ 0.1133
October 15, 2014	December 31, 2014	January 15, 2015	$ 0.1133
Fiscal 2015			
January 22, 2015	February 2, 2015	February 13, 2015	$ 0.1133
January 22, 2015	February 27, 2015	March 13, 2015	$ 0.1133
January 22, 2015	March 31, 2015	April 15, 2015	$ 0.1133
April 15, 2015	April 30, 2015	May 15, 2015	$ 0.1133
April 15, 2015	May 29, 2015	June 15, 2015	$ 0.1133
April 15, 2015	June 30, 2015	July 15, 2015	$ 0.1133
July 8, 2015	July 31, 2015	August 14, 2015	$ 0.1133

July 8, 2015	August 31, 2015	September 15, 2015	$ 0.1133
July 8, 2015	September 20, 2015	October 15, 2015	$ 0.1133
October 14, 2015	October 30, 2015	November 13, 2015	$ 0.1133
October 14, 2015	November 30, 2015	December 15, 2015	$ 0.1133
October 14, 2015	December 31, 2015	January 15, 2016	$ 0.1133

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NOTE 3 DISTRIBUTIONS (continued)

Date Declared	Record Date	Payment Date	Per Share
Fiscal 2016			
January 13, 2016	January 29, 2016	February 15, 2016	$ 0.1133
January 13, 2016	February 29, 2016	March 15, 2016	$ 0.1133
January 13, 2016	March 31, 2016	April 15, 2016	$ 0.1133
April 15, 2016	April 29, 2016	May 13, 2016	$ 0.1133
April 15, 2016	May 31, 2016	June 15, 2016	$ 0.1133
April 15, 2016	June 30, 2016	July 15, 2016	$ 0.1133
July 7, 2016	July 29, 2016	August 15, 2016	$ 0.1133
July 7, 2016	August 31, 2016	September 15, 2016	$ 0.1133
July 7, 2016	September 30, 2016	October 14, 2016	$ 0.1133
October 7, 2016	October 31, 2016	November 15, 2016	$ 0.1133
October 7, 2016	November 30, 2016	December 15, 2016	$ 0.1133
October 7, 2016	December 30, 2016	January 13, 2017	$ 0.1133
Fiscal 2017			
January 13, 2017	January 31, 2017	February 15, 2017	$ 0.1133
January 13, 2017	February 28, 2017	March 15, 2017	$ 0.1133
January 13, 2017	March 31, 2017	April 14, 2017	$ 0.1133
April 14, 2017	April 28, 2017	May 15, 2017	$ 0.1133
April 14, 2017	May 31, 2017	June 15, 2017	$ 0.1133
April 14, 2017	June 30, 2017	July 14, 2017	$ 0.1133
July 7, 2017	July 31, 2017	August 15, 2017	$ 0.1133
July 7, 2017	August 31, 2017	September 15, 2017	$ 0.1133
July 7, 2017	September 29, 2017	October 13, 2017	$ 0.1133
October 12, 2017	October 31, 2017	November 15, 2017	$ 0.1133
October 12, 2017	November 30, 2017	December 15, 2017	$ 0.1133
October 12, 2017	December 29, 2017	January 12, 2018	$ 0.1133
Fiscal 2018			
January 11, 2018	January 31, 2018	February 15, 2018	$ 0.1133
January 11, 2018	February 28, 2018	March 15, 2018	$ 0.1133
January 11, 2018	March 29, 2018	April 13, 2018	$ 0.1133
April 16, 2018	April 30, 2018	May 15, 2018	$ 0.1133
April 16, 2018	May 31, 2018	June 15, 2018	$ 0.1133
April 16, 2018	June 29, 2018	July 13, 2018	$ 0.1133
July 12, 2018	July 31, 2018	August 15, 2018	$ 0.1133
July 12, 2018	August 31, 2018	September 14, 2018	$ 0.1133

July 12, 2018	September 28, 2018	October 15, 2018	$ 0.1133
October 16, 2018	October 31, 2018	November 15, 2018	$ 0.1133
October 16, 2018	November 29, 2018	December 14, 2018	$ 0.1133
October 16, 2018	December 31, 2018	January 15, 2019	$ 0.1133
Total			$ 8.4042

The Company has adopted an opt out dividend reinvestment plan (DRIP) pursuant to which a stockholder whose shares are held in his own name will receive distributions in shares of the Company s common stock under the Company s DRIP unless it elects to receive distributions in cash. Shareholders whose shares are held in the name of a broker or the nominee of a broker may

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 3 DISTRIBUTIONS (continued)

have distributions reinvested only if such service is provided by the broker or the nominee, or if the broker or the nominee permits participation in our DRIP. Shareholders whose shares are held in the name of a broker or other nominee should contact the broker or nominee for details. Although distributions paid in the form of additional shares of the Company s common stock will generally be subject to U.S. federal, state and local taxes in the same manner as cash distributions, investors participating in the Company s DRIP will not receive any corresponding cash distributions with which to pay any such applicable taxes. Any distributions reinvested through the issuance of shares through the Company s DRIP will increase the Company s gross assets on which the base management fee and the incentive fee are determined and paid to Stellus Capital. The Company issued 7,931 shares through the DRIP during the year ended December 31, 2018. No new shares were issued in connection with the DRIP during the year ended December 31, 2017.

NOTE 4 EQUITY OFFERINGS AND RELATED EXPENSES

The table below illustrates the number of common stock shares the Company issued since inception through various equity offerings and pursuant to the Company s DRIP.

Issuance of Common Stock	Number of Shares	Gross[(1)(2)] Proceeds	Underwriting fees	Offering Expenses	Net Proceeds	Offering Price
Year ended December 31, 2012	12,035,023	$180,522,093	$4,959,720	$835,500	$174,726,873	$14.90
Year ended December 31, 2013	63,998	899,964			899,964	$14.06
Year ended December 31, 2014	380,936	5,485,780	75,510	29,904	5,380,366	$14.47
Year ended December 31, 2015						
Year ended December 31, 2016						
Year ended December 31, 2017	3,465,922	48,741,406	1,358,880	307,021	47,075,505	$14.06
Year ended December 31, 2018	7,931	93,737			94,018	$11.85
Total	15,953,810	$235,742,980	$6,394,110	$1,172,425	$228,176,445	

(1) Net of partial share redemptions. Such share redemptions reduced gross proceeds by $1,051, $142, $31 and $29 in

2018, 2017, 2016 and 2015, respectively.

(2) Includes common shares issued under the DRIP of $94,788 during the year ended December 31, 2018, $0 for the years ended 2017, 2016 and 2015, and $398,505, $930,385, $113,000 for the years ended 2014, 2013, and 2012, respectively.

The Company issued 7,931 shares through the DRIP during the year ended December 31, 2018. No new shares were issued in connection with the DRIP during the year ended December 31, 2017.

The Company issued 3,162,500 shares in a secondary offering and 303,422 shares in connection with the ATM program during the year ended December 31, 2017. Gross proceeds resulting from the secondary offering totaled $44,591,250 and underwriting and other expenses totaled $1,530,632. The per share offering price for the secondary offering was $14.10. Gross proceeds resulting from the ATM Program in 2017 totaled $4,150,299 and underwriting and other expenses totaled $135,270. The average per share offering price of shares issued in the ATM Program during 2017 was $13.68.

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NOTE 5 NET INCREASE IN NET ASSETS PER COMMON SHARE

The following information sets forth the computation of net increase in net assets resulting from operations per common share for the years ended December 31, 2018, 2017 and 2016.

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Net increase in net assets resulting from operations	$ 26,194,578	$ 22,613,257	$ 23,199,062
Weighted average common shares	15,953,571	14,870,981	12,479,959
Basic and diluted earnings per common share	$ 1.64	$ 1.52	$ 1.86

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE

In accordance with the authoritative guidance on fair value measurements and disclosures under U.S. GAAP, the Company discloses the fair value of its investments in a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The guidance establishes three levels of the fair value hierarchy as follows:

Level 1	Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
Level 2	Quoted prices in markets that are not considered to be active or financial instruments for which significant inputs are observable, either directly or indirectly;
Level 3	Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

The level of an asset or liability within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. However, the determination of what constitutes observable requires significant judgment by management.

The Company considers whether the volume and level of activity for the asset or liability have significantly decreased and identifies transactions that are not orderly in determining fair value. Accordingly, if the Company determines that either the volume and/or level of activity for an asset or liability has significantly decreased (from normal conditions for that asset or liability) or price quotations or observable inputs are not associated with orderly transactions, increased analysis and management judgment will be required to estimate fair value. Valuation techniques such as an income approach might be appropriate to supplement or replace a market approach in those circumstances.

STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

At December 31, 2018, the Company had investments in 57 portfolio companies. The total cost and fair value of the investments were $502,743,649 and $504,483,668 respectively. The composition of our investments as of December 31, 2018 is as follows:

	Cost	Fair Value
Senior Secured First Lien[(1)]	$ 297,965,589	$ 292,004,982
Senior Secured Second Lien	155,382,612	149,661,220
Unsecured Debt	25,436,237	23,697,466
Equity	23,959,211	39,120,000
Total Investments	$ 502,743,649	$ 504,483,668

(1) Includes unitranche investments, which account for 20.6% of our portfolio at fair value. Unitranche structures may combine characteristics of first lien senior secured as well as second lien and/or subordinated loans and our unitranche loans will expose us to the risks associated with the second lien and subordinated loans to the extent we invest in the last-out tranche.

At December 31, 2017, the Company had investments in 48 portfolio companies. The total cost and fair value of the investments were $368,453,206 and $371,839,772 respectively. The composition of our investments as of December 31, 2017 was as follows:

	Cost	Fair Value
Senior Secured First Lien[(1)]	$ 140,915,106	$ 141,006,923
Senior Secured Second Lien	181,164,730	178,432,850
Unsecured Debt	27,903,141	27,430,000
Equity	18,470,229	24,969,999
Total Investments	$ 368,453,206	$ 371,839,772

(1) Includes unitranche investments, which account for 13.2% of our portfolio at fair value. Unitranche structures may combine characteristics of first lien senior secured as well as second lien and/or subordinated loans and our unitranche loans will expose us to the risks associated with the second lien and subordinated loans to the extent we invest in the last-out tranche.

The Company s investment portfolio may contain loans that are in the form of lines of credit or revolving credit facilities, which require the Company to provide funding when requested by portfolio companies in accordance with the terms of the underlying loan agreements. As of December 31, 2018 and December 31, 2017, the Company had eleven and four such investments with aggregate unfunded commitments of $21,213,962 and $8,686,667, respectively. The Company maintains sufficient liquidity to fund such unfunded loan commitments should the need arise.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The fair values of our investments disaggregated into the three levels of the fair value hierarchy based upon the lowest level of significant input used in the valuation as of December 31, 2018 are as follows:

		Quoted Prices in Active Markets for Identical Securities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Senior Secured	First Lien	$	$	$ 292,004,982	$ 292,004,982
Senior Secured	Second Lien			149,661,220	149,661,220
Unsecured Debt				23,697,466	23,697,466
Equity				39,120,000	39,120,000
Total Investments		$	$	$ 504,483,668	$ 504,483,668

The fair values of our investments disaggregated into the three levels of the fair value hierarchy based upon the lowest level of significant input used in the valuation as of December 31, 2017 are as follows:

		Quoted Prices in Active Markets for Identical Securities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Senior Secured	First Lien	$	$	$ 141,006,923	$ 141,006,923
Senior Secured	Second Lien			178,432,850	178,432,850
Unsecured Debt				27,430,000	27,430,000
Equity				24,969,999	24,969,999
Total Investments		$	$	$ 371,839,772	$ 371,839,772

The aggregate values of Level 3 portfolio investments changed during the year ended December 31, 2018 are as follows:

Senior Secured	Senior Secured	Unsecured	Equity	Total

	Loans-First Lien	Loans-Second Lien	Debt		
Fair value at beginning of period	$141,006,923	$178,432,850	$27,430,000	$24,969,999	$371,839,772
Purchases of investments	224,555,549	38,515,000	251,180	9,605,730	272,927,459
Payment-in-kind interest	106,314	1,696,547	67,044		1,869,905
Sales and Redemptions	(68,382,321)	(66,658,090)	(2,903,096)	(9,657,263)	(147,600,770)
Realized Gains				5,540,518	5,540,518
Change in unrealized appreciation (depreciation) included in earnings	(6,052,424)	(2,989,511)	(1,265,630)	8,661,016	(1,646,549)
Amortization of premium and accretion of discount, net	770,941	664,424	117,968		1,553,333
Fair value at end of period	$292,004,982	$149,661,220	$23,697,466	$39,120,000	$504,483,668
Change in unrealized depreciation on Level 3 investments still held as of December 31, 2018	$(5,820,453)	$(3,157,990)	$(1,285,630)	$10,831,127	$567,054

There were no Level 3 transfers during the twelve months ended December 31, 2018.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The aggregate values of Level 3 portfolio investments changed during the year ended December 31, 2017 are as follows:

	Senior Secured Loans-First Lien	Senior Secured Loans-Second Lien	Unsecured Debt	Equity	Total
Fair value at beginning of year	$113,482,205	$144,521,388	$70,725,412	$18,931,886	$347,660,891
Purchases of investments	85,892,733	73,388,500	6,203,400	6,686,613	172,171,246
Payment-in-kind interest	113,723	319,629	66,244		499,596
Sales and redemptions	(57,242,106)	(47,725,650)	(49,578,812)	(9,369,308)	(163,915,876)
Transfer from term loan to equity	(864,101)			864,101	
Net realized gain (loss)	(626,949)			5,367,925	4,740,976
Change in unrealized appreciation (depreciation)	(126,190)	(2,146,961)	(278,564)	2,488,782	(62,933)
Amortization of premium and accretion of discount, net	377,608	525,944	292,320		1,195,872
Transfer from Level 2		9,550,000			9,550,000
Fair value at end of year	$141,006,923	$178,432,850	$27,430,000	$24,969,999	$371,839,772
Change in unrealized depreciation on Level 3 investments still held as of December 31, 2017	$(498,183)	$(1,679,419)	$(278,567)	$3,465,063	$1,008,894

During the year ended December 31, 2017, there was one transfer from a Level 2 to a Level 3 because the observable inputs were not available. Transfers are reflected at the value of the securities at the beginning of the period.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The following is a summary of geographical concentration of our investment portfolio as of December 31, 2018:

	Cost	Fair Value	% of Total Investments at fair value
Texas	$ 100,229,354	$ 97,474,226	19.32 %
California	86,550,134	85,880,918	17.03 %
New Jersey	43,513,698	41,473,072	8.22 %
Ohio	36,209,514	36,273,224	7.19 %
Illinois	19,941,053	29,880,018	5.92 %
Canada	27,902,537	27,935,931	5.54 %
Arizona	21,682,522	21,603,741	4.28 %
South Carolina	20,871,587	20,385,325	4.04 %
New York	20,446,690	20,287,086	4.02 %
Tennessee	20,117,218	19,381,134	3.84 %
Arkansas	17,696,537	18,013,941	3.57 %
Pennsylvania	17,732,831	17,824,372	3.53 %
Maryland	17,237,500	17,237,500	3.42 %
Wisconsin	11,437,711	10,869,000	2.15 %
Colorado	10,777,822	10,777,822	2.14 %
Georgia	5,988,728	9,820,000	1.95 %
Indiana	7,363,628	7,087,500	1.40 %
Puerto Rico	8,797,954	5,029,913	1.00 %
North Carolina	4,946,554	4,425,000	0.88 %
Massachusetts	1,317,406	1,670,000	0.33 %
Missouri	139,656	670,000	0.13 %
Virginia	50,001	280,000	0.06 %
Florida	242,304	110,000	0.02 %
Utah	1,550,710	93,945	0.02 %
	$ 502,743,649	$ 504,483,668	100.00 %

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The following is a summary of geographical concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Texas	$ 109,043,496	$ 108,445,000	29.16	%
New Jersey	34,531,876	34,595,527	9.30	%
New York	28,939,268	29,365,000	7.90	%
Canada	26,315,677	26,440,000	7.11	%
California	25,519,753	25,930,000	6.97	%
Illinois	24,250,169	25,700,000	6.91	%
Massachusetts	22,534,191	22,247,850	5.98	%
Arizona	13,565,958	13,840,000	3.72	%
North Carolina	12,248,770	12,499,167	3.36	%
Ohio	10,112,627	9,990,000	2.69	%
Tennessee	9,848,614	9,950,000	2.68	%
Missouri	9,152,087	9,530,000	2.56	%
Georgia	5,929,223	8,329,998	2.24	%
Pennsylvania	7,848,470	8,058,746	2.17	%
Arkansas	7,397,881	7,618,484	2.05	%
Minnesota	5,421,770	5,420,000	1.46	%
Puerto Rico	8,827,864	5,080,000	1.37	%
Washington	4,172,743	4,520,000	1.22	%
Alabama	1,206,682	2,880,000	0.77	%
Utah	1,293,782	880,000	0.24	%
Florida	242,304	420,000	0.11	%
Virginia	50,001	100,000	0.03	%
	$ 368,453,206	$ 371,839,772	100.00	%

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The following is a summary of industry concentration of our investment portfolio as of December 31, 2018:

	Cost	Fair Value	% of Total Investments at fair value	
Services: Business	$ 60,784,467	$ 63,810,643	12.65	%
Healthcare & Pharmaceuticals	58,682,811	54,785,327	10.86	%
Consumer Goods: Durable	44,218,515	44,049,052	8.73	%
Finance	34,208,412	41,910,000	8.30	%
Software	37,427,547	38,026,250	7.54	%
Media: Broadcasting & Subscription	38,137,844	37,733,004	7.48	%
Retail	28,764,221	27,525,897	5.45	%
Education	26,562,249	25,325,000	5.02	%
High Tech Industries	21,094,192	21,094,192	4.18	%
Beverage, Food, & Tobacco	20,709,134	18,213,945	3.61	%
Services: Consumer	17,952,663	17,640,255	3.50	%
Automotive	17,457,259	17,282,187	3.43	%
Energy: Oil & Gas	14,312,328	15,542,102	3.08	%
Consumer goods: non-durable	14,994,980	14,579,375	2.89	%
Chemicals, Plastics, & Rubber	11,835,100	11,707,835	2.32	%
Containers, Packaging, & Glass	11,437,711	10,869,000	2.15	%
Construction & Building	10,374,827	10,280,000	2.04	%
Utilities: Oil & Gas	9,853,435	9,853,435	1.95	%
Capital Equipment	7,535,876	7,929,775	1.57	%
Transportation: Cargo	6,808,345	6,841,739	1.36	%
Insurance	5,425,301	5,460,000	1.08	%
Hotel, Gaming, & Leisure	3,170,307	3,414,655	0.68	%
Environmental Industries	946,124	330,000	0.07	%
Services: Government	50,001	280,000	0.06	%
	$ 502,743,649	$ 504,483,668	100.00	%

STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

The following is a summary of industry concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Software	$ 48,560,675	$ 48,997,850	13.18	%
Healthcare & Pharmaceuticals	41,192,879	37,829,167	10.17	%
High Tech Industries	36,058,477	35,460,000	9.54	%
Finance	26,500,097	28,330,000	7.62	%
Services: Business	23,386,714	25,749,999	6.93	%
Capital Equipment	24,300,027	24,170,000	6.50	%
Media: Broadcasting & Subscription	21,680,239	23,665,000	6.36	%
Chemicals, Plastics, & Rubber	20,825,458	21,145,000	5.69	%
Services: Consumer	17,862,616	18,070,000	4.86	%
Construction & Building	17,913,413	17,980,000	4.84	%
Education	17,197,396	17,335,526	4.66	%
Consumer Goods: Durable	16,559,947	16,798,484	4.52	%
Consumer goods: non-durable	13,250,000	13,250,000	3.56	%
Retail	8,288,083	8,280,000	2.23	%
Automotive	7,848,470	8,058,746	2.17	%
Transportation: Cargo	6,785,894	6,840,000	1.84	%
Energy: Oil & Gas	6,766,968	6,700,000	1.80	%
Insurance	5,410,226	5,500,000	1.48	%
Beverage, Food, & Tobacco	3,964,242	3,580,000	0.96	%
Hotel, Gaming, & Leisure	3,284,942	3,420,000	0.92	%
Environmental Industries	766,442	580,000	0.16	%
Services: Government	50,001	100,000	0.03	%
	$ 368,453,206	$ 371,839,772	100.00	%

The following provides quantitative information about Level 3 fair value measurements as of December 31, 2018:

Description	Fair Value	Valuation Technique	Unobservable Inputs	Range (Average)[1]
First lien debt	$292,004,982	Income/Market[2] approach	HY credit spreads,	-1.03% to 2.59% (0.85%)

			Risk free rates Market multiples	-5.62% to 6.64% (1.64%) 4x to 22x (10x)[4]
Second lien debt	$149,661,220	Income/Market[2] approach	HY credit spreads, Risk free rates Market multiples	-0.00% to 2.66% (0.93%) -0.14% to 10.66% (1.70%) 2x to 17x (11x)[4]
Unsecured debt	$23,697,466	Income/Market approach[2]	HY credit spreads, Risk free rates Market multiples	-1.03% to 0.57% (-0.01%) -5.62% to 0.32% (-1.27%) 2x to 9x (3x)[4]
Equity investments	$39,120,000	Market approach[5]	Underwriting EBITDA Multiple	2x to 15x (10x)
Total Long Term Level 3 Investments	$504,483,668			

(1) Weighted average based on fair value as of December 31, 2018.

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NOTES TO THE FINANCIAL STATEMENTS
December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

(2) Inclusive of but not limited to (a) the market approach which is used to determine sufficient enterprise value, and (b) the income approach which is based on discounting future cash flows using an appropriate market yield.

(3) The Company calculates the price of the loan by discounting future cash flows, which include forecasted future LIBOR rates based on the published forward LIBOR curve at the valuation date, using an appropriate yield calculated as of the valuation date. This yield is calculated based on the loan s yield at the original investment and is adjusted as of the valuation date based on: changes in comparable credit spreads, changes in risk free interest rates (per swap rates), and changes in credit quality (via an estimated shadow rating). Significant movements in any of these factors would result in a significantly lower or higher fair value measurement. As an example, the Range (Average) for a first lien debt instruments in the table above indicates that the change in the HY spreads between the date a loan closed and the valuation date ranged from -1.03% (-103 basis points) to 2.59% (259 basis points). The average of all changes was 0.85%.

(4) Median of LTM (last twelve months) EBITDA multiples of comparable companies.

(5) The primary significant unobservable input used in the fair value measurement of the Company s equity investments is the EBITDA multiple (the Multiple). Significant increases (decreases) in the Multiple in isolation would result in a significantly higher (lower) fair value measurement. To determine the Multiple for the market approach, the Company considers current market trading and/or transaction multiple, portfolio company performance (financial ratios) relative to public and private peer companies and leverage levels, among other factors. Changes in one or more of these factors can have a similar directional change on other factors in determining the appropriate Multiple to use in the market approach.

The following provides quantitative information about Level 3 fair value measurements as of December 31, 2017:

Description	Fair Value	Valuation Technique	Unobservable Inputs	Range (Average)[(1)(3)]
First lien debt	$141,006,923	Income/Market[(2)] approach	HY credit spreads, Risk free rates Market multiples	-3.73% to 5.53% (-0.81%) -0.24% to 1.12% (0.54%) 11x to 13x (12x)[(4)]
Second lien debt	$178,432,850	Income/Market[(2)] approach	HY credit spreads, Risk free rates Market multiples	-2.52% to 4.78% (-0.58%) -0.28% to 1.01% (0.39%) 8x to 8x (8x)[(4)]

Unsecured debt	$27,430,000	Income/Market approach(2)	HY credit spreads, Risk free rates Market multiples	-0.67% to 3.93% (0.89%) 0.12% to 1.18% (0.52%) 1x to 14x (13x)(4)
Equity investments	$24,969,999	Market approach(5)	Underwriting multiple/ EBITDA Multiple	1x to 15x (9x)
Total Long Term Level 3 Investments	$371,839,772			

(1) Weighted average based on fair value as of December 31, 2017.

(2) Including but not limited to (a) the market approach which is used to determine sufficient enterprise value, and (b) the income approach which is based on discounting future cash flows using an appropriate market yield.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE (continued)

(3) The Company calculates the price of the loan by discounting future cash flows, which include forecasted future LIBOR rates based on the published forward LIBOR curve at the valuation date, using an appropriate yield calculated as of the valuation date. This yield is calculated based on the loan s yield at the original investment and is adjusted as of the valuation date based on: changes in comparable credit, changes in risk free interest rates (per swap rates), and changes in credit quality (via an estimated shadow rating). Significant movements in any of these factors could result in a significantly lower or higher fair value measurement. As an example, the Range (Average) for first lien debt instruments in the table above indicates that the change in the HY spreads between the date a loan closed and the valuation date ranged from -3.73% (-373 basis points) to 5.53% (553 basis points). The average of all changes was 0.81%.

(4) Median of LTM (last twelve months) EBITDA multiples of comparable companies.

(5) The primary significant unobservable input used in the fair value measurement of the Company s equity investments is the EBITDA multiple (the Multiple). Significant increases (decreases) in the Multiple in isolation could result in a significantly higher (lower) fair value measurement. To determine the Multiple for the market approach, the Company considers current market trading and/or transaction multiple, portfolio company performance (financial ratios) relative to public and private peer companies and leverage levels, among other factors. Changes in one or more of these factors can have a similar directional change on other factors in determining the appropriate Multiple to use in the market approach.

NOTE 7 COMMITMENTS AND CONTINGENCIES

The Company is currently not subject to any material legal proceedings, nor, to our knowledge, is any material legal proceeding threatened against us. From time to time, we may be a party to certain legal proceedings in the ordinary course of business, including proceedings relating to the enforcement of our rights under contracts with our portfolio companies. While the outcome of these legal proceedings cannot be predicted with certainty, we do not expect that these proceedings will have a material effect upon our business, financial condition or results of operations.

As of December 31, 2018, the Company had $21,213,961 of unfunded commitments to provide debt financing to eleven existing portfolio companies. As of December 31, 2017 the Company had $8,686,667 of unfunded commitments to provide debt financing to four existing portfolio companies. As of December 31, 2018, the Company had sufficient liquidity to fund such unfunded loan commitments should the need arise.

STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 8 FINANCIAL HIGHLIGHTS

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Per Share Data:[1]					
Net asset value at beginning of year/period	$13.81	$13.69	$13.19	$13.94	$14.54
Net investment income	1.42	1.21	1.39	1.33	1.34
Change in unrealized appreciation (depreciation)	(0.11)		1.49	(0.74)	(0.53)
Realized gain (loss)	0.35	0.31	(1.05)	0.03	0.04
Provision for taxes on realized gains	(0.02)				
Benefit (Provision) for taxes on unrealized appreciation			0.03	(0.01)	(0.02)
Total from investment operations	1.64	1.52	1.86	0.61	0.83
Sales Load		(0.09)			(0.01)
Offering Costs		(0.02)			
Stockholder distributions from:					
Net investment income	(1.03)	(1.20)	(1.36)	(1.33)	(1.31)
Net realized capital gains	(0.33)	(0.16)		(0.03)	(0.12)
Other[2][3]		0.07			0.01
Net asset value at the end of year/period	$14.09	$13.81	$13.69	$13.19	$13.94
Per share market value at end of year/period	$12.95	$13.14	$12.06	$9.64	$11.78
Total return based on market value[4]	8.68%	20.29%	42.83%	(7.76)%	(13.09)%
Weighted average shares outstanding at the end of period	15,953,571	14,870,981	12,479,959	12,479,961	12,281,178
Ratio/Supplemental Data:					
	$224,845,007	$220,247,242	$170,881,785	$164,651,104	$173,949,452

Net assets at the end of year/period					
Weighted average net assets	$223,750,302	$195,211,550	$165,189,142	$173,453,813	$176,458,141
Annualized ratio of gross operating expenses to net assets(7)(8)	13.72 %	11.10 %	13.20 %	11.16 %	9.92 %
Annualized ratio of net operating expenses to net assets(7)(8)	13.72 %	11.10 %	13.20 %	10.78 %	9.12 %
Annualized ratio of interest expense and other fees to net assets(9)	5.51 %	4.02 %	4.84 %	3.56 %	3.01 %
Annualized ratio of net investment income before fee waiver to net assets(7)(8)	10.09 %	9.21 %	10.71 %	9.11 %	8.40 %
Annualized ratio of net investment income to net assets(7)(8)	10.09 %	9.21 %	10.71 %	9.49 %	9.19 %
Portfolio Turnover(5)	32 %	48 %	16 %	29 %	19 %
Notes Payable	$48,875,000	$48,875,000	$25,000,000	$25,000,000	$25,000,000
Credit Facility Payable	$99,550,000	$40,750,000	$116,000,000	$109,500,000	$106,500,000
SBA-guaranteed debentures	$150,000,000	$90,000,000	$65,000,000	$65,000,000	$16,250,000
Asset Coverage Ratio(6)	2.51x	3.46x	2.21x	2.22x	2.32x

(1) Financial highlights are based on weighted average shares outstanding as of year/period ended.

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NOTE 8 FINANCIAL HIGHLIGHTS (continued)

(2) The per share impact of the Company s reinvestment of stockholder distributions has an impact to net assets of less than $0.01 per share during the applicable period.

(3) Includes the impact of different share amounts as a result of calculating certain per share data based on weighted average shares outstanding during the period and certain per share data based on shares outstanding as of the period end.

(4) Total return on market value is based on the change in market price per share since the end of the prior quarter and includes dividends paid, which are assumed to be reinvested. The total returns are not annualized.

(5) Calculated as the lesser of purchases or paydowns divided by average portfolio balance and is not annualized.

(6) Asset coverage ratio is equal to total assets less all liabilities and indebtedness not represented by senior securities over the aggregate amount of the senior securities. SBA-guaranteed debentures are excluded from the numerator and denominator.

(7) These ratios include the impact of the benefit (provision) for income taxes related to net unrealized loss (gain) on certain investments of $(67,953), $8,593, and $373,131 for the years ended December 31, 2018, 2017 and 2016 respectively, which are not reflected in net investment income, gross operating expenses or net operating expenses. The benefit (provision) for income taxes related to net realized loss or unrealized loss (gain) on investments at taxable subsidiaries to net assets for the years ended December 31, 2018, 2017 and 2016 is less than (.03)%, (0.01)% and (0.23)%, respectively.

(8) Deferred offering costs of $261,761 for the year ended December 31, 2016 are not annualized.

(9) Excludes debt extinguishment costs of $416,725 for the year ended December 31, 2017. Including these costs, this ratio would be 4.24%.

NOTE 9 CREDIT FACILITY

On November 7, 2012, the Company entered into a revolving credit facility (the Original Facility) with various lenders. SunTrust Bank, one of the lenders, served as administrative agent under the Original Facility. The Original Facility, as amended on November 21, 2014 and August 31, 2016, provided for borrowings in an aggregate amount of $120,000,000 on a committed basis with an accordion feature that allowed the Company to increase the aggregate commitments up to $195,000,000, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. The Company terminated the Original Facility on October 11, 2017, in conjunction with securing and entering into a new senior secured revolving credit agreement, dated as of October 10, 2017, as amended on March 28, 2018 and August 2, 2018, with ZB, N.A., dba Amegy Bank and various other lenders (the Credit Facility).

The Credit Facility, as amended, provides for borrowings up to a maximum of $180,000,000 on a committed basis with an accordion feature that allows the Company to increase the aggregate commitments up to $195,000,000, subject to new or existing lenders agreeing to participate in the increase and other customary conditions.

Borrowings under the Credit Facility bear interest, subject to the Company s election, on a per annum basis equal to (i) LIBOR plus 2.50% (or 2.75% during certain periods in which the Company s asset coverage ratio is equal to or below 1.90 to 1.00) with no LIBOR floor, or (ii) 1.50% (or 1.75% during certain periods in which the Company s asset coverage ratio is equal to or below 1.90 to 1.00) plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate

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December 31, 2018

NOTE 9 CREDIT FACILITY (continued)

plus 0.5% or one month LIBOR plus 1.0%. The Company pays unused commitment fees of 0.50% per annum on the unused lender commitments under the Credit Facility. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 10, 2021.

The Company s obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. The Credit Facility contains certain covenants, including but not limited to: (i) maintaining a minimum liquidity test of at least $10,000,000, including cash, liquid investments and undrawn availability, (ii) maintaining an asset coverage ratio of at least 1.75 to 1.0, and (iii) maintaining a minimum shareholder s equity. As of December 31, 2018, the Company was in compliance with these covenants.

As of December 31, 2018 and December 31, 2017, the outstanding balance under the Credit Facility was $99,550,000 and $40,750,000, respectively. The carrying amount of the amount outstanding under the Credit Facility approximates its fair value. The fair values of the Credit Facility is determined in accordance with ASC 820, which defines fair value in terms of the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of the Credit Facility is estimated based upon market interest rates for our own borrowings or entities with similar credit risk, adjusted for nonperformance risk, if any. The Company had previously incurred total costs of $3,117,715 in connection with obtaining, amending, and maintaining the Original Facility. The Company has incurred costs of $1,510,018 in connection with the current Credit Facility, which are being amortized over the life of the facility. Additionally, $341,979 of costs from the Original Facility will continue to be amortized over the remaining life of the Credit Facility. As of December 31, 2018 and 2017, $1,312,773 and $1,417,521 of such prepaid loan structure fees and administration fees had yet to be amortized, respectively. These prepaid loan fees are presented on our consolidated statement of assets and liabilities as a deduction from the debt liability attributable to the Credit Facility as required by ASU No. 2015-3.

The following is a summary of the Credit Facility, net of prepaid loan structure fees:

	December 31, 2018	December 31, 2017
Credit Facility payable	$ 99,550,000	$ 40,750,000
Prepaid loan structure fees	1,312,773	1,417,521
Credit facility payable, net of prepaid loan structure fees	$ 98,237,227	$ 39,332,479

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NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 9 CREDIT FACILITY (continued)

Interest is paid quarterly in arrears. The following table summarizes the interest expense and amortized loan fees on the Credit Facility for the years ended December 31, 2018, 2017, and 2016:

	For the years ended December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$3,737,735	$2,247,048	$3,383,572
Loan fee amortization	415,179	416,612	471,501
Commitment fees on unused portion	387,601	311,174	66,787
Administration fees	40,972	39,282	52,335
Total interest and financing expenses	$4,581,487	$3,014,116	$3,974,195
Loss on extinguishment of debt	$	$113,993	$
Weighted average interest rate	4.7 %	3.7 %	3.2 %
Effective interest rate (including fee amortization)	5.7 %	5.0 %	3.7 %
Average debt outstanding	$79,818,493	$60,053,425	$106,601,093
Cash paid for interest and unused fees	$4,158,382	$2,476,340	$3,423,226

NOTE 10 SBA-GUARANTEED DEBENTURES

Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. Under the regulations applicable to SBIC funds, a single licensee can have outstanding debentures guaranteed by the SBA subject to a regulatory leverage limit, up to two times the amount of regulatory capital. As of December 31, 2018 and 2017, the SBIC subsidiary had $75,000,000 and $67,500,000, respectively, in regulatory capital, as such term is defined by the SBA.

On August 12, 2014, we obtained exemptive relief from the SEC to permit us to exclude the debt of the SBIC subsidiary guaranteed by the SBA from our asset coverage test under the 1940 Act. The exemptive relief provides us with increased flexibility under the asset coverage test by permitting us to borrow up to $150,000,000 more than we would otherwise be able to absent the receipt of this exemptive relief.

On a stand-alone basis, the SBIC subsidiary held $225,525,663 and $161,992,327 in assets at December 31, 2018 and 2017, respectively, which accounted for approximately 42.9% and 40.4% of our total consolidated assets at December 31, 2018 and 2017, respectively.

Debentures guaranteed by the SBA have fixed interest rates that equal prevailing 10-year Treasury Note rates plus a market spread and have a maturity of ten years with interest payable semi-annually. The principal amount of the debentures is not required to be paid before maturity, but may be pre-paid at any time with no prepayment penalty. As of December 31, 2018 and 2017, the SBIC subsidiary had $150,000,000 and $90,000,000 of the SBA-guaranteed debentures outstanding, respectively. SBA-guaranteed debentures incur upfront fees of 3.425%, which consists of a 1.00% commitment fee and a 2.425% issuance discount, which are amortized over the life of the SBA-guaranteed debentures. Once pooled, which occurs in March and September each year, the SBA-guaranteed debentures bear interest at a fixed rate that is set to the current 10-year treasury rate plus a spread at each pooling date.

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NOTE 10 SBA-GUARANTEED DEBENTURES (continued)

The following table summarizes the SBIC subsidiary s SBA-guaranteed debentures as of December 31, 2018:

Issuance Date	Maturity Date	Debenture Amount	Interest Rate	SBA Annual Charge
October 14, 2014	March 1, 2025	$ 6,500,000	2.52 %	0.36 %
October 17, 2014	March 1, 2025	6,500,000	2.52 %	0.36 %
December 24, 2014	March 1, 2025	3,250,000	2.52 %	0.36 %
June 29, 2015	September 1, 2025	9,750,000	2.83 %	0.36 %
October 22, 2015	March 1, 2026	6,500,000	2.51 %	0.36 %
October 22, 2015	March 1, 2026	1,500,000	2.51 %	0.74 %
November 10, 2015	March 1, 2026	8,800,000	2.51 %	0.74 %
November 18, 2015	March 1, 2026	1,500,000	2.51 %	0.74 %
November 25, 2015	March 1, 2026	8,800,000	2.51 %	0.74 %
December 16, 2015	March 1, 2026	2,200,000	2.51 %	0.74 %
December 29, 2015	March 1, 2026	9,700,000	2.51 %	0.74 %
November 28, 2017	March 1, 2028	25,000,000	3.19 %	0.22 %
April 27, 2018	September 1, 2028	40,000,000	3.55 %	0.22 %
July 30, 2018	September 1, 2028	17,500,000	3.55 %	0.22 %
September 25, 2018	March 1, 2029	2,500,000	2.88 %(1)	0.22 %
Total SBA-guaranteed debentures		$ 150,000,000		

(1) Debenture interest rate will be set as determined by the SBA when pooled on March 20, 2019

As of December 31, 2018 and 2017, the carrying amount of the SBA-guaranteed debentures approximated their fair value. The fair values of the SBA-guaranteed debentures are determined in accordance with ASC 820, which defines fair value in terms of the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of the SBA-guaranteed debentures are estimated based upon market interest rates for our own borrowings or entities with similar credit risk, adjusted for nonperformance risk, if any. At December 31, 2018 and 2017, the SBA-guaranteed debentures would be deemed to be Level 3, as defined in Note 6.

As of December 31, 2018, the Company has incurred $5,137,500 in financing costs related to the SBA-guaranteed debentures since receiving our license, which were recorded as prepaid loan fees. As of December 31, 2018 and 2017,

$3,612,198 and $2,181,187 of prepaid financing costs had yet to be amortized, respectively. These prepaid loan fees are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3. See Note 1 for further discussion.

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NOTE 10 SBA-GUARANTEED DEBENTURES (continued)

The following is a summary of the SBA-guaranteed debentures, net of prepaid loan fees:

	December 31, 2018	December 31, 2017
SBA debentures payable	$ 150,000,000	$ 90,000,000
Prepaid loan fees	3,612,198	2,181,187
SBA Debentures, net of prepaid loan fees	$ 146,387,802	$ 87,818,813

The following table summarizes the interest expense and amortized fees on the SBA-guaranteed debentures for the years ended December 31, 2018, 2017 and 2016:

	For the years ended		
	December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$3,982,658	$2,067,308	$1,877,017
Debenture fee amortization	623,989	333,027	326,191
Total interest and financing expenses	$4,606,647	$2,400,335	$2,203,208
Weighted average interest rate	3.2 %	3.1 %	2.9 %
Effective interest rate (including fee amortization)	3.7 %	3.6 %	3.4 %
Average debt outstanding	$125,390,411	$67,328,767	$65,000,000
Cash paid for interest	$3,107,218	$2,019,095	$1,500,528

NOTE 11 NOTES

On May 5, 2014, the Company closed a public offering of $25,000,000 in aggregate principal amount of 6.50% notes (the 2019 Notes) due April 30, 2019. On August 21, 2017, the Company caused notices to be issued to the holders of its 2019 Notes regarding the Company s exercise of its option to redeem all of the issued and outstanding 2019 Notes, pursuant to Section 1101 of the Base Indenture dated as of May 5, 2014, between the Company and U.S. Bank National Association, as trustee, and Section 1.01(h)(i) of the First Supplemental Indenture dated as of May 5, 2014. The Company redeemed all $25,000,000 in aggregate principal amount of the 2019 Notes on September 20, 2017. The 2019 Notes were redeemed at 100% of their principal amount, plus the accrued and unpaid interest thereon through the redemption date. As a result of the redemption, the Company recognized a loss on the extinguishment of debt of $302,732 for the year ended December 31, 2017, due to the write off of the remaining deferred financing costs on the 2019 Notes.

The following table summarizes the interest expense and deferred financing costs on the 2019 Notes for the years ended December 31, 2018, 2017, and 2016:

	For the year ended December 31, 2018	December 31, 2017	December 31, 2016
Interest expense	$	$ 1,169,097	$ 1,625,000
Deferred financing costs		131,377	184,933
Administration fees		5,000	4,850
Total interest and financing expenses	$	$ 1,305,474	$ 1,814,783
Loss on extinguishment of debt	$	$ 302,732	$
Cash paid for interest	$	$ 1,376,736	$ 1,625,000

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NOTE 11 NOTES (continued)

On August 21, 2017, the Company issued $42,500,000 in aggregate principal amount of 5.75% fixed-rate notes due 2022 (the 2022 Notes). On September 8, 2017, the Company issued an additional $6,375,000 in aggregate principal amount of the 2022 Notes pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at the Company s option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. Interest is payable quarterly beginning December 15, 2017.

The Company used all of the net proceeds from the 2022 offering to fully redeem the 2019 Notes and a portion of the amount outstanding under the Original Facility. As of December 31, 2018 and 2017, the aggregate carrying amount of all Notes was $48,875,000 and $25,000,000 and the fair value of the Notes was approximately $47,604,250 and $49,520,150, respectively. The 2022 Notes are listed on New York Stock Exchange under the trading symbol SCA . The fair value of the Notes is based on the closing price of the security, which is a Level 2 input under ASC 820 due to sufficient trading volume.

In connection with the issuance and maintenance of the 2022 Notes, we have incurred $1,688,961 of fees that are being amortized over the term of the 2022 Notes, of which $1,233,203 and $1,568,512 remained to be amortized as of December 31, 2018 and 2017, respectively. These financing costs are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3.

The following table summarizes the interest expense and deferred financing costs on the 2022 Notes for the years ended December 31, 2018, 2017, 2016.

	For the year ended December 31, 2018	For the year ended December 31, 2017	For the year ended December 31, 2016
Interest expense	$ 2,810,312	$ 1,014,835	$
Deferred financing costs	332,404	118,066	
Administration fees	7,905	2,383	
Total interest and financing expenses	$ 3,150,621	$ 1,135,284	$
Cash paid for interest	$ 2,810,312	$ 889,932	$

The following is a summary of the Notes Payable, net of deferred financing costs:

	December 31, 2018	December 31, 2017

Notes payable	$ 48,875,000	$ 48,875,000
Deferred financing costs	1,233,203	1,568,512
Notes payable, net of deferred financing costs	$ 47,641,797	$ 47,306,488

The indenture and supplements thereto relating to the 2022 Notes contain certain covenants, including but not limited to (i) a requirement that the Company comply with the asset coverage requirements of the 1940 Act or any successor provisions, and (ii) a requirement to provide financial information to the holders of the notes and the trustee under the indenture if the Company should no longer be subject to the reporting requirements under the Exchange Act.

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NOTE 12 SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table sets forth the results of operations for the years ended December 31, 2018, 2017, and 2016. Results for any quarter are not necessarily indicative of results for the full year or for any future quarter.

	2018			
	Qtr. 1	Qtr. 2	Qtr. 3	Qtr. 4
Total Investment Income	$10,911,781	$12,619,657	$14,487,623	$15,247,277
Net Investment Income	$4,475,379	$4,727,236	$5,609,974	$7,823,948
Net Increase in Net Assets from Operations	$7,343,929	$7,603,246	$8,884,517	$2,362,886
Total Investment Income per share(1)	$0.68	$0.79	$0.91	$0.96
Net Investment Income per share(1)	$0.28	$0.30	$0.35	$0.49
Net Increase in Net Assets from Operations per share(1)	$0.46	$0.48	$0.56	$0.14

	2017			
	Qtr. 1	Qtr. 2	Qtr. 3	Qtr. 4
Total Investment Income	$9,863,980	$10,394,365	$9,978,345	$9,411,503
Net Investment Income	$4,143,627	$4,938,459	$4,475,952	$4,412,722
Net Increase in Net Assets from Operations	$6,024,752	$6,044,766	$5,636,598	$4,907,141
Total Investment Income per share(1)	$0.79	$0.68	$0.64	$0.59
Net Investment Income per share(1)	$0.33	$0.32	$0.29	$0.28
Net Increase in Net Assets from Operations per share(1)	$0.48	$0.39	$0.36	$0.31

	2016			
	Qtr. 1	Qtr. 2	Qtr. 3	Qtr. 4
Total Investment Income	$9,467,833	$9,623,169	$10,202,753	$10,196,442
Net Investment Income	$4,099,290	$3,945,102	$4,608,743	$4,659,066
Net Increase in Net Assets from operations	$2,523,849	$5,029,920	$9,927,466	$5,717,827
Total Investment Income per share(1)	$0.76	$0.77	$0.82	$0.82
Net Investment Income per share(1)	$0.33	$0.32	$0.37	$0.37

Net Increase in Net Assets from Operations per share[1]	$0.20	$0.41	$0.80	$0.45

(1) Per share amounts are calculated using weighted average shares outstanding during the period.

NOTE 13 INCOME TAXES

As of December 31, 2018 and December 31, 2017, the Company had $8,572,366 and $394,559, respectively, of undistributed ordinary income.[1] Undistributed capital gains were $700,000 and $723,753 for the periods ended December 31, 2018 and December 31, 2017, respectively. Undistributed qualified dividends were $31,504 and $0 for the years ended December 31, 2018 and 2017, respectively. The Company intends to distribute all of the undistributed ordinary income as of December 31, 2018 within the required period of time such that the Company will not have to pay corporate-level U.S. federal income tax for the year ended December 31, 2018. We will be

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NOTE 13 INCOME TAXES (continued)

subject to a 4% nondeductible U.S. federal excise tax on our undistributed income to the extent we did not distribute an amount equal to at least 98% of our net ordinary income plus 98.2% of our capital gain net income attributable to the period. The Company has accrued $316,092 and $27,717 of U.S. federal excise tax for the tax years ended December 31, 2018 and December 31, 2017, respectively, independent of prior year adjustments. See Note 1 for further discussion of tax expense in each year.

Ordinary dividend distributions from a RIC do not qualify for the reduced maximum tax rate on qualified dividend income from domestic corporations, except to the extent that the RIC received the income in the form of qualifying dividends from domestic corporations and qualified foreign corporations. The tax character[2] of distributions paid in the years ended December 31, 2018 and 2017 was as follows:

	December 31, 2018	December 31, 2017
Ordinary income	$ 15,492,724	$ 17,823,305
Qualified dividends	250,000	1,500,000
Distributions of long-term capital gains[2]	5,947,826	1,000,000
Total distributions accrued or paid to common stockholders	$ 21,690,550	$ 20,323,305

(1) The Company s taxable income for each period is an estimate and will not be finally determined until the Company files its tax return for each year. Therefore, final taxable income earned in each period, and the undistributed ordinary income and capital gains for each period carried forward for distribution in the following period, may be different than this estimate.

(2) Distributions of long-term capital gains of $5,947,826 as of December 31, 2018 differs from distributions of net capital gains on the Consolidated Statement of Changes in Net Assets because certain long-term capital gains were recognized in Taxable Subsidiaries. The qualified dividend amount in 2018 derived from qualified dividends received by the Company from a portfolio company. The qualified dividend amount in 2017 is derived from a long-term capital gain transaction and represents a cash distribution from the Taxable Subsidiary to the Company. Additional differences arise because certain prepayment gains are characterized differently for tax reporting purposes.

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NOTE 13 INCOME TAXES (continued)

Listed below is a reconciliation of Net increase in net assets resulting from operations to taxable income and total distributions declared to common stockholders for the years ended December 31, 2018, 2017 and 2016:

	2018	2017	2016
Net increase in net assets resulting from operations (includes NII, realized gain/loss, unrealized gain/loss and taxes)	$26,194,578	$22,613,257	$23,199,062
Net change in unrealized appreciation (depreciation)	1,646,549	22,072	(18,603,401)
Income tax provision (benefit)	67,953	(8,593)	(373,131)
Pre-tax (income) expense, (gain) loss reported at Taxable Subsidiaries, not consolidated for tax purposes	416,203	(4,721,039)	13,451,549
Book income and tax income differences, including debt origination, interest accrual, income from pass-through investments, dividends, realized gains (losses) and changes in estimates	1,524,556	1,835,779	583,041
Estimated taxable income	$29,849,839	$19,741,476	$18,257,120
Taxable income earned in prior year and carried forward for distribution in current year	(662,990)	(106,530)	(1,395,300)
Taxable income earned prior to period end and carried forward for distribution next period	(9,303,869)	(1,118,312)	(1,307,452)
Distribution payable as of period end and paid in following period	1,807,570	1,806,671	1,413,982
Total distributions accrued or paid to common stockholders	$21,690,550	$20,323,305	$16,968,350

The aggregate gross unrealized appreciation and depreciation, the net unrealized appreciation, and the aggregate cost of the Company s portfolio company securities for federal income tax purposes as of December 31, 2018 and December 31, 2017 were as follows:

	2018	2017
Aggregate cost of portfolio securities for federal income tax purposes	$503,079,738	$368,453,206
Gross unrealized appreciation of portfolio company securities	18,423,224	10,263,285
Gross unrealized depreciation of portfolio company securities	(16,683,205)	(6,876,717)
Net unrealized appreciation of portfolio company securities	$1,740,019	$3,386,568

As of December 31, 2018, the Taxable Subsidiaries had generated unrealized losses in investments, net operating loss (NOL) carryovers and capital loss carryovers creating a net deferred tax asset equal to $1,282,487, as reflected below.

As of December 31, 2018, for U.S. federal income tax purposes, the Taxable Subsidiaries had capital loss carryforwards totaling $7,189,833, which, if unused, will expire in the taxable year 2021. As of December 31, 2018, for U.S. federal income tax purposes, the Taxable Subsidiaries had net operating loss carryforwards totaling $1,615,912 which, if unused, will expire during the tax years 2034 through 2037. Due to the nature of the Taxable Subsidiaries holdings, a valuation allowance was established when management

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 13 INCOME TAXES (continued)

determined it is more likely than not that some of the deferred tax assets will not be realized prior to expiration. Although our future projections indicate that we may be able to realize some of these deferred tax assets, due to the degree of uncertainty of these projections, management has recorded a deferred tax asset valuation allowance of $1,350,441.

The deferred tax asset and deferred tax liability amounts, before valuation allowance, reflected below, take into account the reduction in corporate income tax rate from 35% to 21% as enacted by the Tax Cuts and Jobs Act of 2017 (Tax Reform) as of the year ended December 31, 2017. Before the effect of Tax Reform, the ending net deferred tax asset at December 31, 2017 would have been approximately $2,612,000, compared to the reflected ending net deferred tax asset of $1,567,062, before valuation allowance. Therefore the reduction in corporate tax rates had the effect of reducing the Taxable Subsidiaries net deferred tax asset by approximately $1,045,000 for the year ended December 31, 2017. This reduction also resulted in a reduction in the required valuation allowance in an equal amount, resulting in $0 net change in tax expense arising as a result of the Tax Reform rate reduction.

	2018	2017
Deferred Tax Asset	$2,930,694	$2,779,563
Deferred Tax Liability	(1,648,207)	(1,212,501)
Total Deferred Tax Asset before valuation allowance	$1,282,487	$1,567,062
Deferred tax valuation allowance	$(1,350,440)	$(1,567,062)
Net Deferred Tax Liability	$(67,953)	$

In connection with the gain realized from the exit of its equity investment in Eating Recovery Center, LLC, the Company recorded an income tax provision on realized gains of $267,975 for the year ended December 31, 2018. No income tax provision was recorded on realized gains from the exit of equity investments for the years ended December 31, 2017 and 2016.

Although the Company files federal and state tax returns, its major tax jurisdiction is federal. The 2015, 2016 and 2017 federal tax years for the Company remain subject to examination by the Internal Revenue Service.

NOTE 14 SUBSEQUENT EVENTS

Investment Portfolio

On January 4, 2019, the Company received full repayment on the first lien term loan of EOS Fitness OPCO Holdings, LLC for total proceeds of $3,064,655. The Company also received a distribution related to our equity of $126,190.

On January 7, 2019, the Company received $278,428 in full realization on the equity of OGS Holdings, Inc., resulting in a realized gain $228,427.

On February 4, 2019, the Company invested $8,500,000 in the first lien term loan of ASC Communications, LLC, an existing portfolio company.

On February 8, 2019, the Company invested $12,250,000 in the first lien term loan of Exacta Land Surveyors LLC, a provider of land surveys and field management services used to facilitate the purchasing, selling, and development of residential real estate in the U.S. Additionally, the Company committed $1,500,000 in the unfunded revolver, $4,000,000 million in the unfunded delayed draw term loan, and the Company invested $904,250 in the equity of the company.

On February 15, 2019, the Company received $52,562 in full realization on the equity of Glori Energy Production, LLC.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE FINANCIAL STATEMENTS December 31, 2018

NOTE 14 SUBSEQUENT EVENTS (continued)

On February 28, 2019, the Company invested $1,428,571 in the first lien term loan of Convergence Technologies, Inc., an existing portfolio company. Additionally, we funded $5.4 million under the existing delayed draw term loan and an additional $54,614 in the equity of the company.

Credit Facility

The outstanding balance under the Credit Facility as of March 4, 2019 was $112,800,000.

SBA-guaranteed Debentures

The total balance of SBA-guaranteed debentures outstanding as of March 4, 2019 was $150,000,000.

Dividend Declared

On January 11, 2019, the Company s board of directors declared a regular monthly dividend for each of January, February and March 2019 as follows:

Declared	Ex-Dividend Date	Record Date	Payment Date	Amount per Share
1/11/2019	1/30/2019	1/31/2019	2/15/2019	$ 0.1133
1/11/2019	2/27/2019	2/28/2019	3/15/2019	$ 0.1133
1/11/2019	3/28/2019	3/29/2019	4/15/2019	$ 0.1133

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STELLUS CAPITAL INVESTMENT CORPORATION

Consolidated Schedule of Investments in and Advances to Affiliates December 31, 2018 (dollars in thousands)

This schedule should be read in conjunction with Stellus s consolidated financial statements, including the consolidated schedule of investments and notes to the consolidated financial statements.

(1) The principal amount and ownership detail for equity investments is included in the consolidated schedule of investments.

(2) Represents the total amount of interest, fees and dividends credited to income for the portion of the period for which an investment was included in Control or Affiliate categories, respectively. For investments transferred between Control and Affiliate categories during the period, any income or investment balances related to the time period it was in the category other than the one shown at period end is included in Amounts from investments transferred from other 1940 Act classifications during the period.

(3) Gross additions include increases in the cost basis of investments resulting from new portfolio investments, follow-on investments and accrued PIK interest, and the exchange of one or more existing securities for one or more new securities. Gross additions also include the movement of an existing portfolio company into this category and out of a different category.

(4) Gross reductions include decreases in the cost basis of investments resulting from principal repayments or sales and the exchange of one or more existing securities for one or more new securities. Gross reductions also include the movement of an existing portfolio company out of this category and into a different category. During the year ended December 31, 2018, all gross reductions on our affiliated investment were repayments of our investment.

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PROSPECTUS

Stellus Capital Investment Corporation

Common Stock
Preferred Stock
Subscription Rights
Debt Securities
Warrants

We may offer, from time to time in one or more offerings, up to $200,000,000 of our common stock, preferred stock, subscription rights, debt securities or warrants to purchase common stock, preferred stock or debt securities, which we refer to, collectively, as the securities. There is $102,383,451 of securities available for issuance under this prospectus as a result of our issuance of $48,875,000 in aggregate principal amount of 5.75% notes in August 2017, $44,591,250 of shares of our common stock in April 2016 and $4,150,299 of shares of common stock through an at-the-market sales program during 2017. Our securities may be offered at prices and on terms to be disclosed in one or more supplements to this prospectus. You should read this prospectus and the applicable prospectus supplement carefully before you invest in our securities.

Our securities may be offered directly to one or more purchasers through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will identify any agents or underwriters involved in the sale of our securities, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See Plan of Distribution. We may not sell any of our securities through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of such securities.

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company under the Investment Company Act of 1940, as amended, or the 1940 Act. Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation. The companies in which we invest are typically highly leveraged, and, in most cases, our investments in such companies will not be rated by national rating agencies. If such investments were rated, we believe that they would likely receive a rating below investment grade (i.e., below BBB or Baa), which are often referred to as junk.

On June 25, 2018, the last reported sale price of our common stock on the New York Stock Exchange was $13.22. We are required to determine the net asset value per share of our common stock on a quarterly basis. On March 31, 2018, our net asset value per share was $13.93.

Shares of closed-end investment companies, including business development companies, frequently trade at a discount to their net asset value. If our shares trade at a discount to our net asset value, it will likely increase the risk of loss for purchasers in this offering. We are not generally able to issue and sell our common stock at a price below net asset value per share. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below then-current net asset value per share of our common stock if our board of directors determines that such sale is in our best interests, and if our stockholders approve such sale. At our 2017 annual meeting of stockholders, our stockholders voted to allow us to issue common stock at a price below net asset value per share for the period ending on the earlier of the one-year anniversary of the date of the Company s 2017 Annual Meeting of Stockholders and the date of the Company s 2018 Annual Meeting of Stockholders. The proposal approved by our stockholders did not specify a maximum discount below net asset value at which we are able to issue our common stock, although the number of shares sold in each offering may not exceed 25% of our outstanding common stock immediately prior to such sale. We are seeking similar approval at our 2018 Annual Meeting of Stockholders, scheduled for June 28, 2018. We cannot issue shares of our common stock below net asset value unless our board of directors determines that it would be in our and our stockholders best interests to do so. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. In addition, continuous sales of common stock below net asset value may have a negative impact on total returns and could have a negative impact on the market price of our shares of common stock. See Sales of Common Stock Below Net Asset Value.

Investing in our common stock involves a high degree of risk. Before buying any shares, you should read the discussion of the material risks of investing in our common stock in Risk Factors beginning on page 17 of this prospectus.

This prospectus and the accompanying prospectus supplement contain important information you should know before investing in our common stock. Please read this prospectus and the accompanying prospectus supplement before you invest and keep it for future reference. We file annual, quarterly and current reports, proxy statements and other information about us with the Securities and Exchange Commission, or SEC. The SEC also maintains a website at *http://www.sec.gov* that contains such information. This information is also available free of charge by contacting us at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, Attention: Investor Relations, or by calling us collect at (713) 292-5400 or on our website at *www.stelluscapital.com* (under the Public Investors section). Information contained on our website is not incorporated by reference into this prospectus, and you should not consider that information to be part of this prospectus or the accompanying prospectus supplement.

The Securities and Exchange Commission has not approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is June 29, 2018

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ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we have filed with the SEC using the shelf registration process. Under the shelf registration process, we may offer, from time to time, up to $200,000,000 of our securities on terms to be determined at the time of the offering. This prospectus provides you with a general description of the securities that we may offer. Each time we use this prospectus to offer securities, we will provide a prospectus supplement that will contain specific information about the terms of that offering. The prospectus supplement may also add, update or change information contained in this prospectus. Please carefully read this prospectus and any accompanying prospectus supplement together with the additional information described under Risk Factors and Available Information before you make an investment decision.

No dealer, salesperson or other person is authorized to give any information or to represent anything not contained in this prospectus or any accompanying supplement to this prospectus. You must not rely on any unauthorized information or representations not contained in this prospectus or any accompanying prospectus supplement as if we had authorized it. This prospectus and any accompanying prospectus supplement do not constitute an offer to sell or a solicitation of any offer to buy any security other than the registered securities to which they relate, nor do they constitute an offer to sell or a solicitation of an offer to buy any securities in any jurisdiction to any person to whom it is unlawful to make such an offer or solicitation in such jurisdiction. The information contained in this prospectus and any accompanying prospectus supplement is accurate as of the dates on their covers. Our financial condition, results of operations and prospects may have changed since that date. To the extent required by law, we will amend or supplement the information contained in this prospectus and any accompanying prospectus supplement to reflect any material changes to such information subsequent to the date of the prospectus and any accompanying prospectus supplement and prior to the completion of any offering pursuant to the prospectus and any accompanying prospectus supplement.

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PROSPECTUS SUMMARY

This summary highlights some of the information in this prospectus. It is not complete and may not contain all of the information that you may want to consider. You should read the more detailed information set forth under Risk Factors and the other information included in this prospectus and any prospectus supplement carefully.

Except as otherwise indicated, the terms we, us, our, and the Company refer to Stellus Capital Investment Corporation; and Stellus Capital Management refers to our investment adviser and administrator, Stellus Capital Management, LLC.

Stellus Capital Investment Corporation

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company, or BDC , under the Investment Company Act of 1940, or the 1940 Act. We originate and invest primarily in private middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA (earnings before interest, taxes, depreciation and amortization)) through first lien, second lien, unitranche and mezzanine debt financing, with corresponding equity co-investments. Unitranche debt is typically structured as first lien loans with certain risk characteristics of mezzanine debt. Mezzanine debt includes senior unsecured and subordinated loans.

Our investment activities are managed by our investment adviser, Stellus Capital Management, an investment advisory firm led by Robert T. Ladd and its other senior investment professionals. We source investments primarily through the extensive network of relationships that the senior investment professionals of Stellus Capital Management have developed with financial sponsor firms, financial institutions, middle-market companies, management teams and other professional intermediaries. The companies in which we invest are typically highly leveraged, and, in most cases, our investments in such companies will not be rated by national rating agencies. If such investments were rated, we believe that they would likely receive a rating which is often referred to as junk.

Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation. We seek to achieve our investment objective by:

- accessing the extensive origination channels that have been developed and established by the Stellus Capital Management investment professionals that include long-standing relationships with private equity firms, commercial banks, investment banks and other financial services firms;
- investing in what we believe to be companies with strong business fundamentals, generally within our core middle-market company focus;
- focusing on a variety of industry sectors, including business services, energy, general industrial, government services, healthcare, software and specialty finance;
- focusing primarily on directly originated transactions;
- applying the disciplined underwriting standards that the Stellus Capital Management investment professionals have developed over their extensive investing careers; and
- capitalizing upon the experience and resources of the Stellus Capital Management investment team to monitor our investments.

In addition, we received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). Under the terms of the relief permitting us to co-invest with other funds managed by Stellus Capital Management, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is consistent with our investment objectives and strategies. We intend to co-invest, subject to the conditions included in the exemptive order we received from

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the SEC, with private credit funds managed by Stellus Capital Management that have an investment strategy that is identical to our investment strategy. We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification.

As a BDC, we are required to comply with regulatory requirements, including limitations on our use of debt. We are permitted to, and expect to continue to, finance our investments through borrowings.

Prior to March 23, 2018, Section 61(a) of the 1940 Act (which incorporates the requirements of Sections 18(a)(1) and 18(a)(2) of the 1940 Act) did not permit a BDC to issue senior securities unless, at the time of issuance, the BDC had an asset coverage ratio of at least 200%, taking into account that issuance of senior securities (the Asset Coverage Ratio). However, on March 23, 2018, the Small Business Credit Availability Act (the SBCA) was signed into law by the President. The SBCA, among other things, permits BDCs to be subject to a minimum Asset Coverage Ratio of 150% (the 150% Asset Coverage), if specific conditions are satisfied, when issuing senior securities. In other words, prior to the enactment of the SBCA, a BDC could borrow $1 for investment purposes for every $1 of investor equity. Now, for those BDCs that satisfy the Act s approval and disclosure requirements, the BDC can borrow $2 for investment purposes for every $1 of investor equity.

The SBCA provides that in order for a BDC whose common stock is traded on a national securities exchange to be subject to 150% Asset Coverage, the BDC must either obtain: (i) approval of the required majority of its non-interested directors who have no financial interest in the proposal, which would become effective one year after the date of such approval (the Board Effective Date), or (ii) obtain stockholder approval (of more than 50% of the votes cast for the proposal at a meeting in which quorum is present), which would become effective on the first day after the date of such stockholder approval.

On April 4, 2018, our board of directors (the Board), including a majority of the non-interested directors who have no financial interest in this proposal, deemed it in the best interests of the Company and its stockholders for the Company to be subject to 150% Asset Coverage. Our Board believes that having the flexibility for the Company to incur additional leverage in certain instances is in the best interests of stockholders. In connection with this determination, our Board approved a resolution permitting the Company to be subject to 150% Asset Coverage, to be effective on the Board Effective Date, or April 4, 2019. This approval will allow us to incur twice as much debt as we could have without such approval after the 150% Asset Coverage becomes effective.

In addition, the Board also approved and recommended that stockholders vote for a proposal to authorize the Company to be subject to 150% Asset Coverage at our 2018 Annual Meeting, scheduled for June 28, 2018. If our stockholders approve this proposal, the reduced Asset Coverage Ratio would be effective the day after the 2018 Annual Meeting. Because we have received Board approval, if the proposal does not receive approval of the majority of the votes cast at the meeting, we will be subject to the reduced Asset Coverage Ratio beginning on April 4, 2019.

The amount of leverage that we employ will depend on our assessment of market conditions and other factors at the time of any proposed borrowing, such as the maturity, covenant package and rate structure of the proposed borrowings, our ability to raise funds through the issuance of our securities and the risks of such borrowings within the context of our investment outlook. Ultimately, we only intend to use leverage if the expected returns from borrowing to make investments will exceed the cost of such borrowings. For more information about the expected amount of and costs associated with our borrowings, see Fees and Expenses in this prospectus.

We have elected and qualified to be treated for federal income tax purposes as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code, or the Code. As a RIC, we generally will not have to pay corporate-level federal income taxes on any net ordinary income or capital gains that we distribute to our stockholders as dividends if we meet certain source-of-income, distribution and asset diversification requirements.

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SBIC License

Our wholly owned subsidiary holds a license to operate as a small business investment company, or SBIC. Our wholly-owned SBIC subsidiary s SBIC license allows it to obtain leverage by issuing SBA-guaranteed debentures up to a maximum of $150 million under current SBIC regulations, subject to required capitalization of the SBIC subsidiary and other requirements. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. We believe that the SBA-guaranteed debentures are an attractive source of debt capital.

We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the asset coverage ratio we are required to maintain under the 1940 Act. This exemptive relief allows us increased flexibility under the asset coverage test by allowing us to borrow up to $150.0 million more than we would otherwise be able to borrow absent the receipt of this exemptive relief based on regulatory capital of $75.0 million at March 31, 2018.

Portfolio Composition

Our investments generally range in size from $5.0 million to $30.0 million, and we may also selectively invest in larger positions. We generally expect that the size of our positions will increase in proportion to the size of our capital base. Pending such investments, we may reduce our outstanding indebtedness or invest in cash, cash equivalents, U.S. government securities and other high-quality debt investments with a maturity of one year or less. In the future, we may adjust opportunistically the percentage of our assets held in various types of loans, our principal loan sources and the industries to which we have greatest exposure, based on market conditions, the credit cycle, available financing and our desired risk/return profile.

The following table provides a summary of our portfolio investments as of March 31, 2018:

		As of March 31, 2018 ($ in millions)	
Number of investments		52	
Fair value[a]		$ 431.3	
Cost		$ 426.4	
% of portfolio at fair value	first lien debt[a]	46.2	%
% of portfolio at fair value	second lien debt	41.2	%
% of portfolio at fair value	mezzanine debt	6.2	%
% of portfolio at fair value	equity	6.4	%
Weighted-average annual yield[b]		11.1	%

(a) As of March 31, 2018, $383.9 million of our debt investments at fair value were at floating interest rates, which represented approximately 89% of our total portfolio of debt investments at fair value. As of March 31, 2018, $47.4 million of our debt investments at fair value were at fixed interest rates, which represented approximately 11% of our total portfolio of debt investments at fair value.

(b)

The weighted average yield on all of our debt investments as of March 31, 2018, was approximately 11.1%, of which approximately 10.3% was current cash interest. The weighted average yield of our debt investments on accrual is not the same as a return on investment for our stockholders but, rather, relates to a portion of our investment portfolio and is calculated before the payment of all of our and our subsidiaries fees and expenses. The weighted average yield was computed using the effective interest rates for all of our debt investments, which represents the interest rate on our debt investment restated as an interest rate payable annually in arrears and is computed including cash and payment in kind, or PIK interest, as well as including accretion of original issue discount. There can be no assurance that the weighted average yield will remain at their current level.

(c) Includes unitranche investments, which account for 16.1% of our investment portfolio at fair value.

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Leverage

Credit Facility. We have entered into a senior secured revolving credit agreement, dated as of October 10, 2017, with ZB, N.A., dba Amegy Bank and various other leaders (the Credit Facility). The Credit Facility provides for borrowings up to a maximum of $140.0 million on a committed basis with an accordion feature that allows the Company to increase the aggregate commitments up to 195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. Borrowings under the Credit Facility bear interest, subject to our election, on a per annum basis equal to (i) LIBOR plus 2.50% with no LIBOR floor or (ii) 1.50% plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%. We pay unused commitment fees of 0.50% per annum on the unused lender commitments. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 1, 2021. Our obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. As of March 31, 2018, we had approximately $118.3 million outstanding under the Credit Facility.

5.75% Notes. On August 21, 2017, we issued $42.5 million in aggregate principal amount of 5.75% fixed-rate notes due 2022 (the 2022 Notes) and issued an additional $6.4 million in aggregate principal amount of the 2022 Notes pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at the Company s option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. As of March 31, 2018, we had $48.9 million of 2022 Notes outstanding.

SBA-guaranteed Debentures. Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. As of March 31, 2018, the SBIC subsidiary had $90.0 million of SBA-guaranteed debentures outstanding.

Stellus Capital Management

Stellus Capital Management manages our investment activities and is responsible for analyzing investment opportunities, conducting research and performing due diligence on potential investments, negotiating and structuring our investments, originating prospective investments and monitoring our investments and portfolio companies on an ongoing basis.

The senior investment professionals of Stellus Capital Management have an average of over 28 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing loans and debt securities through market cycles. The Stellus Capital Management investment professionals continue to provide investment sub-advisory services to D. E. Shaw & Co., L.P. and its associated investment funds (the D. E. Shaw group) with respect to an approximately $90.0 million investment portfolio (as of March 31, 2018) in middle-market companies pursuant to sub-advisory arrangements.

In addition to serving as our investment adviser and the sub-advisor to the D. E. Shaw group as noted above, Stellus Capital Management currently manages a private credit fund that has an investment strategy that is identical to our investment strategy and energy private equity funds. We received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management (other than the D. E. Shaw group funds) where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification. We will not co-invest with the energy private equity funds, as the energy private equity funds focus on predominantly equity-related investments, and we focus on predominantly credit-related investments.

Stellus Capital Management is headquartered in Houston, Texas, and also maintains offices in the Washington, D.C. area and Charlotte, North Carolina.

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Market Opportunity

We originate and invest primarily in private middle-market companies through first lien, second lien, unitranche and mezzanine debt financing, with a corresponding equity co-investment. We believe the environment for investing in middle-market companies is attractive for several reasons, including:

Robust Demand for Debt Capital. We believe that private equity firms have significant committed but uncalled capital, a large portion of which is still available for investment in the United States. We expect the large amount of uninvested capital commitments will drive buyout activity over the next several years, which should, in turn, create lending opportunities for us. In addition to increased buyout activity, a high volume of senior secured and high yield debt was originated in the calendar years 2011 through 2013 and will come due in the near term and, accordingly, we believe that new financing opportunities will increase as many companies seek to refinance this indebtedness.

Reduced Availability of Capital for Middle-Market Companies. We believe there are fewer providers of, and less capital available for financing to middle-market companies, as compared to the time period prior to the economic downturn that began in December 2007. We believe that, as a result of that downturn, many financing providers have chosen to focus on large, liquid corporate loans and managing capital markets transactions rather than lending to middle-market businesses. In addition, we believe regulatory changes, including the adoption of the Dodd-Frank Act and the introduction of the international capital and liquidity requirements under the Basel III Accords, or Basel III, have caused banks to curtail their lending to middle-market-companies. As a result, we believe that less competition will facilitate higher quality deal flow and allow for greater selectivity throughout the investment process.

Attractive Deal Pricing and Structures. We believe that the pricing of middle-market debt investments is higher, and the terms of such investments are more conservative, compared to larger liquid, public debt financings, due to the more limited universe of lenders as well as the highly negotiated nature of these financings. These transactions tend to offer stronger covenant packages, higher interest rates, lower leverage levels and better call protection compared to larger financings. In addition, middle-market loans typically offer other investor protections such as default penalties, lien protection, change of control provisions and information rights for lenders.

Specialized Lending Requirements. Lending to middle-market companies requires in-depth diligence, credit expertise, restructuring experience and active portfolio management. We believe that several factors render many U.S. financial institutions ill-suited to lend to middle-market companies. For example, based on the experience of Stellus Capital Management s investment professionals, lending to middle-market companies in the United States (a) is generally more labor intensive than lending to larger companies due to the smaller size of each investment and the fragmented nature of the information available with respect to such companies, (b) requires specialized due diligence and underwriting capabilities, and (c) may also require more extensive ongoing monitoring by the lender. We believe that, through Stellus Capital Management, we have the experience and expertise to meet these specialized lending requirements.

Competitive Strengths

We believe that the following competitive strengths will allow us to achieve positive returns for our investors:

Experienced Investment Team. Through our investment adviser, Stellus Capital Management, we have access to the experience and expertise of the Stellus Capital Management investment professionals, including its senior investment professionals who have an average of over 28 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing loans and debt securities through market cycles. We believe the members of Stellus Capital Management s investment professionals are proven and experienced, with extensive capabilities in leveraged credit investing, having participated in these markets for the predominant portion of their careers. We believe that the experience and demonstrated ability of the Stellus Capital Management investment team to complete transactions enhances the quantity and quality of investment opportunities available to us.

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Established, Rigorous Investment and Monitoring Process. The Stellus Capital Management investment professionals have developed an extensive review and credit analysis process. Each investment that is reviewed by Stellus Capital Management is brought through a structured, multi-stage approval process. In addition, Stellus Capital Management takes an active approach in monitoring all investments, including reviews of financial performance on at least a quarterly basis and regular discussions with management. Stellus Capital Management s investment and monitoring process and the depth and experience of its investment professionals should allow it to conduct the type of due diligence and monitoring that enables it to identify and evaluate risks and opportunities.

Demonstrated Ability to Structure Investments Creatively. Stellus Capital Management has the expertise and ability to structure investments across all levels of a company s capital structure. Furthermore, we believe that current market conditions will allow us to structure attractively priced debt investments and may allow us to incorporate other return-enhancing mechanisms such as commitment fees, original issue discounts, early redemption premiums, payment-in-kind, or PIK, interest or some form of equity securities.

Resources of Stellus Capital Management Platform. We have access to the resources and capabilities of Stellus Capital Management, which has 17 investment professionals, including Robert T. Ladd, Dean D Angelo, Joshua T. Davis and Todd A. Overbergen, who are supported by six managing directors, two principals, two vice presidents and three analysts. These individuals have developed long-term relationships with middle-market companies, management teams, financial sponsors, lending institutions and deal intermediaries by providing flexible financing throughout the capital structure. We believe that these relationships provide us with a competitive advantage in identifying investment opportunities in our target market. We also expect to benefit from Stellus Capital Management s due diligence, credit analysis, origination and transaction execution experience and capabilities, including the support provided with respect to those functions by Mr. Huskinson, who serves as our chief financial officer and chief compliance officer, and his staff of eight finance and operations professionals.

Risk Factors

An investment in our securities is subject to risks. The following is a summary of the principal risks that you should carefully consider before investing in our securities. In addition, see Risk Factors beginning on page 17 of this prospectus to read about factors you should consider before deciding to invest in our securities.

We are dependent upon key personnel of Stellus Capital Management for our future success. If Stellus Capital Management were to lose any of its key personnel, our ability to achieve our investment objective could be significantly harmed.
Our business model depends to a significant extent upon strong referral relationships. Any inability of Stellus Capital Management to maintain or develop these relationships, or the failure of these relationships to generate investment opportunities, could adversely affect our business.
Our financial condition, results of operations and cash flows will depend on our ability to manage our business effectively.
There are significant potential conflicts of interest that could negatively affect our investment returns.
The incentive fee structure we have with Stellus Capital Management may create incentives that are not fully aligned with the interests of our stockholders.
We will be subject to corporate-level income tax and may default under our revolving credit facility with various lenders (the Credit Facility) if we are unable to maintain our qualification as a RIC under Subchapter M of the Code.
Regulations governing our operation as a BDC affect our ability to and the way in which we raise additional capital and, as a BDC, the necessity of raising additional capital may expose us to risks, including the typical risks associated with leverage.

Because we finance our investments with borrowed money, the potential for gain or loss on amounts invested in us is magnified and may increase the risk of investing in us.

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Because we use debt to finance our investments, changes in interest rates will affect our cost of capital and net investment income.

Adverse developments in the credit markets may impair our ability to borrow money.

Most of our portfolio investments are recorded at fair value as determined in good faith by our board of directors and, as a result, there may be uncertainty as to the value of our portfolio investments.

Our ability to enter into transactions with our affiliates will be restricted, which may limit the scope of investments available to us.

The involvement of our interested directors in the valuation process may create conflicts of interest.

There are conflicts related to other arrangements with Stellus Capital Management.

If we fail to maintain our status as a BDC, our business and operating flexibility could be significantly reduced.

Because we have received Board approval, and have submitted a proposal to a stockholder vote at our 2018 Annual Meeting, we will be subject to 150% Asset Coverage beginning on April 4, 2019 or following our 2018 Annual Meeting if we receive stockholder approval. This approval will allow us to incur twice as much debt as we could have without such approval, potentially heightening the risks associated with leverage described above.

The effect of global climate change may impact the operations of our portfolio companies.

Existing stockholders may incur dilution if, in the future, we sell shares of our common stock in one or more offerings at prices below the then current net asset value per share of our common stock.

Conflicts of Interests

We may have conflicts of interest arising out of the investment advisory activities of Stellus Capital Management, including those described below.

Our investment strategy includes investments in secured debt (including first lien, second lien and unitranche) and mezzanine debt (including senior unsecured and subordinated debt), as well as related equity securities of private middle-market companies. Stellus Capital Management also manages, and in the future may manage, other investment funds, accounts or investment vehicles that invest or may invest in assets eligible for purchase by us. For example, Stellus Capital Management currently manages private credit funds that have an investment strategy that is identical to our investment strategy. Stellus Capital Management also provides non-discretionary advisory services to the D. E. Shaw group, pursuant to sub-advisory arrangements, with respect to a private investment fund and a strategy of a private multi-strategy investment fund (collectively with the D. E. Shaw group fund, the D. E. Shaw group funds) to which the D. E. Shaw group serves as investment adviser that have an investment strategy similar to our investment strategy. Our investment policies, fee arrangements and other circumstances may vary from those of other investment funds, accounts or investment vehicles managed by Stellus Capital Management.

We have received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management (other than the D. E. Shaw group funds), where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). Under the terms of the relief permitting us to co-invest with other funds managed by Stellus Capital Management, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is consistent with our investment objectives and strategies. We intend to co-invest, subject to the conditions included in the exemptive order we received from the SEC, with the private credit funds managed by Stellus Capital

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Management that have an investment strategy that is identical to our investment strategy. We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification.

In the course of our investing activities, we pay management and incentive fees to Stellus Capital Management. We have entered into an investment advisory agreement with Stellus Capital Management that provides that these fees are based on the value of our gross assets. Because these fees are based on the value of our gross assets, Stellus Capital Management will benefit when we incur debt or use leverage. This fee structure may encourage Stellus Capital Management to cause us to borrow money to finance additional investments. Our board of directors is charged with protecting our interests by monitoring how Stellus Capital Management addresses these and other conflicts of interests associated with its management services and compensation. While our board of directors is not expected to review or approve each investment decision, borrowing or incurrence of leverage, our independent directors will periodically review Stellus Capital Management s services and fees as well as its portfolio management decisions and portfolio performance. See Risk Factors The incentive fee structure we have with Stellus Capital Management may create incentives that are not fully aligned with the interests of our stockholders.

Stellus Capital Management may from time to time incur expenses in connection with investments to be made on our behalf and on behalf of other investment funds, accounts and investment vehicles managed by Stellus Capital Management. Stellus Capital Management will allocate such expenses on a pro rata basis according to the participation in a transaction, subject to oversight by our board of directors.

Corporate Information

Our principal executive offices are located at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, and our telephone number is (713) 292-5400. We maintain a website located at *www.stelluscapital.com* (under the Public Investors section). Information on our website is not incorporated into or a part of this prospectus or any accompanying prospectus supplement and you should not consider information on our website to be part of this prospectus or any accompanying prospectus.

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THE OFFERING

We may offer, from time to time, up to $200,000,000 of our securities, on terms to be determined at the time of the offering. Our securities may be offered at prices and on terms to be disclosed in one or more prospectus supplements.

Our securities may be offered directly to one or more purchasers by us or through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will disclose the terms of the offering, including the name or names of any agents or underwriters involved in the sale of our securities by us, the purchase price, and any fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See Plan of Distribution. We may not sell any of our securities directly or through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of our securities.

Set forth below is additional information regarding the offering of our securities:

Use of Proceeds

We plan to use the net proceeds of this offering to make new investments in portfolio companies in accordance with our investment objective and strategies as described in this prospectus and for general working capital purposes. We may also use a portion of the net proceeds to reduce any of our outstanding borrowings. Pending such use, we will invest the net proceeds primarily in high quality, short-term debt securities consistent with our BDC election and our election to be taxed as a RIC. See Use of Proceeds.

Investment Advisory Agreement

We will pay Stellus Capital Management a fee for its services under the investment advisory agreement. This fee consists of two components: a base management fee and an incentive fee. The base management fee is calculated at an annual rate of 1.75% of our gross assets, including assets purchased with borrowed funds or other forms of leverage (including preferred stock, public and private debt issuances, derivative instruments, repurchase agreements and other similar instruments or arrangements) and excluding cash and cash equivalents. The base management fee will be payable quarterly in arrears.

The incentive fee, which provides Stellus Capital Management with a share of the income that it generates for us, consists of two parts. The first part, which is calculated and payable quarterly in arrears, equals 20.0% of our pre-incentive fee net investment income for the immediately preceding quarter, subject to a hurdle rate of 2.0% per quarter for the benefit of Stellus Capital Management, and is subject to a catch-up feature for the benefit of Stellus Capital Management. The second part is calculated and payable in arrears as of the end of each calendar year (or, upon termination of the investment advisory agreement, as of the termination date) and equals 20.0% of our aggregate cumulative realized capital gains from inception through the end of each calendar year, computed net of aggregate cumulative realized capital losses and aggregate cumulative unrealized capital depreciation through the end of such year, less the aggregate amount of any previously paid capital gain incentive fees. See Management Agreements Management Fee and Incentive Fee.

Pre-incentive fee net investment income means interest income, dividend income and any other income (including any other fees, such as commitment, origination, structuring, diligence, managerial assistance and consulting fees or other fees that we receive from portfolio companies) accrued during the calendar quarter, minus our operating expenses for the quarter (including the base management fee, expenses payable under our administration agreement, and any interest expense and any distributions paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incentive fee net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount, or OID, debt instruments with PIK interest and zero coupon securities), accrued income that we have not yet received in cash. However, the portion of such incentive fee that is attributable to deferred interest (such as PIK interest or OID) will be paid to Stellus Capital Management, together with interest thereon from the date of deferral to the date of payment, only if and to the extent we actually receive such interest in cash, and any accrual thereof will be reversed if and to the extent such interest is reversed in connection with any write-off or similar treatment of the investment giving rise to any deferred interest accrual. Stellus Capital Management has agreed to permanently waive any interest accrued on the portion of the incentive fee attributable to deferred interest (such as PIK interest or OID).

New York Stock Exchange symbol

SCM (common stock)
SCA (5.75% notes due 2022)

Trading at a discount

Shares of closed-end investment companies, including business development companies, frequently trade in the secondary market at a discount to their net asset values. The risk that our shares may trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline. We cannot predict whether our shares will trade above, at or below net asset value. See Risk Factors Shares of closed-end investment companies, including business development companies, frequently trade at a discount from their net asset value.

Leverage

We expect to continue to use leverage to make investments. As a result, we may continue to be exposed to the risks of leverage, which include that leverage may be considered a speculative investment technique. The use of leverage magnifies the potential for gain and loss on amounts we invest and therefore, indirectly, increases the risks associated with investing in shares of our common stock. See Risk Factors.

Our current borrowings include:

our 2022 Notes, of which $48.9 million were outstanding as of March 31, 2018;

our Credit Facility, of which $118.3 million was outstanding as of March 31, 2018; and our SBA-Guaranteed debentures, of which $90.0 million were outstanding as of March 31, 2018.

Distributions

We generally intend to pay monthly distributions to our stockholders out of assets legally available for distribution. Our monthly distributions, if any, will be determined by our board of directors.

Taxation

We have elected to be treated for U.S. federal income tax purposes as a RIC. As a RIC, we generally will not have to pay corporate-level U.S. federal income taxes on any net ordinary income or capital gains that we distribute to our stockholders as dividends. To maintain our qualification as a RIC and the associated tax benefits, we must meet specified source-of-income and asset diversification requirements and distribute annually at least 90% of our net ordinary income and net short-term capital gains, if any, in excess of our net long-term capital losses. See Distributions.

Dividend reinvestment plan

We have adopted a dividend reinvestment plan for our stockholders, which is an opt out dividend reinvestment plan. Under this plan, if we declare a cash distribution to our stockholders, the amount of such distribution will be automatically reinvested in additional shares of our common stock unless a stockholder specifically opts out of our dividend reinvestment plan. If a stockholder opts out, that stockholder will receive cash distributions. Stockholders who receive distributions in the form of shares of common stock generally will be subject to the same U.S. federal, state and local tax consequences as stockholders who elect to receive their distributions in cash, but will not receive any corresponding cash distributions with which to pay any applicable taxes. See Dividend Reinvestment Plan.

Administration Agreement

The administration agreement requires us to reimburse Stellus Capital Management for our allocable portion (subject to the review of our board of directors) of overhead and other expenses, including furnishing us with office facilities and equipment and providing clerical, bookkeeping, record keeping and other administrative services at such facilities, and our allocable portion of the cost of our chief financial officer and chief compliance officer and their respective staffs. To the extent that Stellus Capital Management outsources any of its functions, we will pay the fees associated with such functions on a direct basis, without incremental profit to Stellus Capital Management. See Management Agreements Administration Agreement.

License arrangements

We have entered into a license agreement with Stellus Capital Management under which Stellus Capital Management has granted us a non-exclusive, royalty-free license to use the name Stellus Capital. For a description of the license agreement, see Management Agreements License Agreement.

Custodian and transfer agent

ZB, N.A., dba Amegy Bank, serves as our custodian and our transfer and distribution paying agent and registrar. See Custodian, Transfer and Dividend Paying Agent and Registrar.

Anti-takeover provisions

Our charter and bylaws, as well as certain statutory and regulatory requirements, contain certain provisions that may have the effect of discouraging a third party from making an acquisition proposal for us. These anti-takeover provisions may inhibit a change in control in circumstances that could give the holders of our common stock the opportunity to realize a premium over the market price for our common stock. See Description of Capital Stock.

Available information

We are required to file periodic reports, proxy statements and other information with the SEC. This information is available at the SEC s public reference room at 100 F. Street, N.E., Washington, D.C. 20549 and on the SEC s website at *http://www.sec.gov*. Information on the operation of the SEC s public reference room may be obtained by calling the SEC at 1-800-SEC-0330.

We maintain a website at *www.stelluscapital.com* (under the Public Investors section) and make all of our annual, quarterly and current reports, proxy statements and other information available, free of charge, on or through our website. Information on our website is not incorporated into or part of this prospectus or any prospectus supplement and should not be relied upon as such. You may also obtain such information free of charge by contacting us in writing at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, Attention: Investor Relations.

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FEES AND EXPENSES

The following table is intended to assist you in understanding the costs and expenses that an investor in our common stock will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. Moreover, the information set forth below does not include any transaction costs and expenses that investors will incur in connection with each offering of our securities pursuant to this prospectus. As a result, investors are urged to read the "Fees and Expenses" table contained in any corresponding prospectus supplement to fully understand the actual transaction costs and expenses they will incur in connection with each such offering. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "us" or that "we" will pay fees or expenses, common stockholders will indirectly bear such fees or expenses.

Stockholder Transaction Expenses:		
Sales load (as a percentage of offering price)		%(1)
Offering expenses (as a percentage of offering price)		%(2)
Dividend reinvestment plan expenses		(3)
Total Stockholder Transaction Expenses (as a percentage of offering price)		%(4)
Annual Expenses (as percentage of net assets attributable to common stock):		
Base management fees	3.15	%(5)
Incentive fees payable under the investment advisory agreement	1.74	%(6)
Interest payments on borrowed funds	5.46	%(7)
Other expenses	2.78	%(8)
Total annual expenses	13.13	%

(1) In the event that our securities are sold to or through underwriters, a corresponding prospectus supplement will disclose the applicable sales load.

(2) In the event that we conduct an offering of our securities, a corresponding prospectus supplement will disclose the estimated offering expenses. Our common stockholders will bear, directly or indirectly, the expenses of any offering of our securities, including debt securities.

(3) The expenses of the dividend reinvestment plan are included in "Other expenses." See "Dividend Reinvestment Plan."

(4) Total stockholder transaction expenses may include sales load and will be disclosed in a future prospectus supplement, if any.

(5) Our base management fee, payable quarterly in arrears, is 1.75% of our gross assets, including assets purchased with borrowed amounts or other forms of leverage (including traditional and effective leverage such as preferred stock, public and private debt issuances, derivative instruments, repurchase agreements and other similar instruments or arrangements) and excluding cash and cash equivalents and is based on the base management fee incurred for the three months ended March 31, 2018 annualized for a full year.

(6) This item represents the incentive fee payable to Stellus Capital Management based on the actual amounts earned on our "pre-incentive fee net investment income" for the three months ended March 31, 2018 annualized for a full year.

The incentive fee consists of two components, ordinary income and capital gains:

The ordinary income component, which is payable quarterly in arrears, equals 20.0% of the excess, if any, of our "pre-incentive fee net investment income" over a 2.0% quarterly hurdle rate, expressed as a rate of return on the value of our net assets attributable to our common stock, and a "catch-up" provision, measured as of the end of each calendar quarter. Under this provision, in any calendar quarter, our investment adviser receives no incentive fee until our net investment income equals the hurdle rate of 2.0% but then receives, as a "catch-up," 100% of our pre-incentive fee net investment income with respect to that portion of such pre-incentive fee net investment income, if any, that exceeds the hurdle rate but is less than 2.5% subject to a total return requirement and deferral of non-cash amounts. The effect of the catch-up provision is that, subject to the total return and deferral provisions discussed below, if pre-incentive fee net investment income exceeds 2.5% in any calendar quarter, Stellus Capital

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Management will receive 20.0% of our pre-incentive fee net investment income as if a hurdle rate did not apply. The ordinary income component of the incentive fee is computed on income that may include interest that is accrued but not yet received in cash. The foregoing ordinary income component of the incentive fee is subject to a total return requirement, which provides that no incentive fee in respect of the Company s pre-incentive fee net investment income is payable except to the extent 20.0% of the cumulative net increase in net assets resulting from operations (as defined below) over the then current and 11 preceding calendar quarters exceeds the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. In other words, any ordinary income incentive fee that is payable in a calendar quarter will be limited to the lesser of (i) 20.0% of the amount by which our pre-incentive fee net investment income for such calendar quarter exceeds the 2.0% hurdle, subject to the catch-up provision, and (ii) (x) 20.0% of the cumulative net increase in net assets resulting from operations for the then current and 11 preceding calendar quarters *minus* (y) the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters.

For the foregoing purpose, the cumulative net increase in net assets resulting from operations is the sum of pre-incentive fee net investment income, realized gains and losses and unrealized appreciation and depreciation of the Company for the then current and 11 preceding calendar quarters. In addition, the portion of such incentive fee that is attributable to deferred interest (sometimes referred to as payment-in-kind interest, or PIK, or original issue discount, or OID) will be paid to Stellus Capital Management, together with interest thereon from the date of deferral to the date of payment, only if and to the extent we actually receive such interest in cash, and any accrual thereof will be reversed if and to the extent such interest is reversed in connection with any write-off or similar treatment of the investment giving rise to any deferred interest accrual. Any reversal of such accounts would reduce net income for the quarter by the net amount of the reversal (after taking into account the reversal of incentive fees payable) and would result in a reduction and possibly elimination of the incentive fees for such quarter. There is no accumulation of amounts on the hurdle rate from quarter to quarter, and accordingly, there is no clawback of amounts previously paid if subsequent quarters are below the quarterly hurdle, and there is no delay of payment if prior quarters are below the quarterly hurdle.

The capital gains component of the incentive fee equals 20.0% of our Incentive Fee Capital Gains, if any, which equals our aggregate cumulative realized capital gains from inception through the end of each calendar year, computed net of our aggregate cumulative realized capital losses and our aggregate cumulative unrealized capital depreciation, less the aggregate amount of any previously paid capital gain incentive fees. The second component of the incentive fee is payable, in arrears, at the end of each calendar year (or upon termination of the investment advisory agreement, as of the termination date). We will record an expense accrual relating to the capital gains component of the incentive fee payable by us to Stellus Capital Management when the unrealized gains on our investments exceed all realized capital losses on our investments given the fact that a capital gains incentive fee would be owed to Stellus Capital Management if we were to liquidate our investment portfolio at such time. The actual incentive fee payable to our investment adviser related to capital gains is determined and payable in arrears at the end of each fiscal year and includes only realized capital gains for the period. See Management Agreements Management Fee and Incentive Fee.

(7) Interest payments on borrowed funds represent our estimated annual interest payments based on the effective interest rate of borrowings under our Credit Facility, the SBA-guaranteed debentures and the 2022 Notes as of March 31, 2018, and assuming that we increase our borrowings to the following levels over the next twelve months: $150.0 million outstanding under the Credit Facility, $117.0 million of Notes outstanding and $150.0 million in SBA-guranteed debentures. Interest expense is calculated based upon the amounts outstanding on our Credit Facility bearing interest at a weighted average interest rate of 4.4%, amounts outstanding on our notes payable at an interest rate of 5.75% and our SBA-guaranteed debentures bearing interest at a weighted average interest rate of 2.9%, each as of March 31, 2018. Non-use commitment fees of 0.50% related to our Credit Facility is based upon unused commitments as of March 31, 2018. The amount of leverage that we employ, and our interest

expenses on such leverage, at any particular time will depend on, among other things, our board of directors assessment of market and other factors at the time of any proposed borrowing.

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(8) Includes our overhead expenses, including payments under the administration agreement based on our allocable portion of overhead and other expenses incurred by Stellus Capital Management. See Management Agreements Administration Agreement.

Example

The following example demonstrates the projected dollar amount of total cumulative expenses over various periods with respect to a hypothetical investment in us. In calculating the following expense amounts, we have assumed that our annual operating expenses would remain at the levels set forth in the table above. The examples assume no sales load. In the event that shares to which this prospectus relates are sold to or through underwriters, a corresponding prospectus supplement will restate this example to reflect the applicable sales load.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return (none of which is subject to a capital gains incentive fee)	$ 110	$ 310	$ 485	$ 833

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. The incentive fee under the investment management agreement, which, assuming a 5% annual return, would either not be payable or would have a de minimis effect, is not included in the example. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our expenses, and returns to our investors, would be higher. For example, if we assumed that we received our 5.0% annual return completely in the form of net realized capital gains on our investments, which results in a capital gains incentive fee earned, the projected dollar amount of total cumulative expenses set forth in the above illustration and the capital gains incentive fee would be as follows:

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return (all of which is subject to capital gains incentive fee)	$ 126	$ 348	$ 536	$ 887

While the examples assume reinvestment of all distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the distribution payable to a participant by (a) 95% of the market price per share of our common stock at the close of trading on the payment date fixed by our board of directors or (b) the average purchase price of all shares of common stock purchased by the administrator of the dividend reinvestment plan in the event shares are purchased in the open market to satisfy the share requirements of the dividend reinvestment plan, which may be at, above or below net asset value.

This example and the expenses in the table above should not be considered a representation of our future expenses, and actual expenses (including the cost of debt, if any, and other expenses) may be greater or less than those shown.

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SELECTED FINANCIAL DATA

The following selected financial data for the years ended December 31, 2017, 2016, 2015, 2014 and 2013 was derived from our financial statements which have been audited by Grant Thornton, LLP, our independent registered public accounting firm and the selected financial data for the three months ended March 31, 2018 and 2017 is derived from our unaudited financial statements but, in the opinion of management, reflect all adjustments (consisting only of normal recurring adjustments) that are necessary to present fairly the financial condition and operating results for such interim periods. Interim results as of and for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018. The data should be read in conjunction with our financial statements and related notes thereto and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere in this prospectus.

Statement of Operations Data:	For the three months ended March 31, 2018	For the three months ended March 31, 2017	For the year ended December 31, 2017	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014	For the year ended December 31, 2013
Total investment income	$10,911,783	$9,863,980	$39,648,193	$39,490,197	$35,158,559	$32,324,847	$29,400,736
Total expenses, net of fee waiver	$6,436,402	$5,720,353	$21,677,433	$22,177,996	$18,611,431	$15,812,750	$13,389,007
Net investment income	$4,475,379	$4,143,627	$17,970,760	$17,312,201	$16,547,128	$16,512,097	$16,011,729
Net increase in net assets resulting from operations	$7,343,929	$6,024,752	$22,613,257	$23,199,062	$7,670,536	$10,179,142	$17,544,997
Per Share Data:							
Net asset value	$13.93	$13.84	$13.81	$13.69	$13.19	$13.94	$14.54
Net investment income	$0.28	$0.33	$1.21	$1.39	$1.33	$1.34	$1.33
Net increase in net assets resulting from operations	$0.46	$0.48	$1.52	$1.86	$0.61	$0.83	$1.45
Distributions declared	$0.34	$0.34	$1.36	$1.36	$1.36	$1.43	$1.33

(1) Computed using the effective interest rates for all of our debt investments, including accretion of original issue discount.

(2) ASU No. 2015-03 Simplifying the Presentation of Debt Issuance Costs was effective for the quarter ended March 31, 2016. Total assets and total liabilities for the periods prior to the effective date have been modified from their respective filings to conform to this presentation.

(3) The weighted average yield of our debt investments is not the same as a return on investment for our stockholders but, rather, relates to a portion of our investment portfolio and is calculated before the payment of all of our

subsidiaries fees and expenses. The weighted average yield was computed using the effective interest rates for all of our debt investment restated as an interest rate payable annually in arrears and is computed including cash and payment in kind, or PIK interest, as well as accretion of original issue discount.

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RISK FACTORS

Investing in our securities involves a number of significant risks. Before you invest in our securities, you should be aware of various risks, including those described below. You should carefully consider these risk factors, together with all of the other information included in this prospectus and any accompanying prospectus supplement, before you decide whether to make an investment in our securities. Because we are a BDC, there may be special risks associated with investing in our securities, including risks associated with investing in a portfolio of small and developing or financially troubled businesses. The risks below include risks associated with investments in the Company specifically, as well as risks generally associated with investment in a company with investment objectives, investment policies, capital structure, or trading markets similar to the Company s. The risks set out below are not the only risks we face. Additional risks and uncertainties not presently known to us or not presently deemed material by us may also impair our operations and performance. If any of the following events occur, our business, financial condition, results of operations and cash flows could be materially and adversely affected. In such case, our net asset value and the trading price of our securities could decline, and you may lose all or part of your investment.

Risks Relating to our Business and Structure

We are dependent upon key personnel of Stellus Capital Management for our future success. If Stellus Capital Management were to lose any of its key personnel, our ability to achieve our investment objective could be significantly harmed.

We depend on the diligence, skill and network of business contacts of the investment professionals of Stellus Capital Management to achieve our investment objective. Stellus Capital Management s team of investment professionals evaluates, negotiates, structures, closes and monitors our investments in accordance with the terms of our investment advisory agreement. We can offer no assurance, however, that Stellus Capital Management s investment professionals will continue to provide investment advice to us.

Stellus Capital Management s investment committee, which provides oversight over our investment activities, is provided to us by Stellus Capital Management under the investment advisory agreement. Stellus Capital Management s investment committee consists of five members, including Messrs. Ladd, D Angelo and Davis, each a member of our board of directors, Mr. Huskinson, our chief financial officer and chief compliance officer and the chief financial officer of Stellus Capital Management, and Mr. Overbergen, an investment professional of Stellus Capital Management. The loss of any member of Stellus Capital Management s investment committee may limit our ability to achieve our investment objective and operate our business. This could have a material adverse effect on our financial condition, results of operations and cash flows.

Our business model depends to a significant extent upon strong referral relationships. Any inability of Stellus Capital Management to maintain or develop these relationships, or the failure of these relationships to generate investment opportunities, could adversely affect our business.

We depend upon Stellus Capital Management to maintain its relationships with private equity sponsors, placement agents, investment banks, management groups and other financial institutions, and we rely to a significant extent upon these relationships to provide us with potential investment opportunities. If Stellus Capital Management fails to maintain such relationships, or to develop new relationships with other sources of investment opportunities, we will not be able to grow our investment portfolio. In addition, individuals with whom Stellus Capital Management has relationships are not obligated to provide us with investment opportunities, and we can offer no assurance that these relationships will generate investment opportunities for us in the future.

Our financial condition, results of operations and cash flows will depend on our ability to manage our business effectively.

Our ability to achieve our investment objective will depend on our ability to manage our business and to grow our investments and earnings. This will depend, in turn, on Stellus Capital Management s ability to identify, invest in and monitor portfolio companies that meet our investment criteria. The achievement of our investment objective on a cost-effective basis will depend upon Stellus Capital Management s execution of our

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investment process, its ability to provide competent, attentive and efficient services to us and, to a lesser extent, our access to financing on acceptable terms. Stellus Capital Management s investment professionals will have substantial responsibilities in connection with the management of other investment funds, accounts and investment vehicles. The personnel of Stellus Capital Management may be called upon to provide managerial assistance to our portfolio companies. These activities may distract them from sourcing new investment opportunities for us or slow our rate of investment. Any failure to manage our business and our future growth effectively could have a material adverse effect on our business, financial condition, results of operations and cash flows.

There are significant potential conflicts of interest that could negatively affect our investment returns.

The members of Stellus Capital Management s investment committee serve, or may serve, as officers, directors, members, or principals of entities that operate in the same or a related line of business as we do, or of investment funds, accounts, or investment vehicles managed by Stellus Capital Management. Similarly, Stellus Capital Management may have other clients with similar, different or competing investment objectives. In serving in these multiple capacities, they may have obligations to other clients or investors in those entities, the fulfillment of which may not be in the best interests of us or our stockholders. For example, Stellus Capital Management currently manages private credit funds that have an investment strategy that is identical to our investment strategy, and with which we intend to co-invest. Stellus Capital Management also provides sub-advisory services to the D. E. Shaw group with respect to a private investment fund and a strategy of a private multi-strategy investment fund to which the D. E. Shaw group serves as investment adviser that have an investment strategy similar to our investment strategy.

In addition, there may be times when Stellus Capital Management, members of its investment committee or its other investment professionals have interests that differ from those of our stockholders, giving rise to a conflict of interest. In particular, private investment funds for which Stellus Capital Management provides investment advisory services hold minority equity interests in certain of the portfolio companies in which we hold debt investments. As a result, Stellus Capital Management, members of its investment committee or its other investment professionals may face conflicts of interest in connection with making business decisions for these portfolio companies to the extent that such decisions affect the debt and equity holders in these portfolio companies differently. In addition, Stellus Capital Management may face conflicts of interests in connection with making investment or other decisions, including granting loan waivers or concessions, on our behalf with respect to these portfolio companies given that they also provide investment advisory services to a private investment fund that holds the equity interests in these portfolio companies. Although our investment adviser will endeavor to handle these investment and other decisions in a fair and equitable manner, we and the holders of the shares of our common stock could be adversely affected by these decisions. Moreover, given the subjective nature of the investment and other decisions made by our investment adviser on our behalf, we are unable to monitor these potential conflicts of interest between us and our investment adviser; however, our board of directors, including the independent directors, reviews conflicts of interest in connection with its review of the performance of our investment adviser.

The senior investment professionals and other investment team members of Stellus Capital Management may, from time to time, possess material non-public information, limiting our investment discretion.

The senior investment professionals and other investment team members of Stellus Capital Management, including members of Stellus Capital Management s investment committee, may serve as directors of, or in a similar capacity with, portfolio companies in which we invest, the securities of which are purchased or sold on our behalf. In the event that material nonpublic information is obtained with respect to such companies, or we become subject to trading restrictions under the internal trading policies of those companies or as a result of applicable law or regulations, we could be prohibited for a period of time from purchasing or selling the securities of such companies, and this prohibition may have an adverse effect on us.

Our management and incentive fees may induce Stellus Capital Management to incur additional leverage.

Generally, the management and incentive fees payable by us to Stellus Capital Management may create an incentive for Stellus Capital Management to use the additional available leverage if this proposal is approved. For example, the fact that the base management fee that we pay to Stellus Capital Management is

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payable based upon our gross assets (which includes any borrowings for investment purposes) may encourage Stellus Capital Management to use leverage to make additional investments. Such a practice could result in our investing in more speculative securities than would otherwise be the case, which could result in higher investment losses, particularly during cyclical economic downturns. Under certain circumstances, the use of additional leverage may increase the likelihood of our default on our borrowings, which would disfavor holders of our common stock.

In addition, because the incentive fee on net investment income is calculated as a percentage of our net assets subject to a hurdle, having additional leverage available may encourage Stellus Capital Management to use leverage to increase the leveraged return on our investment portfolio. To the extent additional leverage is available at favorable rates, Stellus Capital Management could use leverage to increase the size of our investment portfolio to generate additional income, which may make it easier to meet the incentive fee hurdle. Our adoption of the reduced minimum asset coverage will allow us to incur additional leverage above the previous 1940 Act limitations. As a result, the incentives for Stellus Capital Management to cause us to use additional leverage may be greater.

Our board of directors is charged with protecting our interests by monitoring how Stellus Capital Management addresses these and other conflicts of interests associated with its management services and compensation. While our board of directors is not expected to review or approve each investment decision, borrowing or incurrence of leverage, our independent directors will periodically review Stellus Capital Management s services and fees as well as its portfolio management decisions and portfolio performance. In connection with these reviews, our independent directors will consider whether our fees and expenses (including those related to leverage) remain appropriate.

Our incentive fee may induce Stellus Capital Management to make speculative investments.

We pay Stellus Capital Management an incentive fee based, in part, upon net capital gains realized on our investments. Unlike that portion of the incentive fee based on income, there is no hurdle rate applicable to the portion of the incentive fee based on net capital gains. Additionally, under the incentive fee structure, Stellus Capital Management may benefit when capital gains are recognized and, because Stellus Capital Management will determine when to sell a holding, Stellus Capital Management will control the timing of the recognition of such capital gains. As a result, Stellus Capital Management may have a tendency to invest more capital in investments that are likely to result in capital gains as compared to income producing securities. Such a practice could result in our investing in more speculative securities than would otherwise be the case, which could result in higher investment losses, particularly during economic downturns.

We may be obligated to pay Stellus Capital Management incentive compensation even if we incur a loss and may pay more than 20.0% of our net capital gains because we cannot recover payments made in previous years.

Stellus Capital Management is entitled to incentive compensation for each fiscal quarter in an amount equal to a percentage of the excess of our investment income for that quarter (before deducting incentive compensation) above a threshold return for that quarter and subject to a total return requirement. The general effect of this total return requirement is to prevent payment of the foregoing incentive compensation except to the extent 20.0% of the cumulative net increase in net assets resulting from operations over the then current and 11 preceding calendar quarters exceeds the cumulative incentive fees accrued and/or paid for the 11 preceding calendar quarters. Consequently, we may pay an incentive fee if we incurred losses more than three years prior to the current calendar quarter even if such losses have not yet been recovered in full. Thus, we may be required to pay Stellus Capital

Management incentive compensation for a fiscal quarter even if there is a decline in the value of our portfolio or we incur a net loss for that quarter. If we pay an incentive fee of 20.0% of our realized capital gains (net of all realized capital losses and unrealized capital depreciation on a cumulative basis) and thereafter experience additional realized capital losses or unrealized capital depreciation, we will not be able to recover any portion of the incentive fee previously paid.

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We operate in a highly competitive market for investment opportunities, which could reduce returns and result in losses.

A number of entities compete with us to make the types of investments that we make. We compete with public and private funds, commercial and investment banks, commercial financing companies and, to the extent they provide an alternative form of financing, private equity and hedge funds. Many of our competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, we believe some of our competitors may have access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC or the source-of-income, asset diversification and distribution requirements we must satisfy to maintain our RIC qualification. The competitive pressures we face may have a material adverse effect on our business, financial condition, results of operations and cash flows. As a result of this competition, we may not be able to take advantage of attractive investment opportunities from time to time, and we may not be able to identify and make investments that are consistent with our investment objective.

With respect to the investments we make, we do not seek to compete based primarily on the interest rates we offer, and we believe that some of our competitors may make loans with interest rates that are lower than the rates we offer. With respect to all investments, we may lose some investment opportunities if we do not match our competitors pricing, terms and structure. However, if we match our competitors pricing, terms and structure, we may experience decreased net interest income, lower yields and increased risk of credit loss. We may also compete for investment opportunities with investment funds, accounts and investment vehicles managed by Stellus Capital Management. Although Stellus Capital Management will allocate opportunities in accordance with its policies and procedures, allocations to such investment funds, accounts and investment vehicles will reduce the amount and frequency of opportunities available to us and may not be in the best interests of us and our stockholders.

We will be subject to corporate-level income tax and may default under our revolving credit facility if we are unable to maintain our tax treatment as a RIC under Subchapter M of the Code.

To maintain our tax treatment as a RIC under Subchapter M of the Code, we must meet certain source-of-income, asset diversification and distribution requirements. The distribution requirement for a RIC is satisfied if we distribute at least 90% of our net ordinary income and net short-term capital gains in excess of net long-term capital losses, if any, to our stockholders on an annual basis. Because we incur debt, we will be subject to certain asset coverage ratio requirements under the 1940 Act and financial covenants under loan and credit agreements that could, under certain circumstances, restrict us from making distributions necessary to maintain our tax treatment as a RIC. If we are unable to obtain cash from other sources, we may fail to maintain our tax treatment as a RIC and, thus, may be subject to corporate-level income tax. To maintain our tax treatment as a RIC, we must also meet certain asset diversification requirements at the end of each calendar quarter. Failure to meet these tests may result in our having to dispose of certain investments quickly in order to prevent the loss of our tax treatment as a RIC. Because most of our investments are in private or thinly-traded public companies, any such dispositions may be made at disadvantageous prices and may result in substantial losses. No certainty can be provided, that we will satisfy the asset diversification requirements or the other requirements necessary to maintain our qualification and tax treatment as a RIC. If we fail to maintain our tax treatment as a RIC for any reason and become subject to corporate income tax, the resulting corporate income taxes could substantially reduce our net assets, the amount of income available for distributions to our stockholders and the amount of funds available for new investments. Furthermore, if we fail to maintain our tax treatment as a RIC, we may be in default under the terms of the Credit Facility. Such a failure could have a material adverse effect on us and our stockholders.

We may have difficulty paying our required distributions if we recognize income before, or without, receiving cash representing such income.

For U.S. federal income tax purposes, we include in income certain amounts that we have not yet received in cash, such as the accrual of original issue discount. This may arise if we receive warrants in connection with the making of a loan and in other circumstances, or through contracted PIK interest, which

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represents contractual interest added to the loan balance and due at the end of the loan term. Such original issue discount, which could be significant relative to our overall investment activities, and increases in loan balances as a result of contracted PIK arrangements are included in income before we receive any corresponding cash payments. We also may be required to include in income certain other amounts that we will not receive in cash.

Since in certain cases we may recognize income before or without receiving cash representing such income, we may have difficulty meeting the requirement to distribute at least 90% of our net ordinary income and net short-term capital gains in excess of net long-term capital losses, if any, to maintain our tax treatment as a RIC. In such a case, we may have to sell some of our investments at times we would not consider advantageous or raise additional debt or equity capital or reduce new investment originations to meet these distribution requirements. If we are not able to obtain such cash from other sources, we may fail to maintain our tax treatment as a RIC and thus be subject to corporate-level income tax. See Material U.S. Federal Income Tax Considerations Taxation as a RIC.

PIK interest payments we receive will increase our assets under management and, as a result, will increase the amount of base management fees and incentive fees payable by us to Stellus Capital Management.

Certain of our debt investments may contain provisions providing for the payment of PIK interest. Because PIK interest results in an increase in the size of the loan balance of the underlying loan, the receipt by us of PIK interest will have the effect of increasing our assets under management. As a result, because the base management fee that we pay to Stellus Capital Management is based on the value of our gross assets, the receipt by us of PIK interest will result in an increase in the amount of the base management fee payable by us. In addition, any such increase in a loan balance due to the receipt of PIK interest will cause such loan to accrue interest on the higher loan balance, which will result in an increase in our pre-incentive fee net investment income and, as a result, an increase in incentive fees that are payable by us to Stellus Capital Management.

Regulations governing our operation as a BDC affect our ability to, and the way in which we, raise additional capital. As a BDC, the necessity of raising additional capital may expose us to risks, including the typical risks associated with leverage.

We may issue debt securities or preferred stock and/or borrow money from banks or other financial institutions, which we refer to collectively as senior securities, up to the maximum amount permitted by the 1940 Act. Under the provisions of the 1940 Act, we are permitted as a BDC to issue senior securities in amounts such that our asset coverage ratio, as defined in the 1940 Act, equals at least 200% (or 150% if certain requirements are met) of our gross assets less all liabilities and indebtedness not represented by senior securities, after each issuance of senior securities. If the value of our assets declines, we may be unable to satisfy this test. If that happens, we would not be able to borrow additional funds until we were able to comply with the asset coverage ratio under the 1940 Act. Also, any amounts that we use to service our indebtedness would not be available for distributions to our common stockholders. If we issue senior securities, we will be exposed to typical risks associated with leverage, including an increased risk of loss.

We are not generally able to issue and sell our common stock at a price below net asset value per share. We may, however, sell our common stock, or warrants, options or rights to acquire our common stock, at a price below then-current net asset value per share of our common stock if our board of directors determines that such sale is in our best interests, and if our stockholders approve such sale. At our 2017 Annual Meeting of Stockholders, our stockholders voted to allow us to issue common stock at a price below net asset value per share for the period ending on the earlier of the one-year anniversary of the date of the Company s 2017 Annual Meeting of Stockholders and the date of the Company s 2018 Annual Meeting of Stockholders. Our stockholders did not specify a maximum discount below net asset value at which we are able to issue our common stock, although the number of shares sold in each offering may not exceed 25% of our outstanding common stock immediately prior to such sale. We are seeking similar approval at our 2018 Annual Meeting of Stockholders scheduled for June 28, 2018. We cannot issue shares of our common stock below net asset value unless our board of directors determines that it would be in our and our stockholders best interests to do so. Sales of common stock at prices below net asset value per share dilute the interests of existing stockholders, have the effect of reducing our net asset value per share and may reduce our market price per share. In

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addition, continuous sales of common stock below net asset value may have a negative impact on total returns and could have a negative impact on the market price of our shares of common stock. If we raise additional funds by issuing common stock, then the percentage ownership of our stockholders at that time will decrease, and you may experience dilution.

Because we finance our investments with borrowed money, the potential for gain or loss on amounts invested in us is magnified and may increase the risk of investing in us.

The use of leverage magnifies the potential for gain or loss on amounts invested. The use of leverage is generally considered a speculative investment technique and increases the risks associated with investing in our securities. If we continue to use leverage to partially finance our investments through banks, insurance companies and other lenders, you will experience increased risks of investing in our common stock. Lenders of these funds have fixed dollar claims on our assets that are superior to the claims of our common stockholders, and we would expect such lenders to seek recovery against our assets in the event of a default. We, through our SBIC subsidiary, intend to issue debt securities guaranteed by the SBA and sold in the capital markets. Upon any such issuance of debt securities and as a result of its guarantee of the debt securities, if any, the SBA would also have fixed dollar claims on the assets of our SBIC subsidiary that are superior to the claims of our common stockholders.

Upon the issuance of any debt securities guaranteed by the SBA, if we are unable to meet the financial obligations under the 2022 Notes or the Credit Facility, the SBA, as a creditor, would have a superior claim to the assets of our SBIC subsidiary over our stockholders in the event we liquidate or the SBA exercises its remedies under such debentures as the result of a default by us.

In addition, under the terms of the Credit Facility and any borrowing facility or other debt instrument we may enter into, we are likely to be required to use the net proceeds of any investments that we sell to repay a portion of the amount borrowed under such facility or instrument before applying such net proceeds to any other uses. If the value of our assets decreases, leveraging would cause net asset value to decline more sharply than it otherwise would have had we not leveraged, thereby magnifying losses or eliminating our stake in a leveraged investment. Similarly, any decrease in our revenue or income will cause our net income to decline more sharply than it would have had we not borrowed. Such a decline would also negatively affect our ability to make distributions with respect to our common stock. Our ability to service any debt depends largely on our financial performance and is subject to prevailing economic conditions and competitive pressures. Moreover, as the base management fee payable to Stellus Capital Management is payable based on the value of our gross assets, including those assets acquired through the use of leverage, Stellus Capital Management will have a financial incentive to incur leverage, which may not be consistent with our stockholders   interests. In addition, our common stockholders bear the burden of any increase in our expenses as a result of our use of leverage, including interest expenses and any increase in the base management fee payable to Stellus Capital Management.

As a BDC, we generally are required to meet a coverage ratio of total assets to total borrowings and other senior securities, which include all of our borrowings and any preferred stock that we may issue in the future, of at least 200% (or 150% if certain requirements are met). If this ratio declines below the threshold applicable to us, we will not be able to incur additional debt until we are able to comply with the asset coverage ratio under the 1940 Act. This could have a material adverse effect on our operations, and we may not be able to make distributions. The amount of leverage that we employ will depend on Stellus Capital Management s and our board of directors   assessment of market and other factors at the time of any proposed borrowing. We cannot assure you that we will be able to obtain credit at all or on terms acceptable to us.

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Illustration. The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns, net of expenses. The calculations in the table below are hypothetical and actual results may be higher or lower than those appearing below.

Assumed Return on Our Portfolio(1) (net of expenses)

	-10.0%	-5.0%	0.0%	5.0%	10.0%
Corresponding net return to common stockholder	-26.1 %	-15.3 %	-4.5 %	6.3 %	17.1 %

(1) Assumes \$480.9 million in total assets, \$117.0 million in debt outstanding, \$222.2 million in net assets, and an average cost of funds of 4.0%. Actual interest payments may be different.

We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the 200% asset coverage ratio we are required to maintain under the 1940 Act. This relief allows us increased flexibility under the 200% asset coverage test by allowing us to borrow up to \$150.0 million more than we would otherwise be able to borrow absent the receipt of this exemptive relief, based on regulatory capital of \$75.0 million at March 31, 2018.

In addition, our debt facilities may impose financial and operating covenants that restrict our business activities, including limitations that hinder our ability to finance additional loans and investments or to make the distributions required to maintain our qualification as a RIC under the Code.

Substantially all of our assets are subject to security interests under the Credit Facility or claims of the SBA with respect to SBA-guaranteed debentures we may issue and, if we default on our obligations thereunder, we may suffer adverse consequences, including foreclosure on our assets.

As of March 31, 2018, substantially all of our assets were pledged as collateral under the Credit Facility or are subject to a superior claim over the holders of our common stock or the 2022 Notes by the SBA pursuant to the SBA-guaranteed debentures. If we default on our obligations under the Credit Facility or the SBA-guaranteed debentures the lenders and/or the SBA may have the right to foreclose upon and sell, or otherwise transfer, the collateral subject to their security interests or their superior claim. In such event, we may be forced to sell our investments to raise funds to repay our outstanding borrowings in order to avoid foreclosure and these forced sales may be at times and at prices we would not consider advantageous. Moreover, such deleveraging of our company could significantly impair our ability to effectively operate our business in the manner in which we have historically operated. As a result, we could be forced to curtail or cease new investment activities and lower or eliminate the dividends that we have historically paid to our stockholders.

In addition, if the lenders exercise their right to sell the assets pledged under the Credit Facility, such sales may be completed at distressed sale prices, thereby diminishing or potentially eliminating the amount of cash available to us after repayment of the amounts outstanding under the Credit Facility.

Because we use debt to finance our investments and may in the future issue senior securities including preferred stock and debt securities, if market interest rates were to increase, our cost of capital could increase, which could reduce our net investment income.

Because we borrow money to make investments and may in the future issue senior securities including preferred stock and debt securities, our net investment income will depend, in part, upon the difference between the rate at which we borrow funds and the rate at which we invest those funds. As a result, we can offer no assurance that a significant change in market interest rates would not have a material adverse effect on our net investment income in the event we use debt to finance our investments. In periods of rising interest rates, our cost of funds would increase, which could reduce our net investment income. We may use interest rate risk management techniques in an effort to limit our exposure to interest rate fluctuations. We may utilize instruments such as forward contracts, currency options and interest rate swaps, caps, collars and floors to seek to hedge against fluctuations in the relative values of our portfolio positions from changes in currency exchange rates and market interest rates to the extent permitted by the 1940 Act. For example, to the extent any such instruments were to constitute senior securities under the 1940 Act, we would have to and will

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comply with the asset coverage requirements thereunder or, as permitted in lieu thereof, place certain assets in a segregated account to cover such instruments in accordance with SEC guidance, including, for example, Investment Company Act Release No. IC-10666, as applicable. There is otherwise no limit as to our ability to enter into such derivative transactions. In addition, a rise in the general level of interest rates typically leads to higher interest rates applicable to our debt investments. Accordingly, an increase in interest rates may result in an increase of the amount of our pre-incentive fee net investment income and, as a result, an increase in incentive fees payable to Stellus Capital Management. Adverse developments resulting from changes in interest rates or hedging transactions could have a material adverse effect on our business, financial condition and results of operations.

Provisions in the Credit Facility or any other future borrowing facility may limit our discretion in operating our business.

The Credit Facility is, and any future borrowing facility may be, backed by all or a portion of our loans and securities on which the lenders will or, in the case of a future facility, may have a security interest. We may pledge up to 100% of our assets and may grant a security interest in all of our assets under the terms of any debt instrument we enter into with lenders. We expect that any security interests we grant will be set forth in a guarantee and security agreement and evidenced by the filing of financing statements by the agent for the lenders. In addition, we expect that the custodian for our securities serving as collateral for such loan would include in its electronic systems notices indicating the existence of such security interests and, following notice of occurrence of an event of default, if any, and during its continuance, will only accept transfer instructions with respect to any such securities from the lender or its designee. If we were to default under the terms of any debt instrument, the agent for the applicable lenders would be able to assume control of the timing of disposition of any or all of our assets securing such debt, which would have a material adverse effect on our business, financial condition, results of operations and cash flows.

In addition, any security interests as well as negative covenants under the Credit Facility or any other borrowing facility may limit our ability to incur additional liens or debt and may make it difficult for us to restructure or refinance indebtedness at or prior to maturity or obtain additional debt or equity financing. For example, under the terms of the Credit Facility, we have generally agreed to not incur any additional secured indebtedness, other than certain indebtedness that we may incur, in accordance with the Credit Facility, to allow us to purchase investments in U.S. Treasury Bills. In addition, we have agreed not to incur any additional indebtedness that has a maturity date prior to the maturity date of the Credit Facility. Further, if our borrowing base under the Credit Facility or any other borrowing facility were to decrease, we would be required to secure additional assets in an amount equal to any borrowing base deficiency. In the event that all of our assets are secured at the time of such a borrowing base deficiency, we could be required to repay advances under the Credit Facility or any other borrowing facility or make deposits to a collection account, either of which could have a material adverse impact on our ability to fund future investments and to make stockholder distributions.

In addition, under the Credit Facility or any other borrowing facility, we may be subject to limitations as to how borrowed funds may be used, which may include restrictions on geographic and industry concentrations, loan size, payment frequency and status, average life, collateral interests and investment ratings, as well as regulatory restrictions on leverage which may affect the amount of funding that may be obtained. There may also be certain requirements relating to portfolio performance, including required minimum portfolio yield and limitations on delinquencies and charge-offs, a violation of which could limit further advances and, in some cases, result in an event of default. Furthermore, we expect that the terms of the Credit Facility will contain a covenant requiring us to maintain compliance with RIC provisions at all times, subject to certain remedial provisions. Thus, a failure to maintain compliance with RIC provisions could result in an event of default under the Credit Facility. An event of default under the Credit Facility or any other borrowing facility could result in an accelerated maturity date for all amounts outstanding thereunder, which could have a material adverse effect on our business and financial condition. This could reduce our revenues and, by delaying any cash payment allowed to us under the Credit Facility or any other borrowing facility until the lenders have been paid in full, reduce our liquidity and cash flow and impair our ability to grow our business and maintain our qualification as a RIC.

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Provisions in the Credit Facility or any other future borrowing facility may limit our discretion in operating our busine

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Because we have received Board approval, and have submitted a proposal to a stockholder vote at our 2018 Annual Meeting, we will be subject to 150% Asset Coverage beginning on April 4, 2019 or following our 2018 Annual Meeting if we receive stockholder approval.

The SBCA provides that in order for a BDC whose common stock is traded on a national securities exchange to be subject to 150% Asset Coverage, the BDC must either obtain: (i) approval of the required majority of its non-interested directors who have no financial interest in the proposal, which would become effective one year after the date of such approval (the Board Effective Date), or (ii) obtain stockholder approval (of more than 50% of the votes cast for the proposal at a meeting in which quorum is present), which would become effective on the first day after the date of such stockholder approval. Because our Board has approved the adoption of 150% Asset Coverage, we will be able to incur twice as much indebtedness as we could have without such approval beginning on April 4, 2019. In addition, the Board also approved and recommended that stockholders vote for a proposal to authorize the Company to be subject to 150% Asset Coverage. If our stockholders approve this proposal, the reduced Asset Coverage Ratio would be effective the day after the Meeting. Incurring additional indebtedness could increase the risk of investing in our company. See Risk Factors Risks Relating to our Business and Structure Because we finance our investments with borrowed money, the potential for gain or loss on amounts invested in us is magnified and may increase the risk of investing in us.

We may in the future determine to fund a portion of our investments with preferred stock, which would magnify the potential for gain or loss and the risks of investing in us in the same way as our borrowings.

Preferred stock, which is another form of leverage, has the same risks to our common stockholders as borrowings because the dividends on any preferred stock we issue must be cumulative. Payment of such dividends and repayment of the liquidation preference of such preferred stock must take preference over any dividends or other payments to our common stockholders, and preferred stockholders are not subject to any of our expenses or losses and are not entitled to participate in any income or appreciation in excess of their stated preference.

Adverse developments in the credit markets may impair our ability to enter into any other future borrowing facility.

During the economic downturn in the United States that began in mid-2007, many commercial banks and other financial institutions stopped lending or significantly curtailed their lending activity. In addition, in an effort to stem losses and reduce their exposure to segments of the economy deemed to be high risk, some financial institutions limited refinancing and loan modification transactions and reviewed the terms of existing facilities to identify bases for accelerating the maturity of existing lending facilities. If these conditions recur (for example, as a result of a broadening of the current Euro zone credit crisis), it may be difficult for us to enter into a new borrowing facility, obtain other financing to finance the growth of our investments, or refinance any outstanding indebtedness on acceptable economic terms, or at all.

Most of our portfolio investments are recorded at fair value as determined in good faith by our board of directors and, as a result, there may be uncertainty as to the value of our portfolio investments.

Most of our portfolio investments will take the form of securities that are not publicly traded. The fair value of loans, securities and other investments that are not publicly traded may not be readily determinable, and we value these investments at fair value as determined in good faith by our board of directors, including to reflect significant events affecting the value of our investments. Most, if not all, of our investments (other than cash and cash equivalents) are classified as Level 3 under ASC Topic 820. This means that our portfolio valuations are based on unobservable inputs and our own assumptions about how market participants would price the asset or liability in question. Inputs into the determination of fair value of our portfolio investments require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes, which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes accompanied by disclaimers materially reduces the reliability of such information. We have retained the services of independent service providers to review the valuation of these loans and securities. The types of factors that the board of directors may take into account in determining the

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fair value of our investments generally include, as appropriate, comparison to publicly traded securities including such factors as yield, maturity and measures of credit quality, the enterprise value of a portfolio company, the nature and realizable value of any collateral, the portfolio company s ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business and other relevant factors. Because such valuations, and particularly valuations of private securities and private companies, are inherently uncertain, may fluctuate over short periods of time and may be based on estimates, our determinations of fair value may differ materially from the values that would have been used if a ready market for these loans and securities existed. Our net asset value could be adversely affected if our determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposal of such loans and securities.

We adjust quarterly the valuation of our portfolio to reflect our board of directors determination of the fair value of each investment in our portfolio. Any changes in fair value are recorded in our statement of operations as net change in unrealized appreciation or depreciation.

We may expose ourselves to risks if we engage in hedging transactions.

We may utilize instruments such as forward contracts, currency options and interest rate swaps, caps, collars and floors to seek to hedge against fluctuations in the relative values of our portfolio positions from changes in currency exchange rates and market interest rates. Use of these hedging instruments may expose us to counter-party credit risk. Hedging against a decline in the values of our portfolio positions does not eliminate the possibility of fluctuations in the values of such positions or prevent losses if the values of such positions decline. However, such hedging can establish other positions designed to gain from those same developments, thereby offsetting the decline in the value of such portfolio positions. Such hedging transactions may also limit the opportunity for gain if the values of the portfolio positions should increase. Moreover, it may not be possible to hedge against an exchange rate or interest rate fluctuation that is generally anticipated at an acceptable price.

If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud. As a result, stockholders could lose confidence in our financial and other public reporting, which would harm our business and the trading price of our common stock.

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports and, together with adequate disclosure controls and procedures, are designed to prevent fraud. Any failure to implement required new or improved controls, or difficulties encountered in their implementation could cause us to fail to meet our reporting obligations. In addition, any testing by us conducted in connection with Section 404 of the Sarbanes-Oxley Act, or the subsequent testing by our independent registered public accounting firm (when undertaken, as noted below), may reveal deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses or that may require prospective or retroactive changes to our consolidated financial statements or identify other areas for further attention or improvement. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our common stock.

We are required to disclose changes made in our internal control and procedures on a quarterly basis and our management is required to assess the effectiveness of these controls annually. An independent assessment of the effectiveness of our internal controls could detect problems that our management s assessment might not. Undetected material weaknesses in our internal controls could lead to financial statement restatements and require us to incur the expense of remediation.

Efforts to comply with Section 404 of the Sarbanes-Oxley Act involve significant expenditures, and non-compliance with Section 404 of the Sarbanes-Oxley Act may adversely affect us and the market price of our common stock.

In an effort to comply with Section 404 of the Sarbanes-Oxley Act, we expect to incur additional expenses, which may negatively impact our financial performance and our ability to make distributions to our stockholders. This process also may result in a diversion of management s time and attention. We cannot be

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certain as to the timing of completion of any evaluation, testing and remediation actions or the impact of the same on our operations, and we are not able to ensure that the process is effective or that our internal control over financial reporting is or will continue to be effective in a timely manner. In the event that we are unable to maintain or achieve compliance with Section 404 of the Sarbanes-Oxley Act and related rules, we and, consequently, the market price of our common stock may be adversely affected.

New or modified laws or regulations governing our operations may adversely affect our business.

We and our portfolio companies are subject to regulation by laws at the U.S. federal, state and local levels. These laws and regulations, as well as their interpretation, may change from time to time, and new laws, regulations and interpretations may also come into effect. Any such new or changed laws or regulations could have a material adverse effect on our business.

Additionally, changes to the laws and regulations governing our operations related to permitted investments may cause us to alter our investment strategy in order to avail ourselves of new or different opportunities. Such changes could result in material differences to the strategies and plans set forth in this prospectus and may shift our investment focus from the areas of expertise of Stellus Capital Management to other types of investments in which Stellus Capital Management may have little or no expertise or experience. Any such changes, if they occur, could have a material adverse effect on our results of operations and the value of your investment.

Legislative or other actions relating to taxes could have a negative effect on us.

The rules dealing with U.S. federal income taxation are constantly under review by persons involved in the legislative process and by the IRS and the U.S. Treasury Department. The U.S. House of Representatives and U.S. Senate recently passed tax reform legislation, which the President signed into law. Such legislation makes many changes to the Internal Revenue Code, including, among other things, significant changes to the taxation of business entities, the deductibility of interest expense, and the tax treatment of capital investment. We cannot predict with certainty how any changes in the tax laws might affect us, investors or our portfolio investments. New legislation and any U.S. Treasury regulations, administrative interpretations or court decisions interpreting such legislation could significantly and negatively affect our ability to qualify for tax treatment as a RIC or the U.S. federal income tax consequences to us and our investors of such qualification, or could have other adverse consequences. Investors are urged to consult with their tax advisor regarding tax legislative, regulatory or administrative developments and proposals and their potential effect on an investment in our securities.

The impact on us of recent financial reform legislation, including the Dodd-Frank Act, is uncertain.

The Dodd-Frank Wall Street Reform and Consumer Protection Act, as amended, or the Dodd-Frank Act, institutes a wide range of reforms that will have an impact on financial institutions. Many of the requirements called for in the Dodd-Frank Act are expected to be implemented over time, most of which will likely be subject to implementing regulations over the course of several years. However, the presidential administration has announced its intention to repeal, amend, or replace certain portions of Dodd-Frank and the regulations implemented thereunder. Given the uncertainty associated with the manner in which and whether the provisions of the Dodd-Frank Act will be implemented, repealed, amended or replaced, the full impact such requirements will have on our business, results of operations or financial condition is unclear. The changes resulting from the Dodd-Frank Act or any changes to the regulations already implemented thereunder may require us to invest significant management attention and resources to evaluate and make necessary changes in order to comply with new statutory and regulatory requirements. Failure to comply with any such laws, regulations or principles, or changes thereto, may negatively impact our business, results of operations and financial condition. While we cannot predict what effect any changes in the laws or regulations or their interpretations would have on us as a result of recent financial reform legislation, these changes could be materially adverse to us and our stockholders.

On November 16, 2017, a bipartisan group of U.S. Senators, led by the Senate Banking Committee Chairman, introduced the Economic Growth, Regulatory Relief, and Consumer Protection Act (the Senate Regulatory Relief Bill). The Senate Regulatory Relief Bill would revise various post-crisis regulatory

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requirements and provide targeted regulatory relief to certain financial institutions. Among the most significant of its proposed amendments to the Dodd-Frank Act are a substantial increase in the $50 billion asset threshold for automatic regulation of bank holding companies as systemically important financial institutions or SIFIs, an exemption from the Volcker Rule for insured depository institutions with less than $10 billion in consolidated assets and lower levels of trading assets and liabilities, as well as amendments to the liquidity leverage ratio and supplementary leverage ratio requirements. On December 5, 2017, the Senate Banking Committee approved the Senate Regulatory Relief Bill. If the legislation is adopted in the Senate, it remains unclear whether and how it would be reconciled with its House-passed counterpart, which is substantially different in scope and substance, and ultimately approved by both chambers of Congress. At this time it is unclear what impact this or other pending legislation and developments will have on regulations that affect our, our competitors and our portfolio companies businesses.

Any failure to comply with SBA regulations could have an adverse effect on our SBIC subsidiary s operations.

On June 20, 2014, our wholly-owned subsidiary, Stellus Capital SBIC LP, received a license from the SBA to operate as an SBIC. The SBA places certain limitations on the financing terms of investments by SBICs in portfolio companies and prohibits SBICs from providing funds for certain purposes or to businesses in a few prohibited industries. Compliance with SBIC requirements may cause our SBIC subsidiary to forgo attractive investment opportunities that are not permitted under SBA regulations.

Further, SBA regulations require that an SBIC be examined by the SBA to determine its compliance with the relevant SBA regulations at least every two years. The SBA prohibits, without prior SBA approval, a change of control of an SBIC or transfers that would result in any person (or a group of persons acting in concert) owning 10% or more of a class of capital stock of an SBIC. If our SBIC subsidiary fails to comply with applicable SBA regulations, the SBA could, depending on the severity of the violation, limit or prohibit its use of debentures, declare outstanding debentures immediately due and payable, and/or limit it from making new investments. In addition, the SBA can revoke or suspend a license for willful or repeated violation of, or willful or repeated failure to observe, any provision of the Small Business Investment Act of 1958 or any rule or regulation promulgated thereunder. These actions by the SBA would, in turn, negatively affect us because our SBIC subsidiary is our wholly-owned subsidiary.

Risks Related to Our Operations

Because we intend to distribute substantially all of our income to our stockholders to maintain our status as a RIC, we will continue to need additional capital to finance our growth. If additional funds are unavailable or not available on favorable terms, our ability to grow may be impaired.

We will need additional capital to fund new investments and grow our portfolio of investments. We intend to access the capital markets periodically to issue debt or equity securities or borrow from financial institutions in order to obtain such additional capital. Unfavorable economic conditions could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. A reduction in the availability of new capital could limit our ability to grow. In addition, we are required to distribute at least 90% of our net ordinary income and net short-term capital gains in excess of net long-term capital losses, if any, to our stockholders to maintain our qualification as a RIC. As a result, these earnings will not be available to fund new investments. An inability on our part to access the capital markets successfully could limit our ability to grow our business and execute our business strategy fully and could decrease our earnings, if any, which would have an adverse effect on the value of our shares of common stock.

As a BDC, we are required to meet a coverage ratio of total assets, less liabilities and indebtedness not represented by senior securities and excluding SBA-guaranteed debentures as permitted by exemptive relief obtained from the SEC, to total senior securities, which includes all of our borrowings with the exception of SBA-guaranteed debentures, of at least 200% (or 150% if certain requirements are met). This requirement limits the amount that we may borrow. Since we continue to need capital to grow our investment portfolio, these limitations may prevent us from incurring debt and require us to raise additional equity at a time when it may be disadvantageous to do so. While we expect that we will be able to borrow and to issue additional debt

Because we intend to distribute substantially all of our income to ourstockholders to maintain our status as a RIC, w

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securities and expect that we will be able to issue additional equity securities, which would in turn increase the equity capital available to us, we cannot assure you that debt and equity financing will be available to us on favorable terms, or at all. In addition, as a BDC, we generally are not permitted to issue equity securities priced below net asset value without stockholder approval. If additional funds are not available us, we may be forced to curtail or cease new investment activities, and our net asset value could decline.

Our wholly-owned SBIC subsidiary may be unable to make distributions to us that will enable us to maintain RIC tax treatment, which could result in the imposition of an entity-level tax.

In order for us to continue to qualify for RIC tax treatment and to minimize corporate-level taxes, we are required to distribute substantially all of our net taxable income and net capital gain income, including income from certain of our subsidiaries, which includes the income from our SBIC subsidiary. We are partially dependent on our SBIC subsidiary for cash distributions to enable us to meet the RIC distribution requirements. Our SBIC subsidiary may be limited by the Small Business Investment Act of 1958, and SBA regulations governing SBICs, from making certain distributions to us that may be necessary to maintain our status as a RIC. We may have to request a waiver of the SBA s restrictions for our SBIC subsidiary to make certain distributions to maintain our RIC status. We cannot assure you that the SBA will grant such waiver and if our SBIC subsidiary is unable to obtain a waiver, compliance with the SBA regulations may result in loss of RIC tax treatment and a consequent imposition of an entity-level tax on us.

Our ability to enter into transactions with our affiliates is restricted, which may limit the scope of investments available to us.

We are prohibited under the 1940 Act from participating in certain transactions with our affiliates without the prior approval of our independent directors and, in some cases, the SEC. Any person that owns, directly or indirectly, 5% or more of our outstanding voting securities will be our affiliate for purposes of the 1940 Act, and we are generally prohibited from buying or selling any security from or to such affiliate without the prior approval of our independent directors. The 1940 Act also prohibits certain joint transactions with certain of our affiliates, which could include concurrent investments in the same portfolio company, without prior approval of our independent directors and, in some cases, of the SEC. We are prohibited from buying or selling any security from or to any person that controls us or who owns more than 25% of our voting securities or certain of that person s affiliates, or entering into prohibited joint transactions with such persons, absent the prior approval of the SEC. As a result of these restrictions, we may be prohibited from buying or selling any security (other than any security of which we are the issuer) from or to any portfolio company of a private fund managed by Stellus Capital Management or its affiliates without the prior approval of the SEC, which may limit the scope of investment opportunities that would otherwise be available to us.

We have received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management (other than the D. E. Shaw group funds, as defined below) where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). Under the terms of the relief permitting us to co-invest with other funds managed by Stellus Capital Management, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is consistent with our investment objectives and strategies.

The involvement of our interested directors in the valuation process may create conflicts of interest.

We make many of our portfolio investments in the form of loans and securities that are not publicly traded and for which no market based price quotation is available. As a result, our board of directors determines the fair value of these loans and securities in good faith as described elsewhere in this prospectus. In connection with that determination, investment professionals from Stellus Capital Management may provide our board of directors with valuations based upon the most recent portfolio company financial statements available and projected financial results of each portfolio company. While the valuation for each portfolio investment is reviewed by an independent valuation firm at least twice annually, the ultimate determination of fair value is made by our board of directors, including our interested directors, and not by such third party valuation firm. In addition, Messrs. Ladd, D Angelo and Davis, each an interested member of our board of directors, has a direct pecuniary interest in Stellus Capital Management. The participation of Stellus Capital Management s investment professionals in our valuation process, and the pecuniary interest in Stellus Capital Management by certain members of our board of directors, could result in a conflict of interest as Stellus Capital Management s management fee is based, in part, on the value of our gross assets, and incentive fees are based, in part, on realized gains and realized and unrealized losses.

There are conflicts related to other arrangements with Stellus Capital Management.

We have entered into a license agreement with Stellus Capital Management under which Stellus Capital Management has agreed to grant us a non-exclusive, royalty-free license to use the name Stellus Capital. In addition, we have entered into an administration agreement with Stellus Capital Management pursuant to which we are required to pay to Stellus Capital Management our allocable portion of overhead and other expenses incurred by Stellus Capital Management in performing its obligations under such administration agreement, such as rent and our allocable portion of the cost of our chief financial officer and chief compliance officer and his staff. This will create conflicts of interest that our board of directors will monitor. For example, under the terms of the license agreement, we will be unable to preclude Stellus Capital Management from licensing or transferring the ownership of the Stellus Capital name to third parties, some of whom may compete against us. Consequently, we will be unable to prevent any damage to goodwill that may occur as a result of the activities of Stellus Capital Management or others. Furthermore, in the event the license agreement is terminated, we will be required to change our name and cease using Stellus Capital as part of our name. Any of these events could disrupt our recognition in the market place, damage any goodwill we may have generated and otherwise harm our business.

The investment advisory agreement and the administration agreement with Stellus Capital Management were not negotiated on an arm s length basis and may not be as favorable to us as if they had been negotiated with an unaffiliated third party.

The investment advisory agreement and the administration agreement were negotiated between related parties. Consequently, their terms, including fees payable to Stellus Capital Management, may not be as favorable to us as if they had been negotiated with an unaffiliated third party. In addition, we may choose not to enforce, or to enforce less vigorously, our rights and remedies under these agreements because of our desire to maintain our ongoing relationship with Stellus Capital Management and its affiliates. Any such decision, however, would breach our fiduciary obligations to our stockholders.

The time and resources that Stellus Capital Management devote to us may be diverted, and we may face additional competition due to the fact that Stellus Capital Management and its affiliates are not prohibited from raising money for, or managing, another entity that makes the same types of investments that we target.

Stellus Capital Management and some of its affiliates, including our officers and our non-independent directors, are not prohibited from raising money for, or managing, another investment entity that makes the same types of investments as those we target. For example, Stellus Capital Management currently manages a private credit fund that will have an investment strategy that is identical to our investment strategy and with which we intend to co-invest. In addition, pursuant to sub-advisory arrangements, Stellus Capital Management provides non-discretionary advisory services to the D. E. Shaw group related to a private investment fund and a strategy of a private multi-strategy investment fund to which the D. E. Shaw group serves as investment adviser. As a result, the time and resources they could devote to us may be diverted. In addition, we may compete with any such investment entity for the same investors and investment opportunities.

Our incentive fee arrangements with Stellus Capital Management may vary from those of other investment funds, account or investment vehicles managed by Stellus Capital Management, which may create an incentive for Stellus Capital Management to devote time and resources to a higher fee-paying fund.

If Stellus Capital Management is paid a higher performance-based fee from any of its other funds, it may have an incentive to devote more research and development or other activities, and/or recommend the allocation of investment opportunities, to such higher fee-paying fund. For example, to the extent Stellus

Capital Management s incentive compensation is not subject to a hurdle or total return requirement with respect to another fund, it may have an incentive to devote time and resources to such other fund.

Stellus Capital Management s liability is limited under the investment advisory agreement and we have agreed to indemnify Stellus Capital Management against certain liabilities, which may lead Stellus Capital Management to act in a riskier manner on our behalf than it would when acting for its own account.

Under the investment advisory agreement, Stellus Capital Management has not assumed any responsibility to us other than to render the services called for under that agreement. It will not be responsible for any action of our board of directors in following or declining to follow Stellus Capital Management s advice or recommendations. Under the investment advisory agreement, Stellus Capital Management, its officers, members and personnel, and any person controlling or controlled by Stellus Capital Management will not be liable to us, any subsidiary of ours, our directors, our stockholders or any subsidiary s stockholders or partners for acts or omissions performed in accordance with and pursuant to the investment advisory agreement, except those resulting from acts constituting gross negligence, willful misfeasance, bad faith or reckless disregard of the duties that Stellus Capital Management owes to us under the investment advisory agreement. In addition, as part of the investment advisory agreement, we have agreed to indemnify Stellus Capital Management and each of its officers, directors, members, managers and employees from and against any claims or liabilities, including reasonable legal fees and other expenses reasonably incurred, arising out of or in connection with our business and operations or any action taken or omitted on our behalf pursuant to authority granted by the investment advisory agreement, except where attributable to gross negligence, willful misfeasance, bad faith or reckless disregard of such person s duties under the investment advisory agreement. These protections may lead Stellus Capital Management to act in a riskier manner when acting on our behalf than it would when acting for its own account.

Stellus Capital Management can resign as our investment adviser or administrator upon 60 days notice and we may not be able to find a suitable replacement within that time, or at all, resulting in a disruption in our operations that could adversely affect our financial condition, business and results of operations.

Stellus Capital Management has the right under the investment advisory agreement to resign as our investment adviser at any time upon 60 days written notice, whether we have found a replacement or not. Similarly, Stellus Capital Management has the right under the administration agreement to resign at any time upon 60 days written notice, whether we have found a replacement or not. If Stellus Capital Management was to resign, we may not be able to find a new investment adviser or administrator or hire internal management with similar expertise and ability to provide the same or equivalent services on acceptable terms within 60 days, or at all. If we are unable to do so quickly, our operations are likely to experience a disruption, our financial condition, business and results of operations as well as our ability to pay distributions to our stockholders are likely to be adversely affected and the market price of our shares may decline. In addition, the coordination of our internal management and investment or administrative activities, as applicable, is likely to suffer if we are unable to identify and reach an agreement with a single institution or group of executives having the expertise possessed by Stellus Capital Management. Even if we are able to retain comparable management, whether internal or external, the integration of such management and their lack of familiarity with our investment objective may result in additional costs and time delays that may adversely affect our business, financial condition, results of operations and cash flows.

Our incentive fee arrangements with Stellus Capital Management may varyfrom those of other investment funds, ac

If we fail to maintain our status as a BDC, our business and operating flexibility could be significantly reduced.

We qualify as a BDC under the 1940 Act. The 1940 Act imposes numerous constraints on the operations of BDCs. For example, BDCs are required to invest at least 70.0% of their total assets in specified types of securities, primarily in private companies or thinly-traded U.S. public companies, cash, cash equivalents, U.S. government securities and other high quality debt investments that mature in one year or less. Failure to comply with the requirements imposed on BDCs by the 1940 Act could cause the SEC to bring an enforcement action against us and/or expose us to claims of private litigants. In addition, upon approval of a majority of our stockholders, we may elect to withdraw their respective election as a BDC. If we decide to withdraw our election, or if we otherwise fail to qualify, or maintain our qualification, as a BDC, we may be

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subject to the substantially greater regulation under the 1940 Act as a closed-end investment company. Compliance with these regulations would significantly decrease our operating flexibility and could significantly increase our cost of doing business.

If we do not invest a sufficient portion of our assets in qualifying assets, we could fail to maintain our qualification as a BDC or be precluded from investing according to our current business strategy.

As a BDC, we may not acquire any assets other than qualifying assets unless, at the time of and after giving effect to such acquisition, at least 70% of our total assets are qualifying assets.

We believe that most of the investments that we may acquire in the future will constitute qualifying assets. However, we may be precluded from investing in what we believe to be attractive investments if such investments are not qualifying assets for purposes of the 1940 Act. If we do not invest a sufficient portion of our assets in qualifying assets, we could violate the 1940 Act provisions applicable to BDCs. As a result of such violation, specific rules under the 1940 Act could prevent us, for example, from making follow-on investments in existing portfolio companies (which could result in the dilution of our position).

If we do not maintain our status as a BDC, we would be subject to regulation as a registered closed-end investment company under the 1940 Act. As a registered closed-end investment company, we would be subject to substantially more regulatory restrictions under the 1940 Act which would significantly decrease our operating flexibility.

We may experience fluctuations in our annual and quarterly operating results.

We could experience fluctuations in our annual and quarterly operating results due to a number of factors, including the interest rate payable on the loans and debt securities we acquire, the default rate on such loans and securities, the level of our expenses, variations in and the timing of the recognition of realized and unrealized gains or losses, the degree to which we encounter competition in our markets and general economic conditions. In light of these factors, results for any period should not be relied upon as being indicative of performance in future periods.

Our board of directors may change our investment objective, operating policies and strategies without prior notice or stockholder approval.

Our board of directors has the authority, except as otherwise provided in the 1940 Act, to modify or waive certain of our operating policies and strategies without prior notice and without stockholder approval. However, absent stockholder approval, we may not change the nature of our business so as to cease to be, or withdraw our election as, a BDC. We cannot predict the effect any changes to our current operating policies and strategies would have on our business, operating results and the market price of our common stock. Nevertheless, any such changes could adversely affect our business and impair our ability to make distributions to our stockholders.

Our board of directors is authorized to reclassify any unissued shares of common stock into one or more classes of preferred stock, which could convey special rights and privileges to its owners.

Under Maryland General Corporation Law and our charter, our board of directors is authorized to classify and reclassify any authorized but unissued shares of stock into one or more classes of stock, including preferred stock. Prior to issuance of shares of each class or series, the board of directors will be required by Maryland law and our charter to set the terms, preferences, conversion or other rights, voting powers, restrictions, limitations as to stockholder distributions, qualifications and terms or conditions of redemption for each class or series. Thus, the board of directors could authorize the issuance of shares of preferred stock with terms and conditions which could have the effect of delaying, deferring or preventing a transaction or a change in control that might involve a premium price for holders of our common stock or that otherwise might be in their best interest. The cost of any such reclassification would be borne by our common stockholders. Certain matters under the 1940 Act require the separate vote of the holders of any issued and outstanding preferred stock. For example, the 1940 Act provides that holders of preferred stock are entitled to vote separately from holders of common stock to elect two preferred stock directors. We currently have no plans to issue preferred stock. The issuance of preferred shares convertible into shares of common stock may also reduce the net income and net asset value per share of our common stock upon conversion, provided, that we will only be permitted to issue such convertible preferred stock to the extent we comply with the requirements of Section 61 of the 1940 Act, including obtaining common stockholder approval. These effects, among others, could have an adverse effect on your investment in our common stock.

Provisions of the Maryland General Corporation Law and of our charter and bylaws could deter takeover attempts and have an adverse impact on the price of our common stock.

The Maryland General Corporation Law and our charter and bylaws contain provisions that may discourage, delay or make more difficult a change in control of Stellus Capital Investment Corporation or the removal of our directors. We are subject to the Maryland Business Combination Act, subject to any applicable requirements of the 1940 Act. Our board of directors has adopted a resolution exempting from the Business Combination Act any business combination between us and any other person, subject to prior approval of such business combination by our board of directors, including approval by a majority of our independent directors. If the resolution exempting business combinations is repealed or our board of directors does not approve a business combination, the Business Combination Act may discourage third parties from trying to acquire control of us and increase the difficulty of consummating such an offer. Our bylaws exempt from the Maryland Control Share Acquisition Act acquisitions of our stock by any person. If we amend our bylaws to repeal the exemption from the Control Share Acquisition Act, the Control Share Acquisition Act also may make it more difficult for a third party to obtain control of us and increase the difficulty of consummating such a transaction.

We have also adopted measures that may make it difficult for a third party to obtain control of us, including provisions of our charter classifying our board of directors in three classes serving staggered three-year terms, and authorizing our board of directors to classify or reclassify shares of our stock in one or more classes or series, to cause the issuance of additional shares of our stock, to amend our charter without stockholder approval and to increase or decrease the number of shares of stock that we have authority to issue. These provisions, as well as other provisions of our charter and bylaws, may delay, defer or prevent a transaction or a change in control that might otherwise be in the best interests of our stockholders. See Description of our Capital Stock Certain Provisions of the Maryland General Corporation Law and Our Charter and Bylaws.

We are highly dependent on information systems and systems failures could significantly disrupt our business, which may, in turn, negatively affect the market price of our common stock and our ability to make distributions to our stockholders.

Our business is highly dependent on the communications and information systems of Stellus Capital Management. In addition, certain of these systems are provided to Stellus Capital Management by third party service providers. Any failure or interruption of such systems, including as a result of the termination of an agreement with any such third party service provider, could cause delays or other problems in our activities. This, in turn, could have a material adverse effect on our operating results and negatively affect the market price of our common stock and our ability to make distributions to our stockholders.

The failure in cyber security systems, as well as the occurrence of events unanticipated in our disaster recovery systems and management continuity planning could impair our ability to conduct business effectively.

The occurrence of a disaster such as a cyber attack, a natural catastrophe, an industrial accident, a terrorist attack or war, events unanticipated in our disaster recovery systems, or a support failure from external providers, could have an adverse effect on our ability to conduct business and on our results of operations and financial condition, particularly if those events affect the Company s computer-based data processing, transmission, storage, and retrieval systems or destroy data. If a significant number of our managers were unavailable in the event of a disaster, our ability to effectively conduct its business could be severely compromised.

We depend heavily upon computer systems to perform necessary business functions. Despite our implementation of a variety of security measures, our computer systems could be subject to cyber attacks and unauthorized access, such as physical and electronic break-ins or unauthorized tampering. Like other companies, we may experience threats to its data and systems, including malware and computer virus attacks, unauthorized access, system failures and disruptions. If one or more of these events occurs, it could potentially jeopardize the confidential, proprietary and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our operations, which could result in damage to our reputation, financial losses, litigation, increased costs, regulatory penalties and/or customer dissatisfaction or loss.

Risks Related to Economic Conditions

Global economic, political and market conditions may adversely affect our business, results of operations and financial condition, including our revenue growth and profitability.

The U.S. and global capital markets experienced extreme volatility and disruption during the economic downturn that began in mid-2007, and the U.S. economy was in a recession for several consecutive calendar quarters during the same period. In 2010, a financial crisis emerged in Europe, triggered by high budget deficits and rising direct and contingent sovereign debt, which created concerns about the ability of certain nations to continue to service their sovereign debt obligations. Risks resulting from such debt crisis and any future debt crisis in Europe or any similar crisis elsewhere could have a detrimental impact on the global economic recovery, sovereign and non-sovereign debt in certain countries and the financial condition of financial institutions generally. In July and August 2015, Greece reached agreements with its creditors for bailouts that provide aid in exchange for certain austerity measures. These and similar austerity measures may adversely affect world economic conditions and have an adverse impact on our business and that of our portfolio companies. In the second quarter of 2015, stock prices in China experienced a significant drop, resulting primarily from continued sell-off of shares trading in Chinese markets. In August 2015, Chinese authorities sharply devalued China s currency.

In June 2016, the United Kingdom held a referendum in which voters approved an exit from the European Union, and the implications of the United Kingdom s pending withdrawal from the European Union are unclear at present. In November 2016, voters in the United States elected a new president and the implications of a new presidential administration are unclear at present. These market and economic disruptions affected, and these and other similar market and economic disruptions may in the future affect, the U.S. capital markets, which could adversely affect our business and that of our portfolio companies and the broader financial and credit markets and have reduced the availability of debt and equity capital for the market as a whole and to financial firms, in particular. At various times, these disruptions resulted in, and may in the future result, a lack of liquidity in parts of the debt capital markets, significant write-offs in the financial services sector and the repricing of credit risk.

These conditions may reoccur for a prolonged period of time again or materially worsen in the future, including as a result of U.S. government shutdowns or further downgrades to the U.S. government s sovereign credit rating or the perceived credit worthiness of the United States or other large global economies. Unfavorable economic conditions, including future recessions, also could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. We may in the future have difficulty accessing debt and equity capital on attractive terms, or at all, and a severe disruption and instability in the global financial markets or deteriorations in credit and financing conditions may cause us to reduce the volume of loans we originate and/or fund, adversely affect the value of our portfolio investments or otherwise have a material adverse effect on our business, financial condition, results of operations and cash flows.

Risks Related to our Investments

Our investments in software companies are subject to many risks, including regulatory concerns, litigation risks and intense competition.

As of March 31, 2018, our investments in software companies represented 10.93% of our total portfolio, at fair value. Our investments in software companies are subject to substantial risks. For example, our portfolio companies face intense competition since their businesses are rapidly evolving and intensely

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competitive, and are subject to changing technology, shifting user needs, and frequent introductions of new products and services. Software companies have many competitors in different industries, including general purpose search engines, vertical search engines and e-commerce sites, social networking sites, traditional media companies, and providers of online products and services. Potential competitors to our portfolio companies in the software industries range from large and established companies to emerging start-ups. Further, such companies are subject to laws that were adopted prior to the advent of the Internet and related technologies and, as a result, do not contemplate or address the unique issues of the Internet and related technologies. The laws that do reference the Internet are being interpreted by the courts, but their applicability and scope remain uncertain. For example, the laws relating to the liability of providers of online services are currently unsettled both within the United States, and abroad. Claims have been threatened and filed under both U.S. and foreign laws for defamation, invasion of privacy and other tort claims, unlawful activity, copyright and trademark infringement, or other theories based on the nature and content of the materials searched and the ads posted by a company s users, a company s products and services, or content generated by a company s users. Further, the growth of software companies into a variety of new fields implicate a variety of new regulatory issues and may subject such companies to increased regulatory scrutiny, particularly in the United States and Europe. As a result, these portfolio company investments face considerable risk. This could, in turn, materially adversely affect the value of the software companies in our portfolio.

Changes in healthcare laws and other regulations applicable to some of our portfolio companies businesses may constrain their ability to offer their products and services.

Changes in healthcare or other laws and regulations applicable to the businesses of some of our portfolio companies may occur that could increase their compliance and other costs of doing business, require significant systems enhancements, or render their products or services less profitable or obsolete, any of which could have a material adverse effect on their results of operations. There has also been an increased political and regulatory focus on healthcare laws in recent years, and new legislation could have a material effect on the business and operations of some of our portfolio companies.

Economic recessions or downturns could impair our portfolio companies, which would harm our operating results.

Many of the portfolio companies in which we make, and expect to make, investments, including those currently included in our portfolio, are likely to be susceptible to economic slowdowns or recessions and may be unable to repay our loans during such periods. Therefore, the number of our non-performing assets is likely to increase and the value of our portfolio is likely to decrease during such periods. Adverse economic conditions may decrease the value of collateral securing some of our loans and debt securities and the value of our equity investments. Economic slowdowns or recessions could lead to financial losses in our portfolio and a decrease in revenues, net income and assets. Unfavorable economic conditions also could increase our funding costs, limit our access to the capital markets or result in a decision by lenders not to extend credit to us. These events could prevent us from increasing our investments and harm our operating results.

A portfolio company s failure to satisfy financial or operating covenants imposed by us or other lenders could lead to defaults and, potentially, termination of its loans and foreclosure on its assets, which could trigger cross-defaults under other agreements and jeopardize our portfolio company s ability to meet its obligations under the loans and debt securities that we hold. We may incur expenses to the extent necessary to seek recovery upon default or to negotiate new terms with a defaulting portfolio company. In addition, lenders in certain cases can be subject to lender liability

Our investments in software companies are subject to many risks, includingregulatory concerns, litigation risks and claims for actions taken by them when they become too involved in the borrower s business or exercise control over a borrower. It is possible that we could become subject to a lender s liability claim, including as a result of actions taken if we render significant managerial assistance to the borrower. Furthermore, if one of our portfolio companies were to file for bankruptcy protection, a bankruptcy court might re-characterize our debt holding and subordinate all or a portion of our claim to claims of other creditors, even though we may have structured our investment as senior secured debt. The likelihood of such a re-characterization would depend on the facts and circumstances, including the extent to which we provided managerial assistance to that portfolio company.

Economic recessions or downturns could impair our portfolio companies,which would harm our operating results.

Our investments in leveraged portfolio companies may be risky, and we could lose all or part of our investment.

Investment in leveraged companies involves a number of significant risks. Leveraged companies in which we invest may have limited financial resources and may be unable to meet their obligations under their loans and debt securities that we hold. Such developments may be accompanied by a deterioration in the value of any collateral and a reduction in the likelihood of our realizing any guarantees that we may have obtained in connection with our investment. Smaller leveraged companies also may have less predictable operating results and may require substantial additional capital to support their operations, finance their expansion or maintain their competitive position.

We may hold the loans and debt securities of leveraged companies that may, due to the significant operating volatility typical of such companies, enter into bankruptcy proceedings.

Leveraged companies may experience bankruptcy or similar financial distress. The bankruptcy process has a number of significant inherent risks. Many events in a bankruptcy proceeding are the product of contested matters and adversary proceedings and are beyond the control of the creditors. A bankruptcy filing by a portfolio company may adversely and permanently affect that company. If the proceeding is converted to a liquidation, the value of the portfolio company may not equal the liquidation value that was believed to exist at the time of the investment. The duration of a bankruptcy proceeding is also difficult to predict, and a creditor s return on investment can be adversely affected by delays until the plan of reorganization or liquidation ultimately becomes effective. The administrative costs in connection with a bankruptcy proceeding are frequently high and would be paid out of the debtor s estate prior to any return to creditors. Because the standards for classification of claims under bankruptcy law are vague, our influence with respect to the class of securities or other obligations we own may be lost by increases in the number and amount of claims in the same class or by different classification and treatment. In the early stages of the bankruptcy process, it is often difficult to estimate the extent of, or even to identify, any contingent claims that might be made. In addition, certain claims that have priority by law (for example, claims for taxes) may be substantial.

Our investments in private and middle-market portfolio companies are risky, and we could lose all or part of our investment.

Investment in private and middle-market companies involves a number of significant risks. Generally, little public information exists about these companies, and we rely on the ability of Stellus Capital Management s investment professionals to obtain adequate information to evaluate the potential returns from investing in these companies. If we are unable to uncover all material information about these companies, we may not make a fully informed investment decision, and we may lose money on our investments. Middle-market companies may have limited financial resources and may be unable to meet their obligations under their loans and debt securities that we hold, which may be accompanied by a deterioration in the value of any collateral and a reduction in the likelihood of our realizing any guarantees we may have obtained in connection with our investment. In addition, such companies typically have shorter operating histories, narrower product lines and smaller market shares than larger businesses, which tend to render them more vulnerable to competitors actions and market conditions, as well as general economic downturns. Additionally, middle-market companies are more likely to depend on the management talents and efforts of a small group of persons. Therefore, the death, disability, resignation or termination of one or more of these persons could have a material adverse impact on one or more of the portfolio companies we invest in and, in turn, on us. Middle-market companies also may be parties to litigation and may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence. In addition, our executive officers, directors and investment adviser may, in the ordinary course of business, be named as defendants in litigation arising from our investments in portfolio companies.

The lack of liquidity in our investments may adversely affect our business.

Most of our assets are invested in illiquid loans and securities, and a substantial portion of our investments in leveraged companies are subject to legal and other restrictions on resale or are otherwise less liquid than more broadly traded public securities. The illiquidity of these investments may make it difficult for us to sell such investments if the need arises. In addition, if we are required to liquidate all or a portion of our

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portfolio quickly, we may realize significantly less than the value at which we have previously recorded our investments. Also, as noted above, we may be limited or prohibited in our ability to sell or otherwise exit certain positions in our portfolio as such a transaction could be considered a joint transaction prohibited by the 1940 Act.

Price declines and illiquidity in the corporate debt markets may adversely affect the fair value of our portfolio investments, reducing our net asset value through increased net unrealized depreciation.

As a BDC, we are required to carry our investments at market value or, if no market value is ascertainable, at fair value as determined in good faith by our board of directors. As part of the valuation process, we may take into account the following types of factors, if relevant, in determining the fair value of our investments:

- available current market data, including relevant and applicable market trading and transaction comparables;
- applicable market yields and multiples;
- security covenants;
- call protection provisions;
- information rights;
- the nature and realizable value of any collateral;
- the portfolio company s ability to make payments, its earnings and discounted cash flows and the markets in which it does business;
- comparisons of financial ratios of peer companies that are public;
- comparable merger and acquisition transactions; and
- the principal market and enterprise values.

When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, we use the pricing indicated by the external event to corroborate our valuation. We record decreases in the market values or fair values of our investments as unrealized depreciation. Declines in prices and liquidity in the corporate debt markets may result in significant net unrealized depreciation in our portfolio. The effect of all of these factors on our portfolio may reduce our net asset value by increasing net unrealized depreciation in our portfolio. Depending on market conditions, we could incur substantial realized losses and may suffer additional unrealized losses in future periods, which could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We are a non-diversified investment company within the meaning of the 1940 Act, and therefore we are not limited with respect to the proportion of our assets that may be invested in securities of a single issuer.

We are classified as a non-diversified investment company within the meaning of the 1940 Act, which means that we are not limited by the 1940 Act with respect to the proportion of our assets that we may invest in securities of a single issuer. Beyond the asset diversification requirements associated with our qualification as a RIC under the Code, we do not have fixed guidelines for diversification. To the extent that we assume large positions in the securities of a small number of issuers or our investments are concentrated in relatively few industries, our net asset value may fluctuate to a greater extent than that of a diversified investment company as a result of changes in the financial condition or the market s assessment of the issuer. We may also be more susceptible to any single economic or regulatory occurrence than a diversified investment company.

Our failure to make follow-on investments in our portfolio companies could impair the value of our portfolio.

Following an initial investment in a portfolio company, we may make additional investments in that portfolio company as follow-on investments, in seeking to:

increase or maintain in whole or in part our position as a creditor or equity ownership percentage in a portfolio company;

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exercise warrants, options or convertible securities that were acquired in the original or subsequent financing; or
preserve or enhance the value of our investment.

We have discretion to make follow-on investments, subject to the availability of capital resources. Failure on our part to make follow-on investments may, in some circumstances, jeopardize the continued viability of a portfolio company and our initial investment, or may result in a missed opportunity for us to increase our participation in a successful operation. Even if we have sufficient capital to make a desired follow-on investment, we may elect not to make a follow-on investment because we may not want to increase our level of risk, because we prefer other opportunities or because we are inhibited by compliance with BDC requirements of the 1940 Act or the desire to maintain our qualification as a RIC. Our ability to make follow-on investments may also be limited by our compliance with the conditions under the exemptive relief order we received from the SEC related to co-investments with investment funds managed by Stellus Capital Management or Stellus Capital Management s allocation policy.

Because we generally do not hold controlling equity interests in our portfolio companies, we may not be able to exercise control over our portfolio companies or to prevent decisions by management of our portfolio companies that could decrease the value of our investments.

We do not hold controlling equity positions in any of the portfolio companies included in our portfolio and, although we may do so in the future, we do not currently intend to hold controlling equity positions in our portfolio companies (including those included in our portfolio). As a result, we are subject to the risk that a portfolio company may make business decisions with which we disagree, and that the management and/or stockholders of a portfolio company may take risks or otherwise act in ways that are adverse to our interests. Due to the lack of liquidity of the debt and equity investments that we hold in our portfolio companies, we may not be able to dispose of our investments in the event we disagree with the actions of a portfolio company and may therefore suffer a decrease in the value of our investments.

Defaults by our portfolio companies will harm our operating results.

A portfolio company s failure to satisfy financial or operating covenants imposed by us or other lenders could lead to defaults and, potentially, termination of its loans and foreclosure on its assets. This could trigger cross-defaults under other agreements and jeopardize such portfolio company s ability to meet its obligations under the loans or debt or equity securities that we hold. We may incur expenses to the extent necessary to seek recovery upon default or to negotiate new terms, which may include the waiver of certain financial covenants, with a defaulting portfolio company.

Prepayments of our debt investments by our portfolio companies could adversely impact our results of operations and ability to make stockholder distributions and result in a decline in the market price of our shares.

We are subject to the risk that the debt investments we make in our portfolio companies may be repaid prior to maturity. We expect that our investments will generally allow for repayment at any time subject to certain penalties. When this occurs, we intend to generally reinvest these proceeds in temporary investments, pending their future investment in accordance with our investment strategy. These temporary investments will typically have substantially lower yields than the debt being prepaid, and we could experience significant delays in reinvesting these amounts. Any future investment may also be at lower yields than the debt that was repaid. As a result, our results of operations could be materially adversely affected if one or more of our portfolio companies elects to prepay amounts owed to us. Additionally, prepayments could negatively impact our ability to make, or the amount of, stockholder distributions with respect to our common stock, which could result in a decline in the market price of our shares.

The interest rates of our floating-rate loans to our portfolio companies that extend beyond 2021 might be subject to change based on recent regulatory changes.

LIBOR, the London Interbank Offered Rate, is the basic rate of interest used in lending transactions between banks on the London interbank market and is widely used as a reference for setting the interest rate on loans globally. We typically use LIBOR as a reference rate in floating-rate loans we extend to portfolio

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companies such that the interest due to us pursuant to a term loan extended to a portfolio company is calculated using LIBOR. The terms of our debt investments generally include minimum interest rate floors which are calculated based on LIBOR.

On July 27, 2017, the United Kingdom s Financial Conduct Authority, which regulates LIBOR, announced that it intends to phase out LIBOR by the end of 2021. It is unclear if at that time whether LIBOR will cease to exist or if new methods of calculating LIBOR will be established such that it continues to exist after 2021. The U.S. Federal Reserve, in conjunction with the Alternative Reference Rates Committee, a steering committee comprised of large U.S. financial institutions, is considering replacing U.S. dollar LIBOR with a new index calculated by short term repurchase agreements, backed by Treasury securities. The future of LIBOR at this time is uncertain. If LIBOR ceases to exist, we may need to renegotiate the credit agreements extending beyond 2021 with our portfolio companies that utilize LIBOR as a factor in determining the interest rate to replace LIBOR with the new standard that is established.

The effect of global climate change may impact the operations of our portfolio companies.

There may be evidence of global climate change. Climate change creates physical and financial risk and some of our portfolio companies may be adversely affected by climate change. For example, the needs of customers of energy companies vary with weather conditions, primarily temperature and humidity. To the extent weather conditions are affected by climate change, energy use could increase or decrease depending on the duration and magnitude of any changes. Increases in the cost of energy could adversely affect the cost of operations of our portfolio companies if the use of energy products or services is material to their business. A decrease in energy use due to weather changes may affect some of our portfolio companies financial condition, through decreased revenues. Extreme weather conditions in general require more system backup, adding to costs, and can contribute to increased system stresses, including service interruptions. In December 2015, the United Nations, of which the U.S. is a member, adopted a climate accord with the long-term goal of limiting global warming and the short-term goal of significantly reducing greenhouse gas emissions. As a result, our portfolio companies, particularly those operating in the energy sector, may be subject to new or strengthened regulations or legislation which could increase their operating costs and/or decrease their revenues.

Our portfolio companies may incur debt that ranks equally with, or senior to, our investments in such companies.

We invest a portion of our capital in second lien and subordinated loans issued by our portfolio companies. The portfolio companies usually have, or may be permitted to incur, other debt that ranks equally with, or senior to, the loans in which we invest. By their terms, such debt instruments may provide that the holders are entitled to receive payment of interest or principal on or before the dates on which we are entitled to receive payments in respect of the loans in which we invest. Also, in the event of insolvency, liquidation, dissolution, reorganization or bankruptcy of a portfolio company, holders of debt instruments ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any distribution in respect of our investment. After repaying senior creditors, a portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of debt ranking equally with loans in which we invest, we would have to share any distributions on an equal and ratable basis with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization or bankruptcy of the relevant portfolio company.

Additionally, certain loans that we make to portfolio companies may be secured on a second priority basis by the same collateral securing senior secured debt of such companies. The first priority liens on the collateral will secure the

The interest rates of our floating-rate loans to our portfolio companies thatextend beyond 2021 might be subject to c portfolio company s obligations under any outstanding senior debt and may secure certain other future debt that may be permitted to be incurred by the portfolio company under the agreements governing the loans. The holders of obligations secured by first priority liens on the collateral will generally control the liquidation of, and be entitled to receive proceeds from, any realization of the collateral to repay their obligations in full before us. In addition, the value of the collateral in the event of liquidation will depend on market and economic conditions, the availability of buyers and other factors. There can be no assurance that the proceeds, if any, from sales of all of the collateral would be sufficient to satisfy the loan obligations secured by the second priority liens after payment in full of all obligations secured by the first

Our portfolio companies may incur debt that ranks equally with, or senior to,our investments in such companies.

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priority liens on the collateral. If such proceeds were not sufficient to repay amounts outstanding under the loan obligations secured by the second priority liens, then we, to the extent not repaid from the proceeds of the sale of the collateral, will only have an unsecured claim against the portfolio company s remaining assets, if any.

We may also make unsecured loans to portfolio companies, meaning that such loans will not benefit from any interest in collateral of such companies. Liens on such portfolio companies collateral, if any, will secure the portfolio company s obligations under its outstanding secured debt and may secure certain future debt that is permitted to be incurred by the portfolio company under its secured loan agreements. The holders of obligations secured by such liens will generally control the liquidation of, and be entitled to receive proceeds from, any realization of such collateral to repay their obligations in full before us. In addition, the value of such collateral in the event of liquidation will depend on market and economic conditions, the availability of buyers and other factors. There can be no assurance that the proceeds, if any, from sales of such collateral would be sufficient to satisfy our unsecured loan obligations after payment in full of all secured loan obligations. If such proceeds were not sufficient to repay the outstanding secured loan obligations, then our unsecured claims would rank equally with the unpaid portion of such secured creditors claims against the portfolio company s remaining assets, if any.

The rights we may have with respect to the collateral securing the loans we make to our portfolio companies with senior debt outstanding may also be limited pursuant to the terms of one or more intercreditor agreements that we enter into with the holders of such senior debt. Under a typical intercreditor agreement, at any time that obligations that have the benefit of the first priority liens are outstanding, any of the following actions that may be taken in respect of the collateral will be at the direction of the holders of the obligations secured by the first priority liens:

- the ability to cause the commencement of enforcement proceedings against the collateral;
- the ability to control the conduct of such proceedings;
- the approval of amendments to collateral documents;
- releases of liens on the collateral; and
- waivers of past defaults under collateral documents.

We may not have the ability to control or direct such actions, even if our rights are adversely affected.

We may be exposed to special risks associated with bankruptcy cases.

One or more of our portfolio companies may be involved in bankruptcy or other reorganization or liquidation proceedings. Many of the events within a bankruptcy case are adversarial and often beyond the control of the creditors. While creditors generally are afforded an opportunity to object to significant actions, we cannot assure you that a bankruptcy court would not approve actions that may be contrary to our interests. There also are instances where creditors can lose their ranking and priority if they are considered to have taken over management of a borrower.

To the extent that portfolio companies in which we have invested through a unitranche facility are involved in bankruptcy proceedings, the outcome of such proceedings may be uncertain. For example, it is unclear whether a bankruptcy court would enforce an agreement among lenders which sets the priority of payments among unitranche lenders. In such a case, the first out lenders in the unitranche facility may not receive the same degree of protection as they would if the agreement among lenders was enforced.

The reorganization of a company can involve substantial legal, professional and administrative costs to a lender and the borrower. It is subject to unpredictable and lengthy delays and during the process a company s competitive position may erode, key management may depart and a company may not be able to invest adequately. In some cases, the debtor company may not be able to reorganize and may be required to liquidate assets. The debt of companies in financial reorganization will, in most cases, not pay current interest, may not accrue interest during reorganization and may be adversely affected by an erosion of the issuer s fundamental value.

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In addition, lenders can be subject to lender liability claims for actions taken by them where they become too involved in the borrower s business or exercise control over the borrower. For example, we could become subject to a lender liability claim (alleging that we misused our influence on the borrower for the benefit of its lenders), if, among other things, the borrower requests significant managerial assistance from us and we provide that assistance. To the extent we and an affiliate both hold investments in the same portfolio company that are of a different character, we may also face restrictions on our ability to become actively involved in the event that portfolio company becomes distressed as a result of the restrictions imposed on transactions involving affiliates under the 1940 Act. In such cases, we may be unable to exercise rights we may otherwise have to protect our interests as security holders in such portfolio company.

If we make subordinated investments, the obligors or the portfolio companies may not generate sufficient cash flow to service their debt obligations to us.

We may make subordinated investments that rank below other obligations of the obligor in right of payment. Subordinated investments are subject to greater risk of default than senior obligations as a result of adverse changes in the financial condition of the obligor or economic conditions in general. If we make a subordinated investment in a portfolio company, the portfolio company may be highly leveraged, and its relatively high debt-to-equity ratio may create increased risks that its operations might not generate sufficient cash flow to service all of its debt obligations.

The disposition of our investments may result in contingent liabilities.

Substantially all of our investments involve loans and private securities. In connection with the disposition of an investment in loans and private securities, we may be required to make representations about the business and financial affairs of the portfolio company typical of those made in connection with the sale of a business. We may also be required to indemnify the purchasers of such investment to the extent that any such representations turn out to be inaccurate or with respect to potential liabilities. These arrangements may result in contingent liabilities that ultimately result in funding obligations that we must satisfy through our return of distributions previously made to us.

We may not realize gains from our equity investments.

When we invest in loans and debt securities, we may acquire warrants or other equity securities of portfolio companies as well. We may also invest in equity securities directly. To the extent we hold equity investments, we will attempt to dispose of them and realize gains upon our disposition of them. However, the equity interests we receive may not appreciate in value and, may decline in value. As a result, we may not be able to realize gains from our equity interests, and any gains that we do realize on the disposition of any equity interests may not be sufficient to offset any other losses we experience.

Changes to United States tariff and import/export regulations may have a negative effect on our portfolio companies and, in turn, harm us.

There has been on-going discussion and commentary regarding potential significant changes to United States trade policies, treaties and tariffs. The current administration, along with Congress, has created significant uncertainty about the future relationship between the United States and other countries with respect to the trade policies, treaties and tariffs. These developments, or the perception that any of them could occur, may have a material adverse effect on global economic conditions and the stability of global financial markets, and may significantly reduce global trade and, in particular, trade between the impacted nations and the United States. Any of these factors could depress economic activity and restrict our portfolio companies access to suppliers or customers and have a material adverse effect on their business, financial condition and results of operations, which in turn would negatively impact us.

Risks Relating to an Offering of Our Securities

We may be unable to invest a significant portion of the net proceeds raised from our offerings on acceptable terms, which would harm our financial condition and operating results.

Delays in investing the net proceeds raised in our offerings may cause our performance to be worse than that of other fully invested BDCs or other lenders or investors pursuing comparable investment strategies. We

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cannot assure you that we will be able to identify any investments that meet our investment objective or that any investment that we make will produce a positive return. We may be unable to invest the net proceeds from any offering on acceptable terms within the time period that we anticipate or at all, which could harm our financial condition and operating results. We anticipate that, depending on market conditions, it may take a substantial period of time to invest substantially all of the net proceeds of any offering in securities meeting our investment objective. During such a period, we will continue to invest the net proceeds of any offering primarily in cash, cash equivalents, U.S. government securities, repurchase agreements and high-quality debt instruments maturing in one year or less from the time of investment, which may produce returns that are significantly lower than the returns which we expect to achieve when our portfolio is fully invested in securities meeting our investment objective, and given our expense ratio and the prevailing interest rate climate, there is a possible risk of losing money on the offering proceeds of certain securities, such as debt securities during this interval. As a result, any distributions that we pay during such period may be substantially lower than the distributions that we may be able to pay when our portfolio is fully invested in securities meeting our investment objective. In addition, until such time as the net proceeds of any offering are invested in securities meeting our investment objective, the market price for our securities may decline. Thus, the return on your investment may be lower than when, if ever, our portfolio is fully invested in securities meeting our investment objective.

There is a risk that you may not receive distributions or that our distributions may not grow over time and a portion of our distributions may be a return of capital.

We intend to make distributions on a monthly basis to our stockholders out of assets legally available for distribution (i.e., not subject to any legal restrictions under Maryland law on the distribution thereof). We cannot assure you that we will achieve investment results that will allow us to make a specified level of cash distributions or year-to-year increases in cash distributions. All distributions will be made at the discretion of our board of directors and will depend on our earnings, financial condition, maintenance of RIC status, compliance with applicable BDC, SBA regulations and such other factors as our board of directors may deem relative from time to time. We cannot assure you that we will make distributions to our stockholders in the future.

Our ability to pay distributions might be adversely affected by the impact of one or more of the risk factors described in this prospectus. Due to the asset coverage test applicable to us under the 1940 Act as a BDC, we may be limited in our ability to make distributions. In addition, restrictions and provisions in our Credit Facility, the Notes and any future credit facilities, as well as in the terms of any debt securities we issue, may limit our ability to make distributions in certain circumstances.

When we make distributions, we will be required to determine the extent to which such distributions are paid out of current or accumulated earnings and profits. Distributions in excess of current and accumulated earnings and profits will be treated as a non-taxable return of capital to the extent of an investor s basis in our stock and, assuming that an investor holds our stock as a capital asset, thereafter as a capital gain. See Material U.S. Federal Income Tax Considerations.

We may allocate the net proceeds from an offering in ways with which you may not agree.

We will have significant flexibility in investing the net proceeds of an offering and may use the net proceeds from an offering in ways with which you may not agree or for purposes other than those contemplated at the time of the offering. In addition, we can provide you with no assurance that by increasing the size of our available equity capital our expense ratio or debt ratio will be lowered.

Stockholders may experience dilution in their ownership percentage if they do not participate in our dividend reinvestment plan.

All distributions declared in cash payable to stockholders that are participants in our dividend reinvestment plan are generally automatically reinvested in shares of our common stock. As a result, stockholders that do not participate in the dividend reinvestment plan may experience dilution over time. Stockholders who receive distributions in shares of common stock may experience accretion to the net asset value of their shares if our shares are trading at a premium and dilution if our shares are trading at a discount.

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The level of accretion or discount would depend on various factors, including the proportion of our stockholders who participate in the plan, the level of premium or discount at which our shares are trading and the amount of the distribution payable to a stockholder.

Existing stockholders may incur dilution if, in the future, we sell shares of our common stock in one or more offerings at prices below the then current net asset value per share of our common stock.

The 1940 Act prohibits us from selling shares of our common stock at a price below the current net asset value per share of such stock, with certain exceptions. One such exception is prior stockholder approval of issuances below net asset value provided that our board of directors makes certain determinations. At our 2017 annual meeting of stockholders, our stockholders voted to allow us to issue common stock at a price below net asset value per share for the period ending on the earlier of the one-year anniversary of the date of the Company s 2017 Annual Meeting of Stockholders and the date of the Company s 2018 Annual Meeting of Stockholders. The proposal approved by our stockholders did not specify a maximum discount below net asset value at which we are able to issue our common stock, although the number of shares sold in each offering may not exceed 25% of our outstanding common stock immediately prior to such sale. We are seeking similar approval at our 2018 Annual Meeting of Stockholders, scheduled for June 28, 2018. If we receive such stockholder approval, any decision to sell shares of our common stock below the then current net asset value per share of our common stock would be subject to the determination by our board of directors that such issuance is in our and our stockholders' best interests.

If we were to sell shares of our common stock below net asset value per share, such sales would result in an immediate dilution to the net asset value per share. This dilution would occur as a result of the sale of shares at a price below the then current net asset value per share of our common stock and a proportionately greater decrease in a stockholder s interest in our earnings and assets and voting interest in us than the increase in our assets resulting from such issuance.

Because the number of shares of common stock that could be so issued and the timing of any issuance is not currently known, the actual dilutive effect cannot be predicted; however, the example below illustrates the effect of dilution to existing stockholders resulting from the sale of common stock at prices below the net asset value of such shares. Please see Sales of Common Stock Below Net Asset Value for a more complete discussion of the potentially dilutive impacts of an offering at a price less than net asset value per share.

Illustration: Example of Dilutive Effect of the Issuance of Shares Below Net Asset Value. Assume that Company XYZ has 16,000,000 total shares outstanding, $370,000,000 in total assets and $220,000,000 in total liabilities. The net asset value per share of the common stock of Company XYZ is $13.75. The following table illustrates the reduction to net asset value, or net asset value, and the dilution experienced by Stockholder A following the sale of 1,600,000 shares of the common stock of Company XYZ at $12.24 per share, a price below its net asset value per share.

