

NUVEEN CALIFORNIA DIVIDEND ADVANTAGE MUNICIPAL FUND 2
Form SC 13G/A
May 09, 2011

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SCHEDULE 13G*
(Rule 13d-102)

INFORMATION TO BE INCLUDED
IN STATEMENTS FILED PURSUANT
TO RULES 13d-1(b), (c), AND
(d) AND AMENDMENTS THERETO
FILED PURSUANT TO RULE 13d-2
(AMENDMENT NO. 3)*

NUVEEN CALIFORNIA DIVIDEND ADVANTAGE MUNICIPAL FUND 2

(Name of Issuer)

Auction Rate Preferred

(Title of Class of Securities)

67069X-30-2
(See Item 2(e))

(CUSIP Number)

April 30, 2011

(Date of Event Which Requires Filing of this Statement)

Check the appropriate box to designate the rule pursuant to which this Schedule is filed:

- /X/ Rule 13d-1(b)
- / / Rule 13d-1(c)
- / / Rule 13d-1(d)

*The remainder of this cover page shall be filled out for a reporting person's initial filing on this form with respect to the subject class of securities, and for any subsequent amendment containing information which would alter the disclosures provided in a prior cover page.

The information required in the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act but shall be subject to all other provisions of the Act (however, see the Notes).

CUSIP NO. 67069X-30-2

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(See Item 2(e))

(1) NAMES OF REPORTING PERSONS
I.R.S. IDENTIFICATION NOS. OF ABOVE PERSONS (ENTITIES ONLY)

Citigroup Global Markets Inc.

(2) CHECK THE APPROPRIATE BOX IF A MEMBER OF A GROUP (SEE INSTRUCTIONS)

(a) / /
(b) / /

(3) SEC USE ONLY

(4) CITIZENSHIP OR PLACE OF ORGANIZATION New York

NUMBER OF SHARES	(5) SOLE VOTING POWER	0

BENEFICIALLY OWNED BY	(6) SHARED VOTING POWER	0

EACH REPORTING	(7) SOLE DISPOSITIVE POWER	0

PERSON WITH:	(8) SHARED DISPOSITIVE POWER	0

(9) AGGREGATE AMOUNT BENEFICIALLY OWNED BY EACH REPORTING PERSON 0

(10) CHECK IF THE AGGREGATE AMOUNT IN ROW (9) EXCLUDES CERTAIN SHARES (SEE INSTRUCTIONS) / /

(11) PERCENT OF CLASS REPRESENTED BY AMOUNT IN ROW (9) 0.0%

(12) TYPE OF REPORTING PERSON (SEE INSTRUCTIONS) BD

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(See Item 2(e))

(1) NAMES OF REPORTING PERSONS
 I.R.S. IDENTIFICATION NOS. OF ABOVE PERSONS (ENTITIES ONLY)

Citigroup Financial Products Inc.

(2) CHECK THE APPROPRIATE BOX IF A MEMBER OF A GROUP (SEE INSTRUCTIONS)

(a) / /
 (b) / /

(3) SEC USE ONLY

(4) CITIZENSHIP OR PLACE OF ORGANIZATION Delaware

NUMBER OF	(5) SOLE VOTING POWER	0
SHARES		
BENEFICIALLY	(6) SHARED VOTING POWER	0
OWNED BY		
EACH	(7) SOLE DISPOSITIVE POWER	0
REPORTING		
PERSON	(8) SHARED DISPOSITIVE POWER	0
WITH:		

(9) AGGREGATE AMOUNT BENEFICIALLY OWNED BY EACH REPORTING PERSON 0

(10) CHECK IF THE AGGREGATE AMOUNT IN ROW (9) EXCLUDES CERTAIN SHARES (SEE INSTRUCTIONS) / /

(11) PERCENT OF CLASS REPRESENTED BY AMOUNT IN ROW (9) 0.0%

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(12) TYPE OF REPORTING PERSON (SEE INSTRUCTIONS) CO

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(See Item 2(e))

(1) NAMES OF REPORTING PERSONS
I.R.S. IDENTIFICATