



# Stellus Capital Management (SCM)

Updated September 9<sup>th</sup>, 2026, by Josh Arnold

## Key Metrics

|                             |        |                                            |            |                                  |          |
|-----------------------------|--------|--------------------------------------------|------------|----------------------------------|----------|
| <b>Current Price:</b>       | \$8.40 | <b>5 Year CAGR Estimate:</b>               | 9.0%       | <b>Market Cap:</b>               | \$239 M  |
| <b>Fair Value Price:</b>    | \$8.24 | <b>5 Year Growth Estimate:</b>             | 0.0%       | <b>Ex-Dividend Date:</b>         | 09/30/26 |
| <b>% Fair Value:</b>        | 102%   | <b>5 Year Valuation Multiple Estimate:</b> | -0.4%      | <b>Dividend Payment Date:</b>    | 10/15/26 |
| <b>Dividend Yield:</b>      | 11.9%  | <b>5 Year Price Target</b>                 | \$8.24     | <b>Years Of Dividend Growth:</b> | 0        |
| <b>Dividend Risk Score:</b> | F      | <b>Sector:</b>                             | Financials | <b>Rating:</b>                   | Sell     |

## Overview & Current Events

Stellus Capital Management is a business development company, or BDC, that bills itself as a flexible source of capital for the middle market. The company provides capital solutions to companies with \$5 million to \$50 million of EBITDA and does so with a variety of instruments, the majority of which are debt. Stellus provides first lien, second lien, mezzanine, convertible debt, and equity investments to a diverse group of customers, generally at high yields, in the US and Canada. The company was formed in 2012, should produce just under \$100 million in revenue for 2026, and has a \$239 million market cap.

Stellus posted second quarter earnings on August 11<sup>th</sup>, 2026, and results were as expected. Net investment income was 26 cents per share for the quarter. Investment income was \$22.3 million, down from \$25.7 million a year earlier. Most of the company's investment income is from interest income from its portfolio investments, so it is highly sensitive to interest rates.

The portfolio ended the quarter at \$968 million across 116 portfolio companies. This was down from \$990 million at the end of the March quarter. The company noted it received five full repayments totaling \$38.7 million, a \$500k equity realization that resulted in a \$200k loss, and \$10 million of other repayments that were at par value.

As of the end of the quarter 100% of loans were secured and 92% were at floating rates. The company noted that credit performance was "mixed" against its plan, with 74% of the portfolio rated 1 or 2, and 26% at 3 or below. Five portfolio companies are at the non-accrual stage, accounting for 8.5% of the total cost of the portfolio.

The company cut its dividend once again, this time to an annualized payout of \$1 per share. We've left our estimate of NII-per-share at \$1.03 for this year.

## Growth on a Per-Share Basis

| Year                      | 2016   | 2017   | 2018   | 2019   | 2020   | 2021   | 2022   | 2023   | 2024   | 2025   | 2026          | 2031          |
|---------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|---------------|---------------|
| <b>NII</b>                | \$1.39 | \$1.21 | \$1.42 | \$1.23 | \$1.13 | \$1.12 | \$1.46 | \$1.92 | \$1.64 | \$1.30 | <b>\$1.03</b> | <b>\$1.03</b> |
| <b>DPS</b>                | \$1.36 | \$1.36 | \$1.36 | \$1.36 | \$1.09 | \$1.08 | \$1.36 | \$1.60 | \$1.60 | \$1.60 | <b>\$1.00</b> | <b>\$0.90</b> |
| <b>Shares<sup>1</sup></b> | 12.5   | 14.9   | 16.0   | 18.9   | 19.5   | 19.5   | 19.7   | 24.1   | 27.5   | 28.9   | <b>30</b>     | <b>35</b>     |

Stellus, like most BDCs, has a difficult time growing NII. The combination of high funding costs (generally with debt and/or preferred stock) as well as varying yields on the company's debt portfolio, make it difficult to offset a rising share count over time. We see 0% earnings change going forward from 2026's low base.

Stellus has reset much of its investment portfolio with higher rates, leading to a very strong portfolio yield. However, a possible headwind to this is interest rates declining off currently elevated levels. The company's net assets continue to grow over time, but these gains have been largely offset by a rising share count. We think the share count will continue to be a headwind moving forward, and that Stellus will have a difficult time offsetting this with earnings gains. The company's lending margins have also worsened steadily, and we see this as a continued headwind for the foreseeable future. We note credit quality is getting noticeably worse as of the midpoint of 2026.

<sup>1</sup> Share count in millions

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## Valuation Analysis

| Year       | 2016  | 2017 | 2018  | 2019 | 2020  | 2021 | 2022  | 2023  | 2024  | 2025  | Now   | 2031  |
|------------|-------|------|-------|------|-------|------|-------|-------|-------|-------|-------|-------|
| Avg. P/NII | 7.5   | 11.3 | 9.0   | 11.4 | 8.4   | 11.5 | 9.1   | 6.7   | 8.4   | 9.8   | 8.2   | 8.0   |
| Avg. Yld.  | 13.0% | 9.9% | 10.6% | 9.7% | 12.8% | 8.4% | 10.3% | 12.5% | 11.6% | 12.6% | 11.9% | 11.0% |

Stellus has traded with an average price-to-NII ratio of ~10 in its history as a public company, and we assess fair value at 8 times NII. We note, however, that Stellus' valuation has moved somewhat erratically, trading for 7.5 times NII in 2016 and then 11.3 times the next year, for instance. We see the stock as slightly overvalued today given it trades for 8.2 times NII, implying little impact from the valuation.

The dividend yield is now 11.9%, which is elevated by any standard. Stellus moved from a monthly dividend to a quarterly one, which accompanied the dividend cut from \$1.36 annually to \$1.00. It was then reinstated as a monthly payout, and raised to \$1.60 annually, cut to \$1.36, and now cut again to \$1.00. We have noted the risks of a cut in prior updates, and it's now come to fruition. The new payout is far from safe, but is more sustainable than \$1.36 was.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

| Year   | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 | 2031 |
|--------|------|------|------|------|------|------|------|------|------|------|------|------|
| Payout | 98%  | 112% | 96%  | 111% | 96%  | 96%  | 93%  | 83%  | 98%  | 123% | 97%  | 88%  |

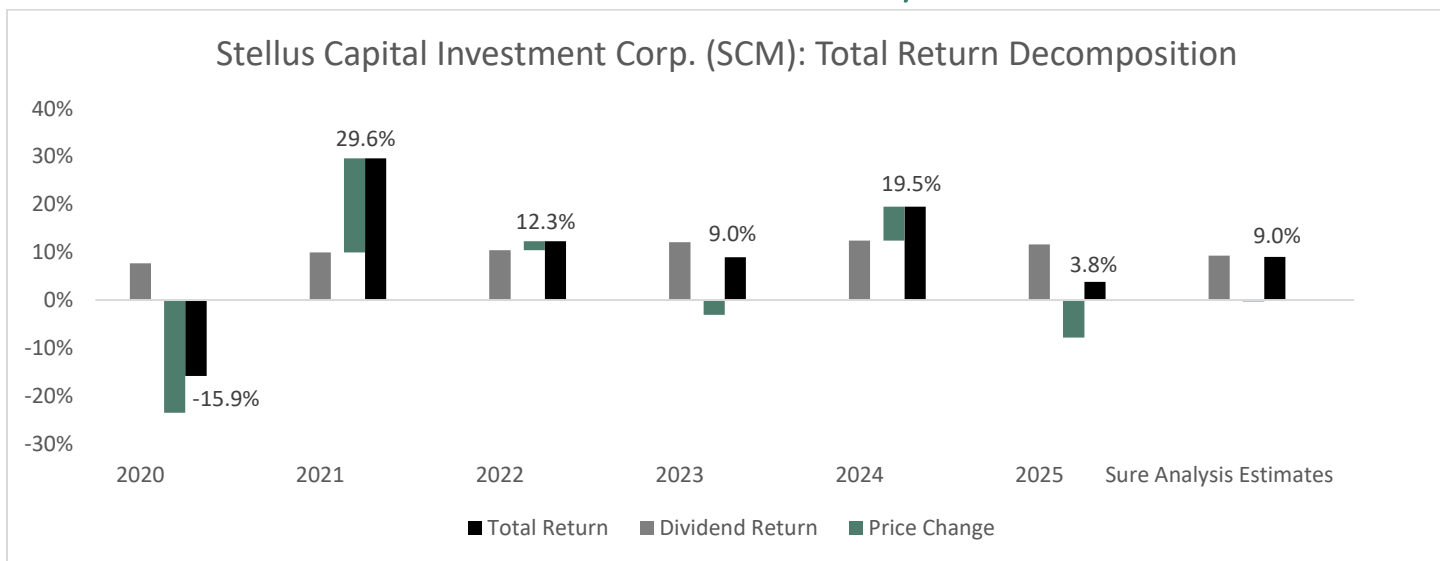
Stellus, like other BDCs, has no competitive advantages. It offers the same products as any other BDC to the same set of customers, so advantages are virtually impossible to achieve. In addition, BDCs suffer mightily during recessions because borrowers have a more difficult time meeting repayment timelines. Stellus wasn't around during the last recession, but we see it as having significant issues with NII generation during future recessions.