	Prior to Sale Below NAV	Following Sale Below NAV	Percentage Change	
Reduction to NAV				
Total Shares Outstanding	16,000,000	17,600,000	10	%
NAV per share	$ 13.75	$ 13.63	-0.9	%
Dilution to Existing Stockholder				
Shares Held by Stockholder A	160,000	160,000(1)	0.0	%

Percentage Held by Stockholder A	1.00	%	0.91	%	-9.0	%
Total Interest of Stockholder A in NAV	$ 2,200,000		$ 2,180,000		-0.9	%

(1) Assumes that Stockholder A does not purchase additional shares in the sale of shares below NAV.

Our shares might trade at premiums that are unsustainable or at discounts from net asset value.

Shares of BDCs like us may, during some periods, trade at prices higher than their net asset value per share and, during other periods, as frequently occurs with closed-end investment companies, trade at prices lower than their net asset value per share. The perceived value of our investment portfolio may be affected by

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a number of factors including perceived prospects for individual companies we invest in, market conditions for common stock generally, for initial public offerings and other exit events for venture capital backed companies, and the mix of companies in our investment portfolio over time. Negative or unforeseen developments affecting the perceived value of companies in our investment portfolio could result in a decline in the trading price of our common stock relative to our net asset value per share.

The possibility that our shares will trade at a discount from net asset value or at premiums that are unsustainable are risks separate and distinct from the risk that our net asset value per share will decrease. The risk of purchasing shares of a BDC that might trade at a discount or unsustainable premium is more pronounced for investors who wish to sell their shares in a relatively short period of time because, for those investors, realization of a gain or loss on their investments is likely to be more dependent upon changes in premium or discount levels than upon increases or decreases in net asset value per share.

Investing in our securities may involve an above average degree of risk.

The investments we make in accordance with our investment objective may result in a higher amount of risk, and higher volatility or loss of principal, than alternative investment options. Our investments in portfolio companies may be speculative and, therefore, an investment in our securities may not be suitable for someone with lower risk tolerance.

The market price of our securities may fluctuate significantly.

The market price and liquidity of the market for our securities may be significantly affected by numerous factors, some of which are beyond our control and may not be directly related to our operating performance. These factors include:

- significant volatility in the market price and trading volume of securities of BDCs or other companies in our sector, which is not necessarily related to the operating performance of these companies;
- changes in regulatory policies or tax guidelines, particularly with respect to RICs, BDCs and SBICs;
- loss of our qualification as a RIC or BDC or the status of our SBIC subsidiary as SBIC;
- changes in earnings or variations in operating results;
- changes in the value of our portfolio of investments;
- changes in accounting guidelines governing valuation of our investments;
- any shortfall in revenue or net income or any increase in losses from levels expected by investors or securities analysts;
- departure of Stellus Capital Management s key personnel;
- operating performance of companies comparable to us; and
- general economic trends and other external factors.

Sales of substantial amounts of our common stock may have an adverse effect on the market price of our common stock.

As of March 31, 2018 we had 15,953,811 shares of common stock outstanding. When effective, our registration statement on Form N-2 will allow us to offer, from time to time, up to $200 million worth of our common stock, preferred stock, subscription rights, debt securities, or warrants representing rights to purchase shares of our common stock, preferred stock or debt securities on terms to be determined at the time of the offering. Sales of substantial amounts of our common stock, or the availability of shares for sale, could adversely affect the prevailing market price of our common stock. If this occurs and continues, it could impair our ability to raise additional capital through the sale of equity securities should we desire to do so.

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If we issue preferred stock and/or debt securities, the net asset value and market value of our common stock may become more volatile.

We cannot assure you that the issuance of preferred stock and/or debt securities would result in a higher yield or return to the holders of our common stock. The issuance of preferred stock and/or debt securities would likely cause the net asset value and market value of our common stock to become more volatile. If the distribution rate on the preferred stock, or the interest rate on the debt securities, were to approach the net rate of return on our investment portfolio, the benefit of leverage to the holders of our common stock would be reduced. If the distribution rate on the preferred stock, or the interest rate on the debt securities, were to exceed the net rate of return on our portfolio, the use of leverage would result in a lower rate of return to the holders of common stock than if we had not issued the preferred stock and/or debt securities. Any decline in the net asset value of our investment would be borne entirely by the holders of our common stock. Therefore, if the market value of our portfolio were to decline, the leverage would result in a greater decrease in net asset value to the holders of our common stock than if we were not leveraged through the issuance of preferred stock and/or debt securities. This decline in net asset value would also tend to cause a greater decline in the market price for our common stock.

There is also a risk that, in the event of a sharp decline in the value of our net assets, we would be in danger of failing to maintain required asset coverage ratios which may be required by the preferred stock and/or debt securities or of a downgrade in the ratings of the preferred stock and/or debt securities or our current investment income might not be sufficient to meet the distribution requirements on the preferred stock or the interest payments on the debt securities. In order to counteract such an event, we might need to liquidate investments in order to fund redemption of some or all of the preferred stock and/or debt securities. In addition, we would pay (and the holders of our common stock would bear) all costs and expenses relating to the issuance and ongoing maintenance of the preferred stock and/or debt securities. Holders of preferred stock and/or debt securities may have different interests than holders of common stock and may at times have disproportionate influence over our affairs.

The trading market or market value of our debt securities or any convertible debt securities, if issued to the public, may be volatile.

Our debt securities or any convertible debt securities, if issued to the public, may or may not have an established trading market. We cannot assure investors that a trading market for our debt securities or any convertible debt securities, if issued to the public, would develop or be maintained if developed. In addition to our creditworthiness, many factors may materially adversely affect the trading market for, and market value of, our publicly issued debt securities or any convertible debt securities. These factors include, but are not limited to, the following:

- the time remaining to the maturity of these debt securities;
- the outstanding principal amount of debt securities with terms identical to these debt securities;
- the general economic environment;
- the supply of debt securities trading in the secondary market, if any;
- the redemption, repayment or convertible features, if any, of these debt securities;
- the level, direction and volatility of market interest rates generally; and
- market rates of interest higher or lower than rates borne by the debt securities.

There also may be a limited number of buyers for our debt securities. This too may materially adversely affect the market value of the debt securities or the trading market for the debt securities. Our debt securities may include convertible features that cause them to more closely bear risks associated with an investment in our common stock.

Terms relating to redemption may materially adversely affect the return on any debt securities.

If we issue any debt securities or any convertible debt securities that are redeemable at our option, we may choose to redeem the debt securities at times when prevailing interest rates are lower than the interest

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rate paid on the debt securities. In addition, if the debt securities are subject to mandatory redemption, we may be required to redeem the debt securities at times when prevailing interest rates are lower than the interest rate paid on the debt securities. In this circumstance, a holder of our debt securities may not be able to reinvest the redemption proceeds in a comparable security at an effective interest rate as high as the debt securities being redeemed.

The issuance of subscription rights, warrants or convertible debt that are exchangeable for our common stock, will cause your interest in us to be diluted as a result of any such rights, warrants or convertible debt offering.

Stockholders who do not fully exercise rights, warrants or convertible debt issued to them in any offering of subscription rights, warrants or convertible debt to purchase our common stock should expect that they will, at the completion of the offering, own a smaller proportional interest in us than would otherwise be the case if they fully exercised their rights, warrants or convertible debt. We cannot state precisely the amount of any such dilution in share ownership because we do not know what proportion of the common stock would be purchased as a result of any such offering.

In addition, if the subscription price, warrant price or convertible debt price is less than our net asset value per share of common stock at the time of such offering, then our stockholders would experience an immediate dilution of the aggregate net asset value of their shares as a result of the offering. The amount of any such decrease in net asset value is not predictable because it is not known at this time what the subscription price, warrant price, convertible debt price or net asset value per share will be on the expiration date of such offering or what proportion of our common stock will be purchased as a result of any such offering. The risk of dilution is greater if there are multiple rights offerings. However, our board of directors will make a good faith determination that any offering of subscription rights, warrants or convertible debt would result in a net benefit to existing stockholders.

Future offerings of debt securities, which would be senior to our common stock upon liquidation, or equity securities, which could dilute our existing stockholders and may be senior to our common stock for the purposes of distributions, may harm the value of our common stock.

In the future, we may attempt to increase our capital resources by making offerings of debt or equity securities, including commercial paper, medium-term notes, senior or subordinated notes and classes of preferred stock or common stock, subject to the restrictions of the 1940 Act. Upon a liquidation of our company, holders of our debt securities and shares of preferred stock and lenders with respect to other borrowings would receive a distribution of our available assets prior to the holders of our common stock. Additional equity offerings by us may dilute the holdings of our existing stockholders or reduce the value of our common stock, or both. Any preferred stock we may issue would have a preference on distributions that could limit our ability to make distributions to the holders of our common stock. Because our decision to issue securities in any future offering will depend on market conditions and other factors beyond our control, we cannot predict or estimate the amount, timing or nature of our future offerings. Thus, our stockholders bear the risk of our future offerings reducing the market price of our common stock and diluting their stock holdings in us. In addition, proceeds from a sale of common stock will likely be used to increase our total assets or to pay down our borrowings, among other uses. This would increase our asset coverage ratio and permit us to incur additional leverage under rules pertaining to business development companies by increasing our borrowings or issuing senior securities such as preferred stock or additional debt securities.

Future offerings of debt securities, which would be senior to our commonstock upon liquidation, or equity securities,

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements in this prospectus and the accompanying prospectus supplement, if any constitute forward-looking statements, which relate to future events or our future performance or financial condition. The forward-looking statements contained in this prospectus and the accompanying prospectus supplement, if any involve risks and uncertainties, including statements as to:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the effect of investments that we expect to make;
- our contractual arrangements and relationships with third parties;
- actual and potential conflicts of interest with Stellus Capital Management;
- the dependence of our future success on the general economy and its effect on the industries in which we invest;
- the ability of our portfolio companies to achieve their objectives;
- the use of borrowed money to finance a portion of our investments;
- the adequacy of our financing sources and working capital;
- the timing of cash flows, if any, from the operations of our portfolio companies;
- the ability of Stellus Capital Management to locate suitable investments for us and to monitor and administer our investments;
- the ability of Stellus Capital Management to attract and retain highly talented professionals;
- our ability to qualify and maintain our qualification as a RIC and as a BDC; and
- the effect of future changes in laws or regulations (including the interpretation of these laws and regulations by regulatory authorities) and conditions in our operating areas, particularly with respect to business development companies or RICs.

Such forward-looking statements may include statements preceded by, followed by or that otherwise include the words may, might, will, intend, should, could, can, would, expect, believe, estimate, anticipa or similar words.

We have based the forward-looking statements included in this prospectus and the accompanying prospectus supplement, if any on information available to us on the date of this prospectus and the accompanying prospectus supplement, if any, and we assume no obligation to update any such forward-looking statements. Actual results could differ materially from those anticipated in our forward-looking statements, and future results could differ materially from historical performance. We undertake no obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by law or SEC rule or regulation. You are advised to consult any additional disclosures that we may make directly to you, including in the form of a prospectus supplement or post-effective amendment to the registration statement to which this prospectus relates, or through reports that we in the future may file with the SEC, including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K.

You should understand that, under Sections 27A(b)(2)(B) of the Securities Act and Section 21E(b)(2)B of the Exchange Act, the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 do not apply to statements made in connection with any offering of securities pursuant to this prospectus and the accompanying prospectus supplement, if any.

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USE OF PROCEEDS

Unless otherwise specified in any prospectus supplement accompanying this prospectus, we intend to use the net proceeds of this offering, to make new investments in portfolio companies in accordance with our investment objective and strategies as described in this prospectus, to reduce a portion of our outstanding borrowings under the Credit Facility or the Notes and for general working capital purposes. Pending such use, we will invest the net proceeds primarily in high quality, short-term debt securities consistent with our BDC election and our election to be taxed as a RIC. We do not intend to use any portion of the net proceeds of this offering to fund distributions to our shareholders.

We estimate that it will take less than six months for us to substantially invest the net proceeds of any offering made pursuant to this prospectus, depending on the availability of attractive opportunities, market conditions and the amount raised. However, we can offer no assurance that we will be able to achieve this goal.

Proceeds not immediately used for new investments or the temporary repayment of debt will be invested primarily in cash, cash equivalents, U.S. government securities and other high-quality investments that mature in one year or less from the date of investment. These securities may have lower yields than the types of investments we would typically make in accordance with our investment objective and, accordingly, may result in lower distributions, if any, during such period.

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PRICE RANGE OF COMMON STOCK AND DISTRIBUTIONS

Our common stock is traded on the New York Stock Exchange, or NYSE, under the symbol SCM. In connection with our initial public offering, our shares of common stock began trading on November 8, 2012, and before that date, there was no established trading market for our common stock.

The following table sets forth, for each fiscal quarter of the two most recent fiscal years and most recent interim period, the range of high and low closing prices of our common stock as reported on the NYSE, the sales price as a percentage of our net asset value, or NAV, and the dividends declared by us.

Fiscal Year Ended	NAV Per Share(1)	Closing Sales Price(2) High	Closing Sales Price(2) Low	Premium or Discount of High Sales to NAV(3)		Premium or Discount of Low Sales to NAV(3)	
December 31, 2018							
Second Quarter (through June 25, 2018)	*	$ 13.60	$ 11.56		*		*
First Quarter	$ 13.93	$ 13.00	$ 11.34	-6.68	%	-18.59	%
December 31, 2017							
Fourth Quarter	$ 13.81	$ 14.29	$ 12.19	3.48	%	-11.73	%
Third Quarter	$ 13.85	$ 13.85	$ 13.30			3.97	%
Second Quarter	$ 13.81	$ 14.55	$ 13.25	5.36	%	4.05	%
First Quarter	$ 13.84	$ 14.57	$ 12.09	5.27	%	-12.64	%
December 31, 2016							
Fourth Quarter	13.69	$ 12.33	$ 10.35	-9.93	%	-24.40	%
Third Quarter	$ 13.57	$ 11.54	$ 10.35	-14.96	%	-23.73	%
Second Quarter	$ 13.12	$ 10.59	$ 9.82	-19.28	%	-25.15	%
First Quarter	$ 13.06	$ 10.22	$ 7.85	-21.75	%	-39.89	%

(1) NAV is determined as of the last date in the relevant quarter and therefore may not reflect the NAV per share on the date of the high and low sales prices. The NAVs shown are based on outstanding shares at the end of each period.

(2) Closing sales price is determined as the high or low closing sales price noted within the respective quarter, not adjusted for dividends.

(3) Calculated as of the respective high or low sales price divided by the quarter end NAV.

* Not determinable at the time of filing.

On June 25, 2018, the last reported sales price of our common stock was $13.22 per share. As of June 25, 2018, we had 10 stockholders of record, which did not include stockholders for whom shares are held in nominee or street name.

Shares of business development companies may trade at a market price that is less than the value of the net assets attributable to those shares. The possibility that our shares of common stock will trade at a discount from net asset value or at premiums that are unsustainable over the long term are separate and distinct from the risk that our net asset value will decrease. Since they began trading on November 8, 2012, in connection with our initial public offering, our shares of common stock have traded at times at a discount to the net assets attributable to those shares.

To the extent that we have income available, we intend to make quarterly distributions to our stockholders. Our quarterly stockholder distributions, if any, will be determined by our board of directors. Any stockholder distribution to our stockholders will be declared out of assets legally available for distribution.

We have elected to be treated as a RIC under the Code. To maintain RIC tax treatment, we must distribute at least 90% of our net ordinary income and net short-term capital gains in excess of our net long-term capital losses, if any, to our stockholders. In order to avoid certain excise taxes imposed on RICs, we currently intend to distribute during each calendar year an amount at least equal to the sum of: (a) 98% of our net ordinary income for such calendar year; (b) 98.2% of our capital gain net income for the one-year period ending on October 31 of the calendar year; and (c) any net ordinary income and capital gain net income for preceding years that were not distributed during such years and on which we previously paid no U.S. federal income tax.

We currently intend to distribute net capital gains (*i.e.*, net long-term capital gains in excess of net short-term capital losses), if any, at least annually out of the assets legally available for such distributions. However, we may decide in the future to retain such capital gains for investment and elect to treat such gains as deemed distributions to you. If this happens, you will be treated for U.S. federal income tax purposes as if you had received an actual distribution of the capital gains that we retain and reinvested the net after tax proceeds in us. In this situation, you would be eligible to claim a tax credit (or in certain circumstances a tax refund) equal to your allocable share of the tax we paid on the capital gains deemed distributed to you. See Material U.S. Federal Income Tax Considerations. We cannot assure you that we will achieve results that will permit us to pay any cash distributions, and if we issue senior securities, we may be prohibited from making distributions if doing so would cause us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or if such distributions are limited by the terms of any of our borrowings.

We have adopted an opt out dividend reinvestment plan for our common stockholders. Unless you elect to receive your distributions in cash, we intend to make such distributions in additional shares of our common stock under our dividend reinvestment plan. Although distributions paid in the form of additional shares of our common stock will generally be subject to U.S. federal, state and local taxes in the same manner as cash distributions, investors participating in our dividend reinvestment plan will not receive any corresponding cash distributions with which to pay any such applicable taxes. If you hold shares of our common stock in the name of a broker or financial intermediary, you should contact such broker or financial intermediary regarding your election to receive distributions in cash in lieu of shares of our common stock. Any distributions reinvested through the issuance of shares through our dividend reinvestment plan will increase our gross assets on which the base management fee and the incentive fee are determined and paid to Stellus Capital Management. See Dividend Reinvestment Plan.

Date Declared	Record Date	Payment Date	Per Share
Fiscal 2012			
December 7, 2012	December 21, 2012	December 27, 2012	$ 0.1812
Fiscal 2013(1)			
various	various	various	$ 1.3600
Fiscal 2014(2)(3)			
various	various	various	$ 1.4246
Fiscal 2015(2)			
various	various	various	$ 1.3596
Fiscal 2016(2)			
various	various	various	$ 1.3596
Fiscal 2017(2)			
January 13, 2017	January 31, 2017	February 15, 2017	$ 0.1133
January 13, 2017	February 28, 2017	March 15, 2017	$ 0.1133
January 13, 2017	March 31, 2017	April 14, 2017	$ 0.1133
April 14, 2017	April 28, 2017	May 15, 2017	$ 0.1133
April 14, 2017	May 31, 2017	June 15, 2017	$ 0.1133
April 14, 2017	June 30, 2017	July 14, 2017	$ 0.1133
July 7, 2017	July 31, 2017	August 15, 2017	$ 0.1133
July 7, 2017	August 31, 2017	September 15, 2017	$ 0.1133
July 7, 2017	September 29, 2017	October 13, 2017	$ 0.1133

October 12, 2017	October 31, 2017	November 15, 2017	$ 0.1133
October 12, 2017	November 30, 2017	December 15, 2017	$ 0.1133
October 12, 2017	December 29, 2017	January 12, 2018	$ 0.1133

Date Declared	Record Date	Payment Date	Per Share
Fiscal 2018[(2)]			
January 11, 2018	January 31, 2018	February 15, 2018	$ 0.1133
January 11, 2018	February 28, 2018	March 15, 2018	$ 0.1133
January 11, 2018	March 29, 2018	April 13, 2018	$ 0.1133
April 16, 2018	April 30, 2018	May 15, 2018	$ 0.1133
April 16, 2018	May 31, 2018	June 15, 2018	$ 0.1133
April 16, 2018	June 29, 2018	July 13, 2018	$ 0.1133
Total			$ 7.7244

(1) Distributions made quarterly

(2) Distributions made monthly

(3) Includes special distribution of $0.065 per share in addition to monthly distributions

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RATIOS OF EARNINGS TO FIXED CHARGES

The following table contains our ratio of earnings to fixed charges for the periods indicated, computed as set forth below. You should read these ratios of earnings to fixed charges in connection with our Consolidated Financial Statements, including the notes to those statements, included in this prospectus.

	For the three months ended March 31, 2018	For the Year Ended December 31, 2017	For the Year Ended December 31, 2016	For the Year Ended December 31, 2015	For the Year Ended December 31, 2014	For the Year Ended December 31, 2013
Earnings to Fixed Charges(1)	4.0	3.9	4.0	2.2	2.8	6.6

(1) Earnings include net realized and unrealized gains or losses. Net realized and unrealized gains or losses can vary substantially from period to period.

For purposes of computing the ratios of earnings to fixed charges, earnings represent net increase in net assets resulting from operations plus (or minus) income tax expense (benefit) including excise tax expense plus fixed charges. Fixed charges include interest and credit facility fees expense and amortization of debt issuance costs.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

We were organized as a Maryland corporation on May 18, 2012, and formally commenced operations on November 7, 2012. Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation through debt and related equity investments in middle-market companies.

We are an externally managed, non-diversified, closed-end investment company that has elected to be regulated as a BDC under the 1940 Act. Our investment activities are managed by our investment advisor, Stellus Capital Management, LLC (Stellus Capital or the Advisor).

As a BDC, we are required to comply with certain regulatory requirements. For instance, as a BDC, we may not acquire any assets other than qualifying assets specified in the 1940 Act unless, at the time the acquisition is made, at least 70% of our total assets are qualifying assets. Qualifying assets include investments in eligible portfolio companies. Under the relevant SEC rules, the term eligible portfolio company includes private operating companies, operating companies whose securities are not listed on a national securities exchange, and certain public operating companies that have listed their securities on a national securities exchange and have a market capitalization of less than $250 million, in each case organized and with their principal of business in the United States.

We have elected to be treated for U.S. federal tax purposes as a RIC under Subchapter M of the Code. To maintain our qualification as a RIC, we must, among other things, meet certain source-of-income and asset diversification requirements. As of March 31, 2018, we were in compliance with the RIC requirements. As a RIC, we generally will not have to pay corporate-level U.S. federal income taxes on any income we distribute to our stockholders.

Portfolio Composition and Investment Activity

Portfolio Composition

We originate and invest primarily in privately-held middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA (earnings before interest, taxes, depreciation and amortization)) through first lien, second lien, unitranche and mezzanine debt financing, often times with a corresponding equity investment.

As of March 31, 2018, we had $431.3 million (at fair value) invested in 52 portfolio companies. As of March 31, 2018, our portfolio included approximately 46% of first lien debt, 41% of second lien debt, 6% of mezzanine debt and 6% of equity investments at fair value. The composition of our investments at cost and fair value as of March 31, 2018 was as follows:

	Cost	Fair Value
Senior Secured First Lien[1]	$ 198,445,230	$ 199,372,307
Senior Secured Second Lien	180,292,855	177,644,589

Unsecured Debt	27,147,168	26,732,823
Equity	20,494,618	27,550,001
Total Investments	$ 426,379,871	$ 431,299,720

(1) Includes unitranche investments, which account for 16.1% of our portfolio at fair value.

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As of December 31, 2017, we had $371.8 million (at fair value) invested in 48 portfolio companies. As of December 31, 2017, our portfolio included approximately 38% of first lien debt, 48% of second lien debt, 7% of mezzanine debt and 7% of equity investments at fair value. The composition of our investments at cost and fair value as of December 31, 2017 was as follows:

		Cost	Fair Value
Senior Secured	First Lien(1)	$ 140,915,106	$ 141,006,923
Senior Secured	Second Lien	181,164,730	178,432,850
Unsecured Debt		27,903,141	27,430,000
Equity		18,470,229	24,969,999
Total Investments		$ 368,453,206	$ 371,839,772

(1) Includes unitranche investments, which account for 13.2% of our portfolio at fair value.

Our investment portfolio may contain loans that are in the form of lines of credit or revolving credit facilities, which require us to provide funding when requested by portfolio companies in accordance with the terms and conditions of the underlying loan agreements. As of March 31, 2018 and December 31, 2017, we had six and four such investments, respectively, with aggregate unfunded commitments of $11.2 million and $8.7 million, respectively. As of March 31, 2018, the Company had sufficient liquidity to fund such unfunded commitments should the need arise.

The following is a summary of geographical concentration of our investment portfolio as of March 31, 2018:

	Cost	Fair Value	% of Total Investments
Texas	$ 111,024,052	$ 110,713,387	25.67 %
California	45,368,765	45,800,000	10.62 %
New Jersey	34,281,271	34,319,692	7.96 %
New York	28,581,847	28,913,750	6.70 %
Canada	26,340,678	26,641,739	6.18 %
Illinois	24,256,766	25,580,000	5.93 %
Arizona	21,414,850	22,190,812	5.15 %
Massachusetts	22,552,094	22,187,850	5.14 %
Ohio	21,660,379	21,760,000	5.05 %
South Carolina	21,100,842	21,090,000	4.89 %
Arkansas	15,364,791	15,678,106	3.64 %
North Carolina	11,841,982	12,032,500	2.79 %
Tennessee	9,854,786	10,000,000	2.32 %
Georgia	5,981,496	8,650,000	2.01 %
Pennsylvania	7,855,929	8,010,938	1.86 %
Minnesota	5,130,946	5,130,946	1.19 %
Puerto Rico	8,842,160	5,080,000	1.18 %
Alabama	1,206,682	3,300,000	0.77 %
Washington	2,132,745	2,560,000	0.59 %
Utah	1,294,505	880,000	0.20 %
Florida	242,304	380,000	0.09 %
Missouri		300,000	0.07 %

Virginia	50,001	100,000	0.02	%
	$ 426,379,871	$ 431,299,720	100.00	%

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The following is a summary of geographical concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Texas	$ 109,043,496	$ 108,445,000	29.16	%
New Jersey	34,531,876	34,595,527	9.30	%
New York	28,939,268	29,365,000	7.90	%
Canada	26,315,677	26,440,000	7.11	%
California	25,519,753	25,930,000	6.97	%
Illinois	24,250,169	25,700,000	6.91	%
Massachusetts	22,534,191	22,247,850	5.98	%
Arizona	13,565,958	13,840,000	3.72	%
North Carolina	12,248,770	12,499,167	3.36	%
Ohio	10,112,627	9,990,000	2.69	%
Tennessee	9,848,614	9,950,000	2.68	%
Missouri	9,152,087	9,530,000	2.56	%
Georgia	5,929,223	8,329,998	2.24	%
Pennsylvania	7,848,470	8,058,746	2.17	%
Arkansas	7,397,881	7,618,484	2.05	%
Minnesota	5,421,770	5,420,000	1.46	%
Puerto Rico	8,827,864	5,080,000	1.37	%
Washington	4,172,743	4,520,000	1.22	%
Alabama	1,206,682	2,880,000	0.77	%
Utah	1,293,782	880,000	0.24	%
Florida	242,304	420,000	0.11	%
Virginia	50,001	100,000	0.03	%
	$ 368,453,206	$ 371,839,772	100.00	%

The following is a summary of industry concentration of our investment portfolio as of March 31, 2018:

	Cost	Fair Value	% of Total Investments	
Software	$ 46,552,172	$ 47,127,850	10.93	%
Healthcare & Pharmaceuticals	48,406,241	45,493,446	10.55	%
Services: Business	34,916,431	37,560,001	8.71	%
Finance	36,356,619	37,510,000	8.70	%
High Tech Industries	36,089,266	35,810,000	8.30	%
Retail	29,289,480	29,278,638	6.79	%
Consumer Goods: Durable	24,556,850	24,778,106	5.74	%
Capital Equipment	24,346,104	24,580,000	5.70	%
Media: Broadcasting & Subscription	21,616,409	24,053,750	5.58	%
Services: Consumer	17,681,579	18,010,000	4.18	%
Construction & Building	17,926,928	17,780,000	4.12	%
Automotive	17,410,929	17,570,938	4.07	%
Education	17,043,239	17,171,053	3.98	%
Consumer goods: non-durable	13,229,563	13,220,000	3.07	%
Chemicals, Plastics, & Rubber	11,683,058	12,065,000	2.80	%

Energy: Oil & Gas	9,040,642	9,068,387	2.10	%
Transportation: Cargo	6,791,312	6,841,739	1.59	%
Insurance	5,413,835	5,510,000	1.28	%
Beverage, Food, & Tobacco	3,967,191	3,600,000	0.83	%
Hotel, Gaming, & Leisure	3,245,580	3,400,812	0.79	%
Environmental Industries	766,442	770,000	0.18	%
Services: Government	50,001	100,000	0.02	%
	$ 426,379,871	$ 431,299,720	100.00	%

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The following is a summary of industry concentration of our investment portfolio as of December 31, 2017:

	Cost	Fair Value	% of Total Investments	
Software	$ 48,560,675	$ 48,997,850	13.18	%
Healthcare & Pharmaceuticals	41,192,879	37,829,167	10.17	%
High Tech Industries	36,058,477	35,460,000	9.54	%
Finance	26,500,097	28,330,000	7.62	%
Services: Business	23,386,714	25,749,999	6.93	%
Capital Equipment	24,300,027	24,170,000	6.50	%
Media: Broadcasting & Subscription	21,680,239	23,665,000	6.36	%
Chemicals, Plastics, & Rubber	20,825,458	21,145,000	5.69	%
Services: Consumer	17,862,616	18,070,000	4.86	%
Construction & Building	17,913,413	17,980,000	4.84	%
Education	17,197,396	17,335,526	4.66	%
Consumer Goods: Durable	16,559,947	16,798,484	4.52	%
Consumer goods: non-durable	13,250,000	13,250,000	3.56	%
Retail	8,288,083	8,280,000	2.23	%
Automotive	7,848,470	8,058,746	2.17	%
Transportation: Cargo	6,785,894	6,840,000	1.84	%
Energy: Oil & Gas	6,766,968	6,700,000	1.80	%
Insurance	5,410,226	5,500,000	1.48	%
Beverage, Food, & Tobacco	3,964,242	3,580,000	0.96	%
Hotel, Gaming, & Leisure	3,284,942	3,420,000	0.92	%
Environmental Industries	766,442	580,000	0.16	%
Services: Government	50,001	100,000	0.03	%
	$ 368,453,206	371,839,772	100.00	%

At March 31, 2018, our average portfolio company investment at amortized cost and fair value was approximately $8.2 million and $8.3 million, respectively, and our largest portfolio company investment at amortized cost and fair value was approximately $22.6 million and $22.2 million, respectively. At December 31, 2017, our average portfolio company investment at amortized cost and fair value was approximately $7.7 million and $7.4 million, respectively, and our largest portfolio company investment at amortized cost and fair value was approximately $22.5 million and $22.2 million, respectively.

At March 31, 2018, 89% of our debt investments bore interest based on floating rates (subject to interest rate floors), such as LIBOR, and 11% bore interest at fixed rates. At December 31, 2017, 87% of our debt investments bore interest based on floating rates (subject to interest rate floors), such as LIBOR, and 13% bore interest at fixed rates.

The weighted average yield on all of our debt investments as of March 31, 2018 and December 31, 2017 was 11.1% and 10.8%, respectively. The weighted average yield was computed using the effective interest rates for all of our debt investments, including accretion of original issue discount. The weighted average yield of our debt investments is not the same as a return on investment for our stockholder, but, rather relates to a portion of our investment portfolio and is calculated before the payment of all of our subsidiaries fees and expenses.

As of March 31, 2018 and December 31, 2017, we had cash and cash equivalents of $45.5 million and $25.1 million, respectively.

Investment Activity

During the three months ended March 31, 2018, we made an aggregate of $71.7 million of investments in four new portfolio companies and four existing portfolio companies. During the three months ended March 31, 2018, we received an aggregate of $15.6 million in proceeds from repayments of our investments.

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Our level of investment activity can vary substantially from period to period depending on many factors, including the amount of debt and equity capital required by middle-market companies, the level of merger and acquisition activity, the general economic environment and the competitive environment for the types of investments we make.

Asset Quality

In addition to various risk management and monitoring tools, Stellus Capital uses an investment rating system to characterize and monitor the credit profile and expected level of returns on each investment in our investment portfolio. This investment rating system uses a five-level numeric scale. The following is a description of the conditions associated with each investment category:

Investment Category 1 is used for investments that are performing above expectations, and whose risks remain favorable compared to the expected risk at the time of the original investment.
Investment Category 2 is used for investments that are performing within expectations and whose risks remain neutral compared to the expected risk at the time of the original investment. All new loans are initially rated 2.
Investment Category 3 is used for investments that are performing below expectations and that require closer monitoring, but where no loss of return or principal is expected. Portfolio companies with a rating of 3 may be out of compliance with financial covenants.
Investment Category 4 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are often in work out. Investments with a rating of 4 are those for which some loss of return but no loss of principal is expected.
Investment Category 5 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are almost always in work out. Investments with a rating of 5 are those for which some loss of return and principal is expected.

Investment Category	As of March 31, 2018 (dollars in millions) Fair Value	% of Total Portfolio		Number of Portfolio Companies[1]	As of December 31, 2017 (dollars in millions) Fair Value	% of Total Portfolio		Number of Portfolio Companies
1	$ 21.3	5	%	8	$ 25.9	7	%	5
2	372.5	86	%	37	306.7	82	%	36
3	36.5	9	%	5	37.0	10	%	5
4	1.0		%	2	1.9	1	%	1
5			%	1	0.4		%	1
Total	$ 431.3	100	%	53	$ 371.9	100	%	48

(1) One portfolio company appears in two categories as of March 31, 2018

Loans and Debt Securities on Non-Accrual Status

We will not accrue interest on loans and debt securities if we have reason to doubt our ability to collect such interest. As of March 31, 2018, we had two loans on non-accrual status which represented approximately 1.0% of our loan portfolio at cost and 0.2% at fair value. As of December 31, 2017, we had two loans on non-accrual status, which represented approximately 1.2% of our loan portfolio at cost and 0.3% at fair value.

Results of Operations

An important measure of our financial performance is net increase (decrease) in net assets resulting from operations, which includes net investment income (loss), net realized gain (loss) and net unrealized appreciation (depreciation). Net investment income (loss) is the difference between our income from interest, dividends, fees and other investment income and our operating expenses including interest on borrowed funds.

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Net realized gain (loss) on investments is the difference between the proceeds received from dispositions of portfolio investments and their amortized cost. Net unrealized appreciation (depreciation) on investments is the net change in the fair value of our investment portfolio.

Comparison of the three months ended March 31, 2018 and 2017

Revenues

We generate revenue in the form of interest income on debt investments and capital gains and distributions, if any, on investment securities that we may acquire in portfolio companies. Our debt investments typically have a term of five to seven years and bear interest at a fixed or floating rate. Interest on our debt securities is generally payable quarterly. Payments of principal on our debt investments may be amortized over the stated term of the investment, deferred for several years or due entirely at maturity. In some cases, our debt investments may pay interest in-kind, or PIK. Any outstanding principal amount of our debt securities and any accrued but unpaid interest will generally become due at the maturity date. The level of interest income we receive is directly related to the balance of interest-bearing investments multiplied by the weighted average yield of our investments. We expect that the total dollar amount of interest and any dividend income that we earn will increase as the size of our investment portfolio increases. In addition, we may generate revenue in the form of prepayment fees, commitment, loan origination, structuring or due diligence fees, fees for providing significant managerial assistance and consulting fees.

The following shows the breakdown of investment income for the three months ended March 31, 2018 and 2017 (in millions).

	Three months ended March 31, 2018	Three months ended March 31, 2017
Interest income	$ 10.5	$ 9.4
PIK Interest	0.2	0.1
Miscellaneous fees	0.2	0.4
Total	$ 10.9	$ 9.9

The increase in interest income from the respective periods was due to the growth in the overall investment portfolio.

Expenses

Our primary operating expenses include the payment of fees to Stellus Capital under the investment advisory agreement, our allocable portion of overhead expenses under the administration agreement and other operating costs described below. We bear all other out-of-pocket costs and expenses of our operations and transactions, which may include:

organization and offering expenses;

Expenses incurred in valuing our assets and calculating our net asset value (including the cost and expenses of any independent valuation firm);

fees and expenses incurred by Stellus Capital or payable to third parties, including agents, consultants or other advisors, in monitoring financial and legal affairs for us and in monitoring our investments and performing due diligence on our prospective portfolio companies or otherwise relating to, or associated with, evaluating and making investments;

interest payable on debt, if any, incurred to finance our investments and expenses related to unsuccessful portfolio acquisition efforts;

offerings of our common stock and other securities;

base management and incentive fees;

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administration fees and expenses, if any, payable under the administration agreement (including our allocable portion of Stellus Capital s overhead in performing its obligations under the administration agreement, including rent and the allocable portion of the cost of our chief compliance officer, chief financial officer and their respective staffs);
transfer agent and custodial fees and expenses;
U.S. federal and state registration fees;
all costs of registration and listing our shares on any securities exchange;
U.S. federal, state and local taxes;
independent directors fees and expenses;
costs of preparing and filing reports or other documents required by the SEC or other regulators;
costs of any reports, proxy statements or other notices to stockholders, including printing costs;
costs associated with individual or group stockholders;
costs and fees associated with any fidelity bond, directors and officers/errors and omissions liability insurance, and any other insurance premiums;
direct costs and expenses of administration and operation, including printing, mailing, long distance telephone, copying, secretarial and other staff, independent auditors and outside legal costs; and
all other expenses incurred by us or Stellus Capital in connection with administering our business.
The following shows the breakdown of operating expenses for the three months ended March 31, 2018 and 2017 (in millions).

	Three months ended March 31, 2018	Three months ended March 31, 2017
Operating Expenses		
Management fees	$ 1.7	$ 1.6
Valuation Fees	0.1	0.2
Administrative services expenses	0.3	0.3
Incentive fees	1.0	1.0
Professional fees	0.5	0.2
Directors fees	0.1	0.1
Insurance expense	0.1	0.1
Interest expense and other fees	2.5	2.1
Other general and administrative	0.1	0.1
Total Operating Expenses	$ 6.4	$ 5.7

The increase in operating expenses for the respective periods was primarily due to 1) an increase in management fees, directly related to the growth of our portfolio, 2) increased interest expense due to our additional 2022 Notes and SBA-guaranteed debentures outstanding during the period, and 3) an increase in professional fees, primarily related to increased costs of Sarbanes-Oxley compliance.