Stellus is required to pay all its NII and then some in distributions as a BDC, so the payout ratio will always be high. While the current payout should be safe for the time being, we note that the risk of lower rates means the payout is constantly at risk as well. Stellus has not cut its dividend yet, but we believe it is just a matter of time.

## Final Thoughts & Recommendation

Total return potential comes in at 9% annually. Given the lack of dividend safety, we're reiterating the stock at a sell rating. The yield is very high at 11.9%, but we note the risks of owning a small BDC are high as well, so only investors with high-risk tolerances should consider Stellus. The stock is quite unattractive and full of risk.

## Total Return Breakdown by Year



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## Income Statement Metrics

| Year             | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  | 2022  | 2023  | 2024  | 2025  |
|------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue          | 26    | 27    | 31    | 32    | 26    | 43    | 21    | 21    | 51    | 104   |
| Gross Profit     | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | 79    |
| Gross Margin     | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | 76.1% |
| SG&A Exp.        | 4     | 5     | 4     | 4     | 5     | 5     | 5     | 6     | 6     | ---   |
| Operating Profit | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | 64    |
| Operating Margin | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | ---   | 61.6% |
| Net Profit       | 23    | 23    | 26    | 26    | 20    | 34    | 14    | 18    | 46    | 27    |
| Net Margin       | 87.7% | 83.0% | 84.3% | 83.4% | 78.0% | 78.7% | 66.7% | 85.7% | 89.5% | 26.1% |
| Free Cash Flow   | 9     | 19    | (102) | (93)  | (3)   | (76)  | (56)  | (17)  | (29)  | 30    |
| Income Tax       | (0)   | (0)   | 1     | 1     | 1     | 4     | 1     | (2)   | 2     | 2     |

## Balance Sheet Metrics

| Year                 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025  |
|----------------------|------|------|------|------|------|------|------|------|------|-------|
| Total Assets         | 380  | 400  | 526  | 649  | 675  | 821  | 898  | 908  | 981  | 1,041 |
| Cash & Equivalents   | 9    | 25   | 17   | 16   | 18   | 44   | 48   | 26   | 20   | 209   |
| Accounts Receivable  | ---  | ---  | ---  | ---  | ---  | ---  | ---  | ---  | ---  | 1,041 |
| Total Liabilities    | 209  | 180  | 301  | 378  | 402  | 536  | 622  | 588  | 611  | 670   |
| Accounts Payable     | 3    | 3    | 4    | 4    | 2    | 5    | 5    | 5    | 9    | ---   |
| Long-Term Debt       | 203  | 174  | 292  | 366  | 393  | 518  | 604  | 576  | 593  | 652   |
| Shareholder's Equity | 171  | 220  | 225  | 271  | 273  | 285  | 276  | 320  | 370  | 371   |
| LTD/E Ratio          | 1.19 | 0.79 | 1.30 | 1.35 | 1.44 | 1.82 | 2.19 | 1.80 | 1.60 | 1.76  |

## Profitability & Per Share Metrics

| Year             | 2016  | 2017  | 2018  | 2019  | 2020  | 2021  | 2022  | 2023  | 2024  | 2025 |
|------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|------|
| Return on Assets | 6.2%  | 5.8%  | 5.7%  | 4.5%  | 3.1%  | 4.5%  | 1.7%  | 1.9%  | 4.9%  | 2.7% |
| Return on Equity | 13.8% | 11.6% | 11.8% | 10.7% | 7.4%  | 12.0% | 5.2%  | 5.9%  | 13.3% | 7.3% |
| ROIC             | 6.3%  | 5.9%  | 5.7%  | 4.6%  | 3.1%  | 4.6%  | 1.7%  | 2.0%  | 4.9%  | 2.7% |
| Shares Out.      | 12.5  | 14.9  | 16.0  | 18.9  | 19.5  | 19.5  | 19.6  | 22.0  | 25.6  | 28.4 |
| Revenue/Share    | 2.12  | 1.83  | 1.95  | 1.73  | 1.33  | 2.19  | 1.07  | 0.96  | 2.00  | 3.65 |
| FCF/Share        | 0.71  | 1.27  | -6.42 | -5.10 | -0.18 | -3.90 | -2.88 | -0.78 | -1.12 | 1.06 |

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

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