Net Investment Income

For the three months ended March 31, 2018, net investment income was $4.5 million, or $0.28 per common share (based on 15,952,841 weighted-average common shares outstanding at March 31, 2018).

For the three months ended March 31, 2017, net investment income was $4.1 million, or $0.33 per common share (based on 12,479,957 weighted-average common shares outstanding at March 31, 2017).

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Net Realized Gains and Losses

We measure realized gains or losses by the difference between the net proceeds from the repayment, sale or disposition and the amortized cost basis of the investment, using the specific identification method, without regard to unrealized appreciation or depreciation previously recognized.

Repayments of investments and amortization of other investments and a non-cash conversion of debt to equity for the three months ended March 31, 2018 totaled $15.6 million and net realized gain totaled $1.3 million.

Repayments of investments and amortization of other investments for the three months ended March 31, 2017 totaled $39.3 million and net realized loss totaled $0.8 million.

Net Change in Unrealized Appreciation/(Depreciation) of Investments

Net change in unrealized appreciation (depreciation) primarily reflects the change in portfolio investment values during the reporting period, including the reversal of previously recorded appreciation or depreciation when gains or losses are realized.

Net change in unrealized appreciation on investments and cash equivalents for the three months ended March 31, 2018 and 2017 totaled $1.5 million and $2.6 million, respectively.

The net change in unrealized appreciation between the respective periods was due to a general tightening of credit spreads. The quarter ending March 31, 2018 did not have as significant of a reversal of previously recorded depreciation as was experienced in the quarter ending March 31, 2017 when one of our debt investments converted into equity.

Provision for Taxes on Unrealized Appreciation on Investments

We have direct wholly owned subsidiaries that have elected to be taxable entities (the Taxable Subsidiaries). The Taxable Subsidiaries permit us to hold equity investments in portfolio companies which are pass through entities for tax purposes and continue to comply with the source income requirements contained in RIC tax provisions of the Code. The Taxable Subsidiaries are not consolidated with us for income tax purposes and may generate income tax expense, benefit, and the related tax assets and liabilities, as a result of their ownership of certain portfolio investments. The income tax expense, or benefit, if any, and related tax assets and liabilities are reflected in our consolidated financial statements. For the three months ended March 31, 2018 and 2017, we recognized a benefit for income tax on unrealized investments of $0 and $8.0 thousand for the Taxable Subsidiaries, respectively. As of March 31, 2018 and December 31, 2017, there was no deferred tax liability or asset on the Consolidated Statement of Assets and Liabilities.

Net Increase in Net Assets Resulting from Operations

For the three months ended March 31, 2018, net increase in net assets resulting from operations totaled $7.3 million, or $0.46 per common share (based on 15,952,841 weighted-average common shares outstanding at March 31, 2018).

For the three months ended March 31, 2017, net increase in net assets resulting from operations totaled $6.0 million, or $0.48 per common share (based on 12,479,957 weighted-average common shares outstanding at March 31, 2017).

The increase in the net increase in net assets between the respective periods was due a higher net investment income during the three months ended March 31, 2018, as well as a realized gain during the period.

Comparison of the Years ended December 31, 2017, 2016, and 2015

Revenues

We generate revenue in the form of interest income on debt investments and capital gains and distributions, if any, on investment securities that we may acquire in portfolio companies. Our debt investments typically have a term of five to seven years and bear interest at a fixed or floating rate. Interest on our debt securities is generally payable quarterly. Payments of principal on our debt investments may be amortized over the stated term of the investment, deferred for several years or due entirely at maturity. In

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some cases, our debt investments may pay interest in-kind, or PIK. Any outstanding principal amount of our debt securities and any accrued but unpaid interest will generally become due at the maturity date. The level of interest income we receive is directly related to the balance of interest-bearing investments multiplied by the weighted average yield of our investments. We expect that the total dollar amount of interest and any dividend income that we earn to increase as the size of our investment portfolio increases. In addition, we may generate revenue in the form of prepayment fees, commitment, loan origination, structuring or due diligence fees, fees for providing significant managerial assistance and consulting fees.

The following shows the breakdown of investment income for the years ended December 31, 2017, 2016, and 2015 (in millions).

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
	(dollars in millions)		
Interest Income	$ 37.6	$ 38.0	$ 34.3
PIK Income	0.5	0.2	0.4
Miscellaneous fees	1.6	1.3	0.5
	$ 39.7	$ 39.5	$ 35.2

The increase in interest income from the respective periods were due primarily to growth in the overall investment portfolio.

Expenses

Our primary operating expenses include the payment of fees to Stellus Capital Management under the investment advisory agreement, our allocable portion of overhead expenses under the administration agreement and other operating costs described below. We bear all other out-of-pocket costs and expenses of our operations and transactions, which may include:

- the cost of calculating our net asset value, including the cost of any third-party valuation services;
- the cost of effecting sales and repurchases of shares of our common stock and other securities;
- fees payable to third parties relating to making investments, including out-of-pocket fees and expenses (such as travel expenses) associated with performing due diligence and reviews of prospective investments;
- transfer agent and custodial fees;
- out-of-pocket fees and expenses associated with marketing efforts;
- federal and state registration fees and any stock exchange listing fees;
- U.S. federal, state and local taxes;
- independent directors fees and expenses;
- brokerage commissions;
- fidelity bond, directors and officers liability insurance and other insurance premiums;
- direct costs, such as printing, mailing, long distance telephone and staff;
- fees and expenses associated with independent audits and outside legal costs;
- costs associated with our reporting and compliance obligations under the 1940 Act and other applicable U.S. federal and state securities laws; and

other expenses incurred by Stellus Capital Management or us in connection with administering our business, including payments under the administration agreement that are based upon our allocable portion of overhead (subject to the review of our board of directors).

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The following shows the breakdown of operating expenses for the years ended December 31, 2017, 2016 and 2015 (in millions).

	Year Ended December 31, 2017	Year Ended December 31, 2016	Year Ended December 31, 2015
Operating Expenses			
Management Fees	$ 6.3	$ 6.3	$ 5.8
Valuation Fees	0.3	0.4	0.4
Administrative services expenses	1.3	1.0	1.0
Incentive fees	2.9	4.3	4.0
Professional fees	1.3	0.7	0.6
Directors fees	0.3	0.3	0.3
Insurance expense	0.4	0.5	0.5
Interest expense and other fees	7.9	8.0	6.2
Deferred offering costs		0.3	
Other general and administrative	0.6	0.4	0.4
Total Operating Expenses	$ 21.3	$ 22.2	$ 19.2
Loss on extinguishment of debt	0.4		
Waiver of Incentive Fees			(0.6)
Total Expenses, net of fee waivers	$ 21.7	$ 22.2	$ 18.6

The decrease in operating expense from 2016 to 2017 was due to: 1) lower incentive fees, due to an increase in net assets, which increased the pre-incentive fee net investment income threshold needed to reach the hurdle rate (see Note 2 for discussion on incentive fee calculation), 2) the offset of an increase in professional fees, primarily related to increased costs of Sarbanes-Oxley compliance and 3) the offset of a one-time loss on extinguishment from our Credit Facility modification and payoff of our 6.50% Notes (the 2019 Notes). See Notes 9 and 11 for discussion on debt modifications during 2017.

The increase in operating expense from 2015 to 2016 was due to: 1) increased interest and fees on our SBA-guaranteed debentures, which were fully drawn in the fourth quarter of 2015, 2) an increase in management and incentive fees due to portfolio growth and 3) deferred offering costs, which were fully expensed in the second quarter of 2016.

While under no obligation to do so, the Advisor waived incentive fees of $646,333 for the year ended December 31, 2015 to support an annualized dividend yield of 9.0% based on the $15.00 price per share of our common stock in the Offering. Such waiver in no way implies that the Advisor will waive incentive fees in any future period. The Advisor did not waive incentive fees during the years ended December 31, 2017 and 2016.

Net Investment Income

Net investment income was $18.0 million, or $1.21 per common share based on 14,870,981 weighted-average common shares outstanding at December 31, 2017. Net investment income was $17.3 million, or $1.39 per common share based on 12,479,959 weighted-average common shares outstanding at December 31, 2016. Net investment income was $16.5 million, or $1.33 per common share based on 12,479,961 weighted-average common shares outstanding at December 31, 2015.

Net investment income for the year ended December 31, 2017 increased compared to the year ended December 31, 2016 as a result of lower incentive fees which declined year over year due to higher net assets, which makes it more difficult to clear the incentive fee hurdle.

Net Realized Gains and Losses

We measure realized gains or losses by the difference between the net proceeds from the repayment, sale or other disposition and the amortized cost basis of the investment, using the specific identification method, without regard to unrealized appreciation or depreciation previously recognized.

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Proceeds from repayments of investments and amortization of other certain investments for the year ended December 31, 2017 totaled $172.3 million and net realized gain totaled $4.7 million. Proceeds from repayments of investments and amortization of other certain investments for the year ended December 31, 2016 totaled $55.9 million and net realized loss totaled $13.1 million, $12.2 million of which is related to the realized loss of our term loan in Binder and Binder. Proceeds from the sales and repayments of investments and amortization of other certain investments for the year ended December 31, 2015 totaled $93.3 million and net realized gains totaled $0.4 million.

Net Change in Unrealized Appreciation (Depreciation) of Investments

Net change in unrealized appreciation primarily reflects the change in portfolio investment values during the reporting period, including the reversal of previously recorded appreciation or depreciation when gains or losses are realized.

Net change in unrealized appreciation (depreciation) on investments and cash equivalents for the year ended December 31, 2017, 2016 and 2015 totaled ($0.02) million, $18.6 million, and ($9.2) million, respectively.

There was relatively no change in unrealized appreciation (depreciation) in 2017. The change in unrealized appreciation in 2016 was due primarily to two factors: (1) the reversal of $8.3 million of unrealized depreciation accrued in prior years resulting from realized losses and (2) $10.3 million from tightening interest rate spreads in 2016. The change in unrealized depreciation in 2015 was due primarily to unrealized depreciation on our one non-accrual investment as well as unrealized depreciation on other investments in the portfolio due to a widening of market interest rate spreads.

Provision for Taxes on Unrealized Appreciation on Investments

We have direct wholly owned subsidiaries that have elected to be taxable entities (the Taxable Subsidiaries). The Taxable Subsidiaries permit us to hold equity investments in portfolio companies which are pass through entities for tax purposes and continue to comply with the source-of-income requirements contained in RIC tax provisions of the Code. The Taxable Subsidiaries are not consolidated with us for income tax purposes and may generate income tax expense, benefit, and the related tax assets and liabilities, as a result of their ownership of certain portfolio investments. The income tax expense, or benefit, if any, and related tax assets and liabilities are reflected in our consolidated financial statements. For the year ended December 31, 2017, 2016 and 2015, we recognized a benefit (provision) for income tax at our taxable subsidiaries of $9.0 thousand, $0.4 million, and $(0.1) million. As of December 31, 2017 and 2016, a deferred tax liability of $0 and $8.0 thousand, respectively, were included on the Consolidated Statement of Assets and Liabilities.

Net Increase in Net Assets Resulting from Operations

Net increase in net assets resulting from operations totaled $22.6 million, or $1.52 per common share based on weighted-average shares of 14,870,981 for the year ended December 31, 2017, as compared to $23.2 million, or $1.86 per common share based on weighted-average shares of 12,479,959 common shares outstanding for the year ended December 31, 2016, as compared to $7.7 million, or $0.61 per common share based on weighted-average shares of 12,479,961 common shares outstanding for the year ended December 31, 2015.

The decrease in net assets resulting from operations for the year ended December 31, 2017 as compared to the year ended December 31, 2016 was due primarily to a higher unrealized appreciation in 2016 partially offset by realized gains and increased net investment income in 2017. Similarly, the increase in net assets resulting from operations for the year ended December 31, 2016 as compared to the year ended December 31, 2015 was due primarily to higher unrealized appreciation in 2016.

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Financial condition, liquidity and capital resources

Cash Flows from Operating and Financing Activities

Our operating activities used net cash of $51.8 million for the three months ended March 31, 2018, primarily in connection with the purchase and origination of new portfolio investments, some of which was offset by the sales and repayments on our investments. Our financing activities for the three months ended March 31, 2018 provided cash of $72.2 million due to net borrowings under the Credit Facility during the period.

Our operating activities provided cash of $20.1 million for the three months ended March 31, 2017, primarily in connection with cash interest received and repayments of our investments, much of which was offset by the purchase and origination of new portfolio investments. Our financing activities for the three months ended March 31, 2017 used cash of $17.8 million due to distributions to stockholders and net repayments of the Original Credit Facility during the period.

Liquidity and Capital Resources

Our liquidity and capital resources are derived from the Credit Facility, the 2022 Notes, SBA-guaranteed debentures and cash flows from operations, including investment sales and repayments, and income earned. Our primary use of funds from operations includes investments in portfolio companies and other operating expenses we incur, as well as the payment of dividends to the holders of our common stock. We used, and expect to continue to use, these capital resources as well as proceeds from turnover within our portfolio and from public and private offerings of securities to finance our investment activities.

Although we expect to fund the growth of our investment portfolio through the net proceeds from future public and private equity offerings and issuances of senior securities or future borrowings to the extent permitted by the 1940 Act, our plans to raise capital may not be successful. In this regard, if our common stock trades at a price below our then-current net asset value per share, we may be limited in our ability to raise equity capital given that we cannot sell our common stock at a price below net asset value per share unless our stockholders approve such a sale and our board of directors makes certain determinations in connection therewith. A proposal, approved by our stockholders at our 2017 annual stockholders meeting, authorizes us to sell shares equal to up to 25% of our outstanding common stock of our common stock below the then current net asset value per share of our common stock in one or more offerings. This authorization will expire on the earlier of May 24, 2018, the one year anniversary of our 2017 annual stockholders meeting. We would need similar future approval from our stockholders to issue shares below the then current net asset value per share any time after the expiration of the current approval. In addition, we intend to distribute between 90% and 100% of our taxable income to our stockholders in order to satisfy the requirements applicable to RICs under Subchapter M of the Code. Consequently, we may not have the funds or the ability to fund new investments, to make additional investments in our portfolio companies, to fund our unfunded commitments to portfolio companies or to repay borrowings. In addition, the illiquidity of our portfolio investments may make it difficult for us to sell these investments when desired and, if we are required to sell these investments, we may realize significantly less than their recorded value.

Also, as a BDC, we generally are required to meet a coverage ratio of total assets, less liabilities and indebtedness not represented by senior securities, to total senior securities, which include all of our borrowings and any outstanding preferred stock, of at least 200% (or 150% if certain requirements are met). This requirement limits the amount that we may borrow. We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the asset coverage test under the 1940

Act. We were in compliance with the asset coverage ratios at all times. As of March 31, 2018 and December 31, 2017, our asset coverage ratio was 233% and 346%, respectively. The amount of leverage that we employ will depend on our assessment of market conditions and other factors at the time of any proposed borrowing, such as the maturity, covenant package and rate structure of the proposed borrowings, our ability to raise funds through the issuance of shares of our common stock and the risks of such borrowings within the context of our investment outlook. Ultimately, we only intend to use leverage if the expected returns from borrowing to make investments will exceed the cost of such borrowing. For more information about the expected amount of and costs associated with our borrowings, see Fees and

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Expenses in this prospectus. As of March 31, 2018 and December 31, 2017, we had cash and cash equivalents of $45.5 million and $25.1 million, respectively.

Credit Facility

On November 7, 2012, the Company entered into a revolving credit facility (the Original Facility) with various lenders. SunTrust Bank, one of the lenders, served as administrative agent under the Original Facility. The Original Facility, as amended on November 21, 2014 and August 31, 2016, provided for borrowings in an aggregate amount of $120.0 million on a committed basis with an accordion feature that allowed the Company to increase the aggregate commitments up to $195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. The Company terminated the Original Facility on October 11, 2017, in conjunction with securing and entering into a new senior secured revolving credit agreement, dated as of October 10, 2017 and as amended on March 28, 2018, with ZB, N.A., dba Amegy Bank and various other leaders (the Credit Facility).

The Credit Facility provides for borrowings up to a maximum of $140.0 million on a committed basis with an accordion feature that allows the Company to increase the aggregate commitments up to $195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions.

Borrowings under the Credit Facility bear interest, subject to the Company s election, on a per annum basis equal to (i) LIBOR plus 2.50% with no LIBOR floor or (ii) 1.50% plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%. The Company pays unused commitment fees of 0.50% per annum on the unused lender commitments under the Credit Facility. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 10, 2021. This represents an interest rate reduction of 12.5 basis points and a three year extension of maturity over the Original Facility.

The Company s obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. The Credit Facility contains certain covenants, including but not limited to: (i) maintaining a minimum liquidity test of at least $10.0 million, including cash, liquid investments and undrawn availability, (ii) maintaining an asset coverage ratio of at least 2.0 to 1.0, and (iii) maintaining a minimum shareholder s equity. As of March 31, 2018, the Company was in compliance with these covenants.

As of March 31, 2018 and December 31, 2017, $118.3 and $40.8 million, respectively, was outstanding under the Credit Facility. The carrying amount of the amount outstanding under the Credit Facility approximates its fair value. The Company incurred total costs of $3.1 million in connection with obtaining, amending, and maintaining the Original Facility. The Company incurred costs of $1.2 million in connection with the Credit Facility, which are being amortized over the life of the facility. Additionally, $0.3 million of costs from the Original Facility will continue to be amortized over the remaining life of the Credit Facility. As of both March 31, 2018 and December 31, 2017, $1.4 million of such prepaid loan structure fees and administration fees had yet to be amortized. These prepaid loan fees are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3. See Note 1 for further discussion.

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Interest is paid quarterly in arrears. The following table summarizes the interest expense and amortized loan fees on the Credit Facility for the three months ended March 31, 2018 and 2017 (in millions):

	For the three months ended	
	March 31, 2018	March 31, 2017
Interest expense	$ 0.7	$ 0.9
Loan fee amortization	0.1	0.1
Commitment fees on unused portion	0.1	
Total interest and financing expenses	$ 0.9	$ 1.0
Weighted average interest rate	4.4 %	3.5 %
Effective interest rate	5.6 %	4.0 %
Average debt outstanding	$ 68.2	$ 104.7
Cash paid for interest and unused fees	$ 0.6	$ 1.0

SBA-Guaranteed Debentures

Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. Under the regulations applicable to SBIC funds, an SBIC can have outstanding debentures guaranteed by the SBA subject to a regulatory leverage limit, up to two times the amount of regulatory capital. The 2016 omnibus spending bill approved by the U.S. Congress and signed into law by the President increased the amount of SBA-guaranteed debentures that affiliated SBIC funds can have outstanding from $225.0 million to $350.0 million, subject to SBA approval. As of March 31, 2018 and December 31, 2017, the SBIC subsidiary had $75.0 million and $67.5 million in regulatory capital, as such term is defined by the SBA.

As a BDC, we are only allowed to employ leverage to the extent that our asset coverage, as defined in the 1940 Act, equals at least 200% after giving effect to such leverage. The amount of leverage that we employ at any time depends on our assessment of the market and other factors at the time of any proposed borrowing.

On August 12, 2014, we obtained exemptive relief from the SEC to permit us to exclude the debt of the SBIC subsidiary guaranteed by the SBA from our 200% asset coverage test under the 1940 Act. The exemptive relief provides us with increased flexibility under the 200% asset coverage test by permitting us to borrow up to $150.0 million more than we would otherwise be able to absent the receipt of this exemptive relief.

On a stand-alone basis, the SBIC subsidiary held $210.3 and $162.0 million in assets at March 31, 2018 and December 31, 2017, respectively, which accounted for approximately 43.7% and 40.4% of our total consolidated assets, respectively.

Debentures guaranteed by the SBA have fixed interest rates that equal prevailing 10-year Treasury Note rates plus a market spread and have a maturity of ten years with interest payable semi-annually. The principal amount of the debentures is not required to be paid before maturity, but may be pre-paid at any time with no prepayment penalty. As of both March 31, 2018 and December 31, 2017, the SBIC subsidiary had $90.0 million of SBA-guaranteed debentures outstanding. See Note 10 for further detail on the SBA-guaranteed debentures outstanding.

As of March 31, 2018 and December 31, 2017, the carrying amount of the SBA-guaranteed debentures approximated their fair value. The fair values of the SBA-guaranteed debentures are determined in accordance with ASC 820, which defines fair value in terms of the price that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The fair value of the SBA-guaranteed debentures are estimated based upon market interest rates for our own borrowings or entities with similar credit risk, adjusted for nonperformance risk, if any. At March 31, 2018 and December 31, 2017 the SBA-guaranteed debentures would be deemed to be Level 3, as defined in Note 6.

As of March 31, 2018, the Company has incurred $3.1 million in financing costs related to the SBA-guaranteed debentures since receiving our license, which were recorded as prepaid loan fees. As of

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March 31, 2018 and December 31, 2017, $2.1 and $2.2 million of prepaid financing costs had yet to be amortized, respectively. These prepaid loan fees are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3. See Note 1 for further discussion.

Interest is paid semi-annually, in March and September. The following table summarizes the interest expense and amortized fees on the SBA-guaranteed debentures for the three ended March 31, 2018 and 2017 (in millions):

	For the three months ended March 31, 2018	March 31, 2017
Interest expense	$ 0.6	$ 0.5
Debenture fee amortization	0.1	0.1
Total interest and financing expenses	$ 0.7	$ 0.6
Weighted average interest rate	2.9 %	3.1 %
Effective interest rate	3.3 %	3.6 %
Average debt outstanding	$ 90.0	$ 65.0
Cash paid for interest	$ 1.2	$ 1.0

Notes Offering

On May 5, 2014, the Company closed a public offering of $25.0 million in aggregate principal amount of 6.50% notes (the 2019 Notes), due on April 30, 2019. On August 21, 2017, the Company caused notices to be issued to the holders of its 2019 Notes regarding the Company s exercise of its option to redeem all of the issued and outstanding 2019 Notes, pursuant to Section 1101 of the Base Indenture dated as of May 5, 2014, between the Company and U.S. Bank National Association, as trustee, and Section 1.01(h)(i) of the First Supplemental Indenture dated as of May 5, 2014. The Company redeemed all $25.0 million in aggregate principal amount of the 2019 Notes on September 20, 2017. The 2019 Notes were redeemed at 100% of their principal amount, plus the accrued and unpaid interest thereon through the redemption date.

The Company incurred no costs on the 2019 Notes for the three months ended March 31, 2018, and incurred interest and fee expense on the Notes of $0.5 million, of which $0.4 million was interest expense and the remainder was amortization of loan fees paid on the Notes and administration fees, for the three months ended March 31, 2017. The Company paid $0 and $0.4 million in interest expense on the 2019 Notes during the respective periods ended March 31, 2018 and 2017.

On August 21, 2017, the Company issued $42.5 million in aggregate principal amount of 5.75% fixed-rate notes due September 15, 2022 (the 2022 Notes). On September 8, 2017, the Company issued an additional $6.4 million in aggregate principal amount of the 2022 Notes pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at the Company s option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. Interest is payable quarterly beginning December 15, 2017.

The Company used all of the net proceeds from this offering to fully redeem the 2019 Notes and a portion of the amount outstanding under the Original Facility. As of March 31, 2018 and December 31, 2017, the aggregate carrying amount of the 2022 Notes was approximately $48.9 million for both periods and the fair value of the Notes was approximately $49.1 million and $49.5 million, respectively. The 2022 Notes are listed on New York Stock Exchange under the trading symbol SCA . The fair value of the Notes is based on the closing price of the security, which is a

Level 2 input under ASC 820 due to sufficient trading volume.

In connection with the issuance and maintenance of the 2022 Notes, we have incurred $1.7 million of fees which are being amortized over the term of the 2022 Notes, of which $1.5 million and $1.6 million remains to be amortized as of March 31, 2018 and December 31, 2017, respectively. These financing costs are presented on the consolidated statement of assets and liabilities as a deduction from the debt liability as required by ASU No. 2015-3.

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For the three months ended March 31, 2018, the Company incurred interest and fee expense on the 2022 Notes of $0.8 million, of which $0.7 million was interest expense and the remainder was amortization of loan fees paid on the 2022 Notes and administration fees. The Company paid $0.7 million in interest expense on the 2022 Notes during the period. The Company neither incurred nor paid any costs associated with the 2022 Notes during the three months ended March 31, 2017.

Off-Balance Sheet Arrangements

We may be a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financial needs of our portfolio companies. As of March 31, 2018 and December 31, 2017, our off-balance sheet arrangements consisted of unfunded commitments to provide debt financing to six and four of our portfolio companies respectively totaling $11.2 million and $8.7 million, respectively. As of March 31, 2018, the Company had sufficient liquidity to fund such unfunded commitments (through cash on hand and available borrowings under the Credit Facility) should the need arise.

Regulated Investment Company Status and Dividends

We have elected to be treated as a RIC under Subchapter M of the Code. So long as we maintain our status as a RIC, we will not be taxed on our investment company taxable income or realized net capital gains, to the extent that such taxable income or gains are distributed, or deemed to be distributed, to stockholders on a timely basis.

Taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses, and generally excludes net unrealized appreciation or depreciation until realized. Dividends declared and paid by us in a year may differ from taxable income for that year as such dividends may include the distribution of current year taxable income or the distribution of prior year taxable income carried forward into and distributed in the current year. Distributions also may include returns of capital.

To qualify for RIC tax treatment, we must, among other things, distribute, with respect to each taxable year, at least 90% of our investment company net taxable income (i.e., our net ordinary income and our realized net short-term capital gains in excess of realized net long-term capital losses, if any). If we maintain our qualification as a RIC, we must also satisfy certain distribution requirements each calendar year in order to avoid a federal excise tax on our undistributed earnings of a RIC.

We intend to distribute to our stockholders between 90% and 100% of our annual taxable income (which includes our taxable interest and fee income). However, the covenants contained in the Credit Facility may prohibit us from making distributions to our stockholders, and, as a result, could hinder our ability to satisfy the distribution requirement. In addition, we may retain for investment some or all of our net taxable capital gains (i.e., realized net long-term capital gains in excess of realized net short-term capital losses) and treat such amounts as deemed distributions to our stockholders. If we do this, our stockholders will be treated as if they received actual distributions of the capital gains we retained and then reinvested the net after-tax proceeds in our common stock. Our stockholders also may be eligible to claim tax credits (or, in certain circumstances, tax refunds) equal to their allocable share of the tax we paid on the capital gains deemed distributed to them. To the extent our taxable earnings for a fiscal taxable year fall below the total amount of our dividends for that fiscal year, a portion of those dividend distributions may be deemed a return of capital to our stockholders.

We may not be able to achieve operating results that will allow us to make distributions at a specific level or to increase the amount of these distributions from time to time. In addition, we may be limited in our ability to make distributions due to the asset coverage test for borrowings applicable to us as a business development company under the 1940 Act and due to provisions in the Credit Facility. We cannot assure stockholders that they will receive any distributions or distributions at a particular level.

In accordance with certain applicable Treasury regulations and private letter rulings issued by the Internal Revenue Service, a RIC may treat a distribution of its own stock as fulfilling its RIC distribution requirements if each stockholder may elect to receive his or her entire distribution in either cash or stock of the RIC, subject to a limitation that the aggregate amount of cash to be distributed to all stockholders must be at least 20% of the aggregate declared distribution. If too many stockholders elect to receive cash, each stockholder electing to receive cash must receive a pro rata amount of cash (with the balance of the distribution paid in stock). In no event will any stockholder, electing to receive cash, receive less than 20% of his or her entire distribution in cash. If these and certain other requirements are met, for U.S. federal income tax purposes, the amount of the dividend paid in stock will be equal to the amount of cash that could have been received instead of stock. We have no current intention of paying dividends in shares of our stock in accordance with these Treasury regulations or private letter rulings.

Recent Accounting Pronouncements

See Note 1 to the consolidated financial statements contained herein for a description of recent accounting pronouncements, if any, including the expected dates of adoption and the anticipated impact on the financial statements.

Critical Accounting Policies

See Note 1 to the consolidated financial statements contained herein for a description of critical accounting policies.

Subsequent Events

Investment Portfolio

On April 2, 2018, the Company invested $7.9 million in the first lien term loan and $0.9 million in the unfunded revolver of BFC SolmeteX LLC, a leading provider of filtration products in the U.S. and Canada. The Company also invested $1.2 million in a first lien term loan of Bonded Filter Co. LLC, a subsidiary of BFC Solmetex LLC.

On April 13, 2018, the Company invested $16.4 million in the first lien term loan and a $0.75 million in the unfunded revolver of DTE Enterprises, Inc., a provider of industrial powertrain repair and maintenance services for the oil & gas and mining sectors. Additionally, the Company invested $1.5 million in the equity of the Company.

On April 13, 2018, the Company made an additional investment of $12.5 million in the 2nd lien term loan of Mobileum, Inc., an existing portfolio company.

On April 24, 2018, the Company received full repayment of the first lien term loan of Catapult Learning, LLC for total proceeds of $12.1 million.

On April 30, 2018, the Company received full repayment of the unsecured term loan of Binder & Binder National Social Security Disability Advocates, LLC for total proceeds of $0.1 million.

On May 2, 2018, the Company invested $4.5 million in the second lien term loan of General LED OPCO, LLC, a provider of LED lighting systems and modules.

Credit Facilities

The outstanding balance under the Credit Facility as of May 4, 2018 was $66.1 million.

SBA-guaranteed Debentures

On April 25, 2018, the Company drew $40.0 million of SBA-guaranteed debentures, bringing the total balance of SBA-guaranteed Debentures outstanding to $130.0 million as of May 4, 2018.

Legislative Changes

On March 23, 2018, the Small Business Credit Availability Act (the SBCAA) was signed into law, which included various changes to regulations under the federal securities laws that impact BDCs. The SBCAA included changes to the 1940 Act to allow BDCs to decrease their asset coverage requirement to 150% from 200% under certain circumstances.

On April 4, 2018, the board of directors (the Board) of Stellus Capital Investment Corporation (the Company), including a required majority (as such term is defined in Section 57(o) of the Investment Company Act of 1940, as amended (the 1940 Act)) of the Board, approved the application of the modified

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asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act. As a result, the asset coverage ratio test applicable to the Company will be decreased from 200% to 150%, effective April 4, 2019 unless approved earlier by a vote of the Company s stockholders. The Board also approved the submission of a proposal to approve the application of the modified asset coverage requirements set forth in Section 61(a)(2) of the 1940 Act at the Company s 2018 annual meeting of stockholders.

Dividend Declared

On April 16, 2018, the Company s board of directors declared a regular monthly dividend for each of April, May and June 2018 as follows:

Declared	Ex-Dividend Date	Record Date	Payment Date	Amount per Share
4/16/2018	4/27/2018	4/30/2018	5/15/2018	$ 0.1133
4/16/2018	5/30/2018	5/31/2018	6/15/2018	$ 0.1133
4/16/2018	6/28/2018	6/29/2018	7/13/2018	$ 0.1133

Quantitative and Qualitative Disclosures About Market Risk

We are subject to financial market risks, including changes in interest rates. For the three months ended March 31, 2018 and 2017, 89% and 77% of the loans in our portfolio bore interest at floating rates, respectively. These floating rate loans typically bear interest in reference to LIBOR, which are indexed to 30-day or 90-day LIBOR rates, subject to an interest rate floor. As of March 31, 2018 and 2017, the weighted average interest rate floor on our floating rate loans was 0.94% and 0.86%, respectively.

Assuming that the Statement of Assets and Liabilities as of March 31, 2018 were to remain constant and no actions were taken to alter the existing interest rate sensitivity, hypothetical 1% increase in LIBOR would increase our interest income approximately $3.6 million on an annualized basis. A hypothetical 1% decrease in LIBOR would decrease our interest income by $3.3 million on an annualized basis, considering interest rate floors where applicable.

Changes in interest rates will also affect our cost of funding. Our interest expense will be affected by changes in the published LIBOR rate in connection with the Credit Facility. At March 31, 2018, based on our applicable levels of our Credit Facility, a 1% increase in interest rates would decrease our annual net investment income by $1.2 million.

Although we believe that this measure is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in credit quality, size and composition of the assets on the balance sheet and other business developments that could affect net increase in net assets resulting from operations, or net income. Accordingly, no assurances can be given that actual results would not differ materially from the potential outcome simulated by this estimate. We may hedge against interest rate fluctuations by using standard hedging instruments such as futures, options and forward contacts subject to the requirements of the 1940 Act. While hedging activities may insulate us against adverse changes in interest rates, they may also limit our ability to participate in the benefits of lower interest rates with respect to our portfolio of investments. For the three months ended March 31, 2018 and 2017, we did not engage in hedging activities.

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SENIOR SECURITIES

Information about our senior securities is shown in the following table as of March 31, 2018 and for the fiscal years ended December 31, 2017, 2016, 2015, 2014, 2013 and 2012. The report of Grant Thornton LLP, our independent registered public accountants, on the senior securities table as of December 31, 2017, is attached as an exhibit to the registration statement of which this prospectus is a part.

Class and Year	Total Amount Outstanding Exclusive of Treasury Securities[1] (Dollars in thousands)	Asset Coverage per Unit[2]	Involuntary Liquidating Preference per Unit[3]	Average Market Value per Unit[4]
SBA Debentures				
Fiscal 2014	$ 16,250	N/A [6]		N/A
Fiscal 2015	65,000	N/A [6]		N/A
Fiscal 2016	65,000	N/A [6]		N/A
Fiscal 2017	$ 90,000	N/A [6]		N/A
Fiscal 2018 (through March 31, 2018)	$ 90,000	N/A [6]		N/A
Original Credit Facility[7]				
Fiscal 2012	$ 38,000	$ 3,090		N/A
Fiscal 2013	110,000	2,470		N/A
Fiscal 2014	106,500	2,320 [6]		N/A
Fiscal 2015	109,500	2,220 [6]		N/A
Fiscal 2016	$ 116,000	$ 2,210 [6]		N/A
Credit Facility				
Fiscal 2017	$ 40,750	$ 3,460 [6]		N/A
Fiscal 2018 (through March 31, 2018)	$ 118,300	$ 2,330 [6]		N/A
5.75% Notes due 2022				
Fiscal 2017	$ 48,875	$ 3,460 [6]		$ 25.34
Fiscal 2018 (through March 31, 2018)	$ 48,875	$ 2,330 [6]		$ 25.23
6.50% Notes due 2019[7]				
Fiscal 2014	$ 25,000	$ 2,320 [6]		$ 25.41
Fiscal 2015	25,000	2,220 [6]		25.27
Fiscal 2016	25,000	2,210 [6]		$ 25.11
Short-Term Loan[5]				
Fiscal 2012	$ 45,000	$ 3,090		N/A
Fiscal 2013	$ 9,000	$ 2,470		N/A

(1) Total amount of senior securities outstanding at the end of the period presented.

(2) Asset coverage per unit is the ratio of the carrying value of our total assets, less all liabilities and indebtedness not represented by senior securities, in relation to the aggregate amount of senior securities representing indebtedness. Asset coverage per unit is expressed in terms of dollar amounts per $1,000 of indebtedness.

(3)

The amount to which such class of senior security would be entitled upon the involuntary liquidation of the issuer in preference to any security junior to it. The indicates information which the SEC expressly does not require to be disclosed for certain types of senior securities.

(4) Average market value per unit for the Notes represents the average of the daily closing prices as reported on the NYSE during the period presented. Average market value per unit for our SBA Debentures and Credit Facility are not applicable because these are not registered for public trading.

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(5) Refers to short-term loans that the Company obtained from Raymond James and repaid in full on January 2, 2013 and January 2, 2014, respectively.

(6) We have excluded our SBA-guaranteed debentures from the asset coverage calculation as of December 31, 2017, 2016, 2015 and 2014 pursuant to the exemptive relief granted by the SEC in August 2014 that permits us to exclude such debentures from the definition of senior securities in the 200% asset coverage ratio we are required to maintain under the 1940 Act.

(7) Such senior securities were retired during the 2017 fiscal year.

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THE COMPANY

Stellus Capital Investment Corporation

We are an externally managed, closed-end, non-diversified management investment company that has elected to be regulated as a BDC under the Investment Company Act of 1940, or the 1940 Act. We originate and invest primarily in private middle-market companies (typically those with $5.0 million to $50.0 million of EBITDA (earnings before interest, taxes, depreciation and amortization)) through first lien, second lien, unitranche and mezzanine debt financing, with corresponding equity co-investments. Unitranche debt is typically structured as first lien loans with certain risk characteristics of mezzanine debt. Mezzanine debt includes senior unsecured and subordinated loans.

Our investment activities are managed by our investment adviser, Stellus Capital Management, an investment advisory firm led by Robert T. Ladd and its other senior investment professionals. We source investments primarily through the extensive network of relationships that the senior investment professionals of Stellus Capital Management have developed with financial sponsor firms, financial institutions, middle-market companies, management teams and other professional intermediaries. The companies in which we invest are typically highly leveraged, and, in most cases, our investments in such companies will not be rated by national rating agencies. If such investments were rated, we believe that they would likely receive a rating which is often referred to as junk.

Our investment objective is to maximize the total return to our stockholders in the form of current income and capital appreciation. We seek to achieve our investment objective by:

- accessing the extensive origination channels that have been developed and established by the Stellus Capital Management investment professionals that include long-standing relationships with private equity firms, commercial banks, investment banks and other financial services firms;
- investing in what we believe to be companies with strong business fundamentals, generally within our core middle-market company focus;
- focusing on a variety of industry sectors, including business services, energy, general industrial, government services, healthcare, software and specialty finance;
- focusing primarily on directly originated transactions;
- applying the disciplined underwriting standards that the Stellus Capital Management investment professionals have developed over their extensive investing careers; and
- capitalizing upon the experience and resources of the Stellus Capital Management investment team to monitor our investments.

In addition, we received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). Under the terms of the relief permitting us to co-invest with other funds managed by Stellus Capital Management, a required majority (as defined in Section 57(o) of the 1940 Act) of our independent directors must make certain conclusions in connection with a co-investment transaction, including that (1) the terms of the proposed transaction, including the consideration to be paid, are reasonable and fair to us and our stockholders and do not involve overreaching of us or our stockholders on the part of any person concerned and (2) the transaction is consistent with the interests of our stockholders and is consistent with our investment objectives and strategies. We intend to co-invest, subject to the conditions included in the exemptive order we received from the SEC, with private credit funds managed by Stellus Capital Management that have an investment strategy that is identical to our investment strategy. We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification.

As a BDC, we are required to comply with regulatory requirements, including limitations on our use of debt. We are permitted to, and expect to continue to, finance our investments through borrowings.

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Prior to March 23, 2018, Section 61(a) of the 1940 Act (which incorporates the requirements of Sections 18(a)(1) and 18(a)(2) of the 1940 Act) did not permit a BDC to issue senior securities unless, at the time of issuance, the BDC had an Asset Coverage Ratio of at least 200%, taking into account that issuance of senior securities. However, on March 23, 2018, the SBCA was signed into law by the President. The SBCA, among other things, permits BDCs to be subject to 150% Asset Coverage, if specific conditions are satisfied, when issuing senior securities. In other words, prior to the enactment of the SBCA, a BDC could borrow $1 for investment purposes for every $1 of investor equity. Now, for those BDCs that satisfy the Act s approval and disclosure requirements, the BDC can borrow $2 for investment purposes for every $1 of investor equity.

The SBCA provides that in order for a BDC whose common stock is traded on a national securities exchange to be subject to 150% Asset Coverage, the BDC must either obtain: (i) approval of the required majority of its non-interested directors who have no financial interest in the proposal, which would become effective on the Board Effective Date, or (ii) obtain stockholder approval (of more than 50% of the votes cast for the proposal at a meeting in which quorum is present), which would become effective on the first day after the date of such stockholder approval.

On April 4, 2018, our Board, including a majority of the non-interested directors who have no financial interest in this proposal, deemed it in the best interests of the Company and its stockholders for the Company to be subject to 150% Asset Coverage. Our Board believes that having the flexibility for the Company to incur additional leverage in certain instances is in the best interests of stockholders. In connection with this determination, our Board approved a resolution permitting the Company to be subject to 150% Asset Coverage, to be effective on the Board Effective Date, or April 4, 2019. This approval will allow us to incur twice as much debt as we could have without such approval after the 150% Asset Coverage becomes effective.

In addition, the Board also approved and recommended that stockholders vote for a proposal to authorize the Company to be subject to 150% Asset Coverage at our 2018 Annual Meeting, scheduled for June 28, 2018. If our stockholders approve this proposal, the reduced Asset Coverage Ratio would be effective the day after the 2018 Annual Meeting. Because we have received Board approval, if the proposal does not receive approval of the majority of the votes cast at the meeting, we will be subject to the reduced Asset Coverage Ratio beginning on April 4, 2019.

The amount of leverage that we employ will depend on our assessment of market conditions and other factors at the time of any proposed borrowing, such as the maturity, covenant package and rate structure of the proposed borrowings, our ability to raise funds through the issuance of our securities and the risks of such borrowings within the context of our investment outlook. Ultimately, we only intend to use leverage if the expected returns from borrowing to make investments will exceed the cost of such borrowings.

We have elected and qualified to be treated for federal income tax purposes as a regulated investment company, or RIC, under Subchapter M of the Internal Revenue Code, or the Code. As a RIC, we generally will not have to pay corporate-level federal income taxes on any net ordinary income or capital gains that we distribute to our stockholders as dividends if we meet certain source-of-income, distribution and asset diversification requirements.

Our principal executive office is currently located at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, and our telephone number is (713) 292-5400. We maintain a website on the Internet at *www.stelluscapital.com* (under the Public Investors section). Information contained on our website is not incorporated by reference into Prospectus and you should not consider information contained on our website to be part of this Prospectus.

SBIC License

Our wholly owned subsidiary holds a license to operate as a small business investment company, or SBIC. Our wholly owned SBIC subsidiary s SBIC license allows it to obtain leverage by issuing SBA-guaranteed debentures up to a maximum of $150 million under current SBIC regulations, subject to required capitalization of the SBIC subsidiary and other requirements. The principal amount of SBA-guaranteed debentures is not required to be paid prior to maturity but may be prepaid at any time without penalty. We believe that the SBA-guaranteed debentures are an attractive source of debt capital.

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We have received exemptive relief from the SEC to permit us to exclude the debt of our SBIC subsidiary guaranteed by the SBA from the definition of senior securities in the asset coverage ratio we are required to maintain under the 1940 Act. This relief allows us increased flexibility under the asset coverage test by allowing us to borrow up to $150.0 million more than we would otherwise be able to borrow absent the receipt of this exemptive relief based on regulatory capital of $75.0 million of March 31, 2018.

Portfolio Composition

Our investments generally range in size from $5.0 million to $30.0 million, and we may also selectively invest in larger positions, and we generally expect that the size of our positions will increase in proportion to the size of our capital base. Pending such investments, we may reduce our outstanding indebtedness or invest in cash, cash equivalents, U.S. government securities and other high-quality debt investments with a maturity of one year or less. In the future, we may adjust opportunistically the percentage of our assets held in various types of loans, our principal loan sources and the industries to which we have greatest exposure, based on market conditions, the credit cycle, available financing and our desired risk/return profile.

The following table provides a summary of our portfolio investments as of March 31, 2018:

		As of March 31, 2018 ($ in millions)	
Number of investments		52	
Fair value[(a)]		$ 431.3	
Cost		$ 426.4	
% of portfolio at fair value	first lien debt[(c)]	46.2	%
% of portfolio at fair value	second lien debt	41.2	%
% of portfolio at fair value	mezzanine debt	6.2	%
% of portfolio at fair value	equity	6.4	%
Weighted-average annual yield[(b)]		11.1	%

(a) As of March 31, 2018, $383.9 million of our debt investments at fair value were at floating interest rates, which represented approximately 89% of our total portfolio of debt investments at fair value. As of March 31, 2018, $47.4 million of our debt investments at fair value were at fixed interest rates, which represented approximately 11% of our total portfolio of debt investments at fair value.

(b) The weighted average yield on all of our debt investments as of March 31, 2018, was approximately 11.1%, of which approximately 10.3% was current cash interest. The weighted average yield of our debt investments on accrual is not the same as a return on investment for our stockholders but, rather, relates to a portion of our investment portfolio and is calculated before the payment of all of our and our subsidiaries fees and expenses. The weighted average yield was computed using the effective interest rates for all of our debt investments, which represents the interest rate on our debt investment restated as an interest rate payable annually in arrears and is computed including cash and payment in kind, or PIK interest, as well as accretion of original issue discount. There can be no assurance that the weighted average yield will remain at their current level.

(c) Includes unitranche investments, which account for 16.1% of our portfolio investments at fair value.

Leverage

Credit Facility. We have entered the Credit Facility. The Credit Facility provides for borrowings up to a maximum of $140.0 million on a committed basis with an accordion feature that allows the Company to increase the aggregate commitments up to 195.0 million, subject to new or existing lenders agreeing to participate in the increase and other customary conditions. Borrowings under the Credit Facility bear interest, subject to our election, on a per annum basis equal to (i) LIBOR plus 2.50% with no LIBOR floor or (ii) 1.50% plus an alternate base rate based on the highest of the Prime Rate, Federal Funds Rate plus 0.5% or one month LIBOR plus 1.0%. The Company pays unused commitment fees of 0.50% per annum on the unused lender commitments. Interest is payable quarterly in arrears. Any amounts borrowed under the Credit Facility will mature, and all accrued and unpaid interest thereunder will be due and payable, on October 1, 2021. Our obligations to the lenders are secured by a first priority security interest in its portfolio of securities and cash not held at the SBIC subsidiary, but excluding short term investments. As of March 31, 2018, we had approximately $118.3 million outstanding under the Credit Facility.

5.75% Notes. On August 21, 2017, we issued $42.5 million in aggregate principal amount (the 2022 Notes) and issued an additional $6.4 million in aggregate principal amount of the 2022 Notes pursuant to a full exercise of the underwriters overallotment option. The 2022 Notes will mature on September 15, 2022, and may be redeemed in whole or in part at any time or from time to time at the Company s option on or after September 15, 2019 at a redemption price equal to 100% of the outstanding principal, plus accrued and unpaid interest. As of March 31, 2018, we had $48.9 million of 2022 Notes outstanding.

SBA-guaranteed Debentures. Due to the SBIC subsidiary s status as a licensed SBIC, we have the ability to issue debentures guaranteed by the SBA at favorable interest rates. As of March 31, 2018, the SBIC subsidiary had $90.0 million of SBA-guaranteed debentures outstanding.

Stellus Capital Management

Stellus Capital Management manages our investment activities and is responsible for analyzing investment opportunities, conducting research and performing due diligence on potential investments, negotiating and structuring our investments, originating prospective investments and monitoring our investments and portfolio companies on an ongoing basis.

The senior investment professionals of Stellus Capital Management have an average of over 28 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing loans and debt securities through market cycles. The Stellus Capital Management investment professionals continue to provide investment sub-advisory services to the D. E. Shaw & Co., L.P. and its associated investment funds (the D. E. Shaw group) with respect to an approximately $90.0 million investment portfolio (as of March 31, 2018) in middle-market companies pursuant to sub-advisory arrangements.

In addition to serving as our investment adviser and the sub-advisor to the D. E. Shaw group as noted above, Stellus Capital Management currently manages a private credit fund that has an investment strategy that is identical to our investment strategy and energy private equity funds. We received exemptive relief from the SEC to co-invest with investment funds managed by Stellus Capital Management (other than the D. E. Shaw group funds) where doing so is consistent with our investment strategy as well as applicable law (including the terms and conditions of the exemptive order issued by the SEC). We believe that such co-investments may afford us additional investment opportunities and an ability to achieve greater diversification. We will not co-invest with the energy private equity funds, as the energy private equity funds focus on predominantly equity-related investments, and we focus on predominantly credit-related investments.

Stellus Capital Management is headquartered in Houston, Texas, and also maintains offices in the Washington, D.C. area and Charlotte, North Carolina.

Market Opportunity

We originate and invest primarily in private middle-market companies through first lien, second lien, unitranche and mezzanine debt financing, with a corresponding equity co-investment. We believe the environment for investing in middle-market companies is attractive for several reasons, including:

Robust Demand for Debt Capital. We believe that private equity firms have significant committed but uncalled capital, a large portion of which is still available for investment in the United States. We expect the large amount of uninvested capital commitments will drive buyout activity over the next several years, which should, in turn, create lending opportunities for us. In addition to increased buyout activity, a high volume of senior secured and high yield debt was originated in the calendar years 2011 through 2013 and will come due in the near term and, accordingly, we believe that new financing opportunities will increase as many companies seek to refinance this indebtedness.

Reduced Availability of Capital for Middle-Market Companies. We believe there are fewer providers of, and less capital available for financing to middle-market companies, as compared to the time period prior to the economic downturn that began in December 2007. We believe that, as a result of that downturn, many financing providers have chosen to focus on large, liquid corporate loans and managing capital markets transactions rather than lending to middle-market businesses. In addition, we believe regulatory changes, including the adoption of the Dodd-Frank Act and the introduction of the international capital and liquidity requirements under the Basel III Accords, or Basel III, have caused banks to curtail their lending to middle-market-companies. As a result, we believe that less competition will facilitate higher quality deal flow and allow for greater selectivity throughout the investment process.

Attractive Deal Pricing and Structures. We believe that the pricing of middle-market debt investments is higher, and the terms of such investments are more conservative, compared to larger liquid, public debt financings, due to the more limited universe of lenders as well as the highly negotiated nature of these financings. These transactions tend to offer stronger covenant packages, higher interest rates, lower leverage levels and better call protection compared to larger financings. In addition, middle-market loans typically offer other investor protections such as default penalties, lien protection, change of control provisions and information rights for lenders.

Specialized Lending Requirements. Lending to middle-market companies requires in-depth diligence, credit expertise, restructuring experience and active portfolio management. We believe that several factors render many U.S. financial institutions ill-suited to lend to middle-market companies. For example, based on the experience of Stellus Capital Management s investment professionals, lending to middle-market companies in the United States (a) is generally more labor intensive than lending to larger companies due to the smaller size of each investment and the fragmented nature of the information available with respect to such companies, (b) requires specialized due diligence and underwriting capabilities, and (c) may also require more extensive ongoing monitoring by the lender. We believe that, through Stellus Capital Management, we have the experience and expertise to meet these specialized lending requirements.

Competitive Strengths

We believe that the following competitive strengths will allow us to achieve positive returns for our investors:

Experienced Investment Team. Through our investment adviser, Stellus Capital Management, we have access to the experience and expertise of the Stellus Capital Management investment team, including its senior investment professionals who have an average of over 28 years of investing, corporate finance, restructuring, consulting and accounting experience and have worked together at several companies. The Stellus Capital Management investment professionals have a wide range of experience in middle-market investing, including originating, structuring and managing loans and debt securities through market cycles. We believe the members of Stellus Capital Management s investment professionals are proven and experienced, with extensive capabilities in leveraged credit investing, having participated in these markets for the predominant portion of their careers. We believe that the experience and demonstrated ability of the Stellus Capital Management investment team to complete transactions enhances the quantity and quality of investment opportunities available to us.

Established, Rigorous Investment and Monitoring Process. The Stellus Capital Management investment professionals have developed an extensive review and credit analysis process. Each investment that is reviewed by Stellus Capital Management is brought through a structured, multi-stage approval process. In addition, Stellus Capital Management takes an active approach in monitoring all investments, including reviews of financial performance on at least a quarterly basis and regular discussions with management. Stellus Capital Management s investment and monitoring process and the depth and experience of its investment professionals should allow it to conduct the type of due diligence and monitoring that enables it to identify and evaluate risks and opportunities.

Demonstrated Ability to Structure Investments Creatively. Stellus Capital Management has the expertise and ability to structure investments across all levels of a company s capital structure. Furthermore, we believe that current market conditions will allow us to structure attractively priced debt investments and may allow us to incorporate other return-enhancing mechanisms such as commitment fees, original issue discounts, early redemption premiums, payment-in-kind, or PIK, interest or some form of equity securities.

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Resources of Stellus Capital Management Platform. We have access to the resources and capabilities of Stellus Capital Management, which has 17 investment professionals, including Messrs. Robert T. Ladd, Dean D Angelo, Joshua T. Davis, W. Todd Huskinson and Todd A. Overbergen, who are supported by six managing directors, two principals, two vice presidents and three analysts. These individuals have developed long-term relationships with middle-market companies, management teams, financial sponsors, lending institutions and deal intermediaries by providing flexible financing throughout the capital structure. We believe that these relationships provide us with a competitive advantage in identifying investment opportunities in our target market. We also expect to benefit from Stellus Capital Management s due diligence, credit analysis, origination and transaction execution experience and capabilities, including the support provided with respect to those functions by Mr. Huskinson, who serves as our chief financial officer and chief compliance officer, and his staff of eight finance and operations professionals.

Investment Strategy

The Stellus Capital Management investment professionals employ an opportunistic and flexible investing approach, combined with strong risk management processes, which we believe will yield a highly diversified portfolio across companies, industries, and investment types. We seek direct origination opportunities of first lien, second lien, unitranche and mezzanine debt financing, with corresponding equity co-investments, in middle-market companies. We believe that businesses in this size range often have limited access to public financial markets, and will benefit from Stellus Capital Management s reliable lending partnership. Many financing providers have chosen to focus on large corporate clients and managing capital markets transactions rather than lending to middle-market businesses. Further, many financial institutions and traditional lenders are faced with constrained balance sheets and are requiring existing borrowers to reduce leverage.

With an average of over 28 years of investing, corporate finance, restructuring, consulting and accounting experience, the senior investment professionals of Stellus Capital Management has demonstrated investment expertise throughout the balance sheet and in a variety of situations, including financial sponsor buyouts, growth capital, debt refinancings, balance sheet recapitalizations, rescue financings, distressed opportunities, and acquisition financings. Our investment philosophy emphasizes capital preservation through superior credit selection and risk mitigation. We expect our portfolio to provide downside protection through conservative cash flow and asset coverage requirements, priority in the capital structure and information requirements. We also anticipate benefiting from equity participation through warrants and other equity instruments structured as part of our investments. This flexible approach enables Stellus Capital Management to respond to market conditions and offer customized lending solutions.

Stellus Capital Management invests across a wide range of industries with deep expertise in select verticals including, but not limited to, business services, retail, general industrial, government services, healthcare, software and specialty finance. Our typical transactions include providing financing for leveraged buyouts, acquisitions, recapitalizations, growth opportunities, rescue financings, distressed or turnaround situations and bridge loans. We seek to maintain a diversified portfolio of investments as a method to manage risk and capitalize on specific sector trends. In addition, we intend to co-invest with private credit funds managed by Stellus Capital Management that have an identical investment strategy as us and where doing so is consistent with conditions of the exemptive order issued by the SEC.

Our objective is to act as the lead or largest investor in transactions, generally investing between $5 million and $30 million per transaction. We expect the average investment holding period to be between two and four years, depending upon portfolio company objectives and conditions in the capital markets.

We focus on middle-market companies with between $5 million and $50 million of EBITDA in a variety of industry sectors with positive long-term dynamics and dependable cash flows. We seek businesses with management teams with demonstrated track records and economic incentives in strong franchises and sustainable competitive advantages with dependable and predictable cash flows.

We employ leverage prudently and within the limitations of the applicable laws and regulations for BDCs. Any decision on our part to use leverage will depend upon our assessment of the attractiveness of available investment opportunities in relation to the costs and perceived risks of such leverage.

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Transaction Sourcing

As access to investment opportunities is highly relationship-driven, the senior investment team and other investment professionals of Stellus Capital Management spend considerable time developing and maintaining contacts with key deal sources, including private equity firms, investment banks and senior lenders. The senior investment team and other investment professionals of Stellus Capital Management have been actively investing in the middle-market for the past decade and have focused on extensive calling and marketing efforts via speaking engagements, sponsorships, industry events and referrals to broaden their relationship network. Existing relationships are constantly cultivated through transactional work and other personal contacts.

In addition to financial sponsors, Stellus Capital Management has developed a network of other deal sources, including:

- management teams and entrepreneurs;
- portfolio companies of private equity firms;
- other investment firms that have similar strategies to Stellus Capital Management and are seeking co-investors;
- placement agents and investment banks representing financial sponsors and issuers;
- corporate operating advisers and other financial advisers; and
- consultants, attorneys and other service providers to middle-market companies and financial sponsors.

We believe that Stellus Capital Management s broad network of deal origination contacts will afford us with a continuous source of investment opportunities.

These origination relationships provide access not only to potential investment opportunities but also to market intelligence on trends across the credit markets. Since inception, Stellus Capital Management has completed financing transactions with more than 130 equity sponsors and completed multiple financing transactions with 29 of those equity sponsors.

We believe that, over the past decade, the senior investment team and other investment professionals of Stellus Capital Management have built a reputation as a thoughtful and disciplined provider of capital to middle-market companies and a preferred financing source for private equity sponsors and management teams. We believe these factors give Stellus Capital Management a competitive advantage in sourcing investment opportunities, which are put to use for our benefit.

Investment Structuring

Stellus Capital Management believes that each investment has unique characteristics that must be considered, understood and analyzed. Stellus Capital Management structures investment terms based on the business, the credit profile, the outlook for the industry in which a potential portfolio company operates, the competitive landscape, the products or services which the company sells and the management team and ownership of the company, among other factors. Stellus Capital Management relies upon the analysis conducted and information gathered through the investment process to evaluate the appropriate structure for our investments.

We invest primarily in the debt securities of middle-market companies. Our investments typically carry a high level of cash pay interest and may incorporate other return-enhancing mechanisms such as commitment fees, original issue discounts, early redemption premiums, PIK interest and some form of equity participation, including preferred stock, common stock, warrants and other forms of equity participation. We expect that a typical debt investment in which we invest will have a term at origination of between five and seven years. We expect to hold most of our investments to maturity or repayment, but we may sell some of our investments earlier if a liquidity event occurs, such as a sale, recapitalization or worsening of the credit quality of the portfolio company.

Stellus Capital Management negotiates covenants in connection with debt investments that provide protection for us but allow appropriate flexibility for the portfolio company. Such covenants may include

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affirmative and negative covenants, default penalties, lien protection and change of control provisions. Stellus Capital Management requires comprehensive information rights including access to management, financial statements and budgets and, in some cases, membership on the board of directors or board of directors observation rights. Additionally, Stellus Capital Management generally requires financial covenants and terms that restrict an issuer s use of leverage and limitations on asset sales and capital expenditures.

Secured Debt

Secured debt, including first lien, second lien and unitranche financing, has liens on the assets of the borrower that serve as collateral in support of the repayment of such loans.

First Lien Debt. First lien debt is structured with first-priority liens on the assets of the borrower that serve as collateral in support of the repayment of such loans. First lien loans may provide for moderate loan amortization in the early years of the loan, with the majority of the amortization deferred until loan maturity.

Second Lien Debt. Second lien debt is structured as junior, secured loans, with second priority liens on an issuer s assets. These loans typically provide for moderate loan amortization in the initial years of the loan, with the majority of the amortization deferred until loan maturity.

Unitranche Debt. Unitranche debt typically is structured as first lien loans with certain risk characteristics of second lien debt. Unitranche debt typically provides for moderate loan amortization in the initial years of the debt, with the majority of the principal payment deferred until loan maturity. Since unitranche debt generally allows the borrower to make a large lump sum payment of principal at the end of the loan term, there is a risk of loss if the borrower is unable to pay the lump sum or refinance the amount owed at maturity. In some cases, we will be the sole lender, or we together with our affiliates will be the sole lender, of unitranche debt, which can provide us with more influence interacting with a borrower in terms of monitoring and, if necessary, remediation in the event of underperformance.

Mezzanine Debt

Mezzanine debt, including senior unsecured and subordinated loans, is not secured by any collateral and is effectively subordinated to the borrower s secured indebtedness (to the extent of the collateral securing such indebtedness), including pursuant to one or more intercreditor agreements that we enter into with holders of a borrower s senior debt.

Senior Unsecured Loans. Senior unsecured loans are structured as loans that rank senior in right of payment to any of the borrower s unsecured indebtedness that is contractually subordinated to such loans. These loans generally provide for fixed interest rates and amortize evenly over the term of the loan. Senior unsecured loans are generally less volatile than subordinated loans due to their priority over subordinated loans.

Subordinated Loans. Subordinated loans are structured as unsecured, subordinated loans that provide for relatively high, fixed interest rates that provide us with significant current interest income. These loans typically have interest-only payments (often representing a combination of cash pay and PIK interest) in the early years, with amortization of principal deferred to maturity. Subordinated loans generally allow the borrower to make a large lump sum payment of principal at the end of the loan term, and there is a risk of loss if the borrower is unable to pay the lump sum or refinance the amount owed at maturity. Subordinated loans are generally more volatile than secured loans and senior unsecured loans and may involve a greater risk of loss of principal as compared to other types of loans. Subordinated loans often include a PIK feature, which effectively operates as negative amortization of loan principal, thereby increasing credit risk exposure over the life of the loan.

Equity Securities

In connection with some of our debt investments, we may also invest in preferred or common stock or receive nominally priced warrants or options to buy an equity interest in the portfolio company. As a result, as a portfolio company appreciates in value, we may achieve additional investment return from this equity interest. We may structure such equity investments and warrants to include provisions protecting our rights as a minority-interest holder, as well as a put, or right to sell such securities back to the issuer, upon the occurrence of specified events. In many cases, we may also seek to obtain registration rights in connection with these equity interests, which may include demand and piggyback registration rights.

Investment Process

Through the resources of Stellus Capital Management, we have access to significant research resources, experienced investment professionals, internal information systems and a credit analysis framework and investment process. Stellus Capital Management has designed a highly involved and interactive investment management process, which is the core of its culture and the basis for what we believe is a strong track record of investment returns. The investment process seeks to select only those investments which it believes have the most attractive risk/reward characteristics. The process involves several levels of review and is coordinated in an effort to identify risks in potential investments. Stellus Capital Management applies its expertise to screen our investment opportunities as described below. This rigorous process, combined with our broad origination capabilities, has allowed the Stellus Capital Management team to be prudent in selecting opportunities in which to make an investment.

All potential investment opportunities undergo an initial informal review by Stellus Capital Management s investment professionals. Each potential investment opportunity that an investment professional determines merits consideration is presented and evaluated at a weekly meeting in which Stellus Capital Management s investment professionals discuss the merits and risks of a potential investment opportunity as well as the due diligence process and the pricing and structure. If Stellus Capital Management s investment professionals believe an investment opportunity merits further review, the deal team prepares and presents to the investment committee for initial review a prescreen memorandum that generally describes the potential transaction and includes a description of the risks, due diligence process and proposed structure and pricing for the proposed investment opportunity.

Prior to making an investment, Stellus Capital Management conducts rigorous diligence on each investment opportunity. In connection with its due diligence on a potential investment opportunity, Stellus Capital Management utilizes its internal diligence resources which include its internally developed credit analytical framework, subscriptions to third party research resources, discussions with industry experts, internal information sharing systems and the analytical expertise of its investment professionals. Stellus Capital Management typically reviews the company s historical financials; industry drivers and outlook, competitive threats, customer concentration, asset coverage, projected financials and credit metrics; management background checks; and, if applicable, the track record and funding capabilities of the private equity sponsor.

Upon review of the prescreen memorandum, if the investment committee determines to proceed with the review of an investment opportunity, the deal team continues its diligence and deal structuring plans, and prepares a credit approval memorandum for review by the investment committee. The credit approval memorandum, updates the prescreen memorandum with more deal specific detail, including an update to the diligence process and any changes in the structure and pricing of the proposed investment. Upon unanimous approval by the investment committee of the proposed investment as presented in the credit approval memorandum, Stellus Capital Management s Chief Investment Officer reviews any amendments before finalizing and closing negotiations with the prospective portfolio company.

Investment Committee

Each new investment opportunity is unanimously approved by Stellus Capital Management s investment committee. Follow-on investments in existing portfolio companies require the investment committee s approval beyond that obtained when the initial investment in the company was made. The purpose of Stellus Capital Management s investment committee is to evaluate and approve all of our investments, subject at all times to the oversight and approval of our board of directors. The investment committee process is intended to bring the diverse experience and perspectives of the committee s members to the analysis and consideration of each investment. The investment committee consists of Messrs. Ladd, D Angelo, Davis, Overbergen and Huskinson. The investment committee serves to provide investment consistency and adherence to our core investment philosophy and policies. The investment committee also determines appropriate investment sizing and suggests ongoing monitoring requirements.

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In addition to reviewing investments, investment committee meetings serve as a forum to discuss credit views and outlooks. Potential transactions and deal flow are reviewed on a regular basis. Members of the investment team are encouraged to share information and views on credits with the investment committee early in their analysis. We believe this process improves the quality of the analysis and assists the deal team members to work more efficiently.

Each transaction is presented to the investment committee in a formal written report. All of our new investments require unanimous approval by the investment committee. Each member of the investment committee performs a similar role for other accounts managed by Stellus Capital Management. In certain instances, including in connection with co-investments under our exemptive order, approval of the Board may also be required prior to the making of an investment.

Monitoring Investments

In most cases, we do not have board influence over portfolio companies. In some instances, Stellus Capital Management s investment professionals may obtain board representation or observation rights in conjunction with our investments. Stellus Capital Management takes an active approach in monitoring all investments, including reviews of financial performance on at least a quarterly basis and regular discussions with management. The monitoring process begins with structuring terms and conditions, which require the timely delivery and access to critical financial and business information on portfolio companies.

Specifically, Stellus Capital Management s monitoring system consists of the following activities:

Regular Investment Committee Updates. Key portfolio company developments are discussed each week as part of the standard investment committee meeting agenda.

Written Reports. The deal teams provide periodic written updates as appropriate for key events that impact portfolio company performance or valuation. In addition, deal teams provide written updates following each portfolio company board meeting.

Quarterly Full Portfolio Review. Stellus Capital Management s Chief Investment Officer and our Chief Compliance Officer perform a quarterly comprehensive review of every portfolio company with the deal teams. This process includes a written performance and valuation update, and credit-specific discussion on each of our portfolio companies. In addition, pursuant to our valuation policy, quarterly valuations are reviewed by our independent third party valuation firm.

As part of the monitoring process, Stellus Capital Management also tracks developments in the broader marketplace. Stellus Capital Management s investment professionals have a wealth of information on the competitive landscape, industry trends, relative valuation metrics, and analyses that assist in the execution of our investment strategy. In addition, Stellus Capital Management s extensive communications with brokers and dealers allows its investment professionals to monitor market and industry trends that could affect portfolio investments. Stellus Capital Management may provide ongoing strategic, financial and operational guidance to some portfolio companies either directly or by recommending its investment professionals or other experienced representatives to participate on the board of directors. Stellus Capital Management maintains an extensive network of strategic and operational advisers to call upon for industry expertise or to supplement existing management teams.

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Asset Quality

In addition to various risk management and monitoring tools, Stellus Capital Management uses an investment ranking system to characterize and monitor the credit profile and expected level of returns on each investment in our portfolio. This investment ranking system uses a five-level numeric scale. The following is a description of the conditions associated with each investment category:

Investment Category 1 is used for investments that are performing above expectations, and whose risks remain favorable compared to the expected risk at the time of the original investment.

Investment Category 2 is used for investments that are performing within expectations and whose risks remain neutral compared to the expected risk at the time of the original investment. All new loans are initially rated 2.

Investment Category 3 is used for investments that are performing below expectations and that require closer monitoring, but where no loss of return or principal is expected. Portfolio companies with a rating of 3 may be out of compliance with financial covenants.

Investment Category 4 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are often in work out. Investments with a rating of 4 are those for which some loss of contractual return but no loss of principal is expected.

Investment Category 5 is used for investments that are performing substantially below expectations and whose risks have increased substantially since the original investment. These investments are almost always in work out. Investments with a rating of 5 are those for which some loss of return and principal is expected.

In the event that Stellus Capital Management determines that an investment is underperforming, or circumstances suggest that the risk associated with a particular investment has significantly increased, Stellus Capital Management will increase its monitoring intensity and prepare regular updates for the investment committee, summarizing current operating results and material impending events and suggesting recommended actions. While the investment ranking system identifies the relative risk for each investment, the ranking alone does not dictate the scope and/or frequency of any monitoring that is performed. The frequency of Stellus Capital Management s monitoring of an investment is determined by a number of factors, including, but not limited to, the trends in the financial performance of the portfolio company, the investment structure and the type of collateral securing the investment.

Determination of Net Asset Value and Portfolio Valuation Process

The net asset value per share of our outstanding shares of common stock is determined quarterly by dividing the value of total assets minus liabilities by the total number of shares outstanding.

In calculating the value of our total assets, investment transactions will be recorded on the trade date. Realized gains or losses will be computed using the specific identification method. Investments for which market quotations are readily available are valued at such market quotations. Debt and equity securities that are not publicly traded or whose market price is not readily available are valued at fair value as determined in good faith by our board of directors based on the input of our management and audit committee. In addition, our board of directors retains one or more independent valuation firms to review at least twice annually, the valuation of each portfolio investment for which a market quotation is not readily available. We also have adopted Accounting Standards Board Accounting Standards Codification 820, Fair Value Measurements and Disclosures, or ASC 820. This accounting statement requires us to assume that the portfolio investment is assumed to be sold in the principal market to market participants, or in the absence of a principal market, the most advantageous market, which may be a hypothetical market. Market participants are defined as buyers and sellers in the principal or most advantageous market that are independent, knowledgeable, and willing and able to transact. In accordance with ASC 820, the market in which we can exit portfolio investments with the greatest volume and level activity is considered our principal market.

A readily available market value is not expected to exist for most of the investments in our portfolio, and we value these portfolio investments at fair value as determined in good faith by our board of directors under our valuation policy and process. The types of factors that our board of directors may take into account in

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determining the fair value of our investments generally include, as appropriate, comparisons of financial ratios portfolio company to peer companies that are public, the nature and realizable value of any collateral, the portfolio company s ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business, and other relevant factors.

When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, we consider the pricing indicated by the external event to corroborate our valuation. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of the investments may differ materially from the values that would have been used had a readily available market value existed for such investments. In addition, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different from the valuations currently assigned.

With respect to investments for which market quotations are not readily available, our board of directors undertakes a multi-step valuation process each quarter, as described below:

our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals of Stellus Capital Management responsible for the portfolio investment;
preliminary valuation conclusions are then documented and discussed with our senior investment professionals and Stellus Capital Management;
at least twice annually, the valuation for each portfolio investment is reviewed by an independent valuation firm;
the audit committee of our board of directors then reviews these preliminary valuations and makes a recommendation to our board of directors; and
the board of directors then discusses the valuations and determines the fair value of each investment in our portfolio in good faith, based on the input of Stellus Capital Management, the independent valuation firm and the audit committee.

In following these approaches, the types of factors that are taken into account in fair value pricing our investments include, as relevant, but are not limited to:

available current market data, including relevant and applicable market trading and transaction comparables;
applicable market yields and multiples;
security covenants;
call protection provisions;
information rights;
the nature and realizable value of any collateral;
the portfolio company s ability to make payments, its earnings and discounted cash flows and the markets in which it does business;
comparisons of financial ratios of peer companies that are public;
comparable merger and acquisition transactions; and
the principal market and enterprise values.

Realization of Investments

The potential exit scenarios of a portfolio company play an important role in evaluating investment decisions. As such, Stellus Capital Management formulates specific exit strategies at the time of investment. Our debt-orientation provides for increased potential exit opportunities, including (a) the sale of investments in the private markets, (b) the refinancing of investments held, often due to maturity or recapitalizations, and

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(c) other liquidity events including the sale or merger of the portfolio company. Since we seek to maintain a debt orientation in our investments, we expect to receive interest income over the course of the investment period, resulting in a significant return on invested capital well in advance of final exit.

Derivatives

We may utilize hedging techniques such as interest rate swaps to mitigate potential interest rate risk on our indebtedness. Such interest rate swaps would principally be used to protect us against higher costs on our indebtedness resulting from increases in both short-term and long-term interest rates. We also may use various hedging and other risk management strategies to seek to manage various risks, including changes in currency exchange rates and market interest rates. Such hedging strategies would be utilized to seek to protect the value of our portfolio investments, for example, against possible adverse changes in the market value of securities held in our portfolio.

Managerial Assistance

As a BDC, we offer, and must provide upon request, managerial assistance to our portfolio companies. This assistance could involve monitoring the operations of our portfolio companies, participating in board and management meetings, consulting with and advising officers of portfolio companies and providing other organizational and financial guidance. Stellus Capital Management or an affiliate of Stellus Capital Management provides such managerial assistance on our behalf to portfolio companies that request this assistance. We may receive fees for these services and will reimburse Stellus Capital Management or an affiliate of Stellus Capital Management for its allocated costs in providing such assistance, subject to the review by our board of directors, including our independent directors.

Competition

Our primary competitors in providing financing to middle-market companies include public and private funds, other BDCs, commercial and investment banks, commercial financing companies and, to the extent they provide an alternative form of financing, private equity and hedge funds. Many of our competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, we believe some competitors may have access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC or to the distribution and other requirements we must satisfy to maintain our qualification as a RIC.

We use the expertise of the investment professionals of Stellus Capital Management to which we have access to assess investment risks and determine appropriate pricing for our investments in portfolio companies. In addition, we believe that the relationships of the investment professionals of Stellus Capital Management enable us to learn about, and compete effectively for, financing opportunities with attractive middle-market companies in the industries in which we invest.

Employees

We do not have any direct employees, and our day-to-day investment operations are managed by Stellus Capital Management. We have a chief executive officer and president and a chief financial officer and chief compliance officer. To the extent necessary, our board of directors may hire additional personnel going forward. Our officers are employees of Stellus Capital Management and our allocable portion of the cost of our chief financial officer and chief compliance officer and his staff is paid by us pursuant to the administration agreement that we have entered into with Stellus Capital Management.

Properties

We do not own any real estate or other physical properties materially important to our operation. Our headquarters are located at 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027. All locations are provided to us by Stellus Capital Management pursuant to the administration agreement. We believe that our office facilities are suitable and adequate for our business as we contemplate conducting it.

Legal Proceedings

We and Stellus Capital Management are not currently subject to any material legal proceedings.

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PORTFOLIO COMPANIES

The following table sets forth certain unaudited information as of March 31, 2018, for the portfolio companies in which we had a debt or equity investment. Other than these investments, our only formal relationships with our portfolio companies are the managerial assistance ancillary to our investments and the board observer or participation rights we may receive in connection with our investment. We do not control any of our portfolio companies, as defined in the 1940 Act. In general, under the 1940 Act, we would control a portfolio company if we owned more than 25.0% of its voting securities and would be an affiliate of a portfolio company if we owned 5.0% or more of its voting securities.

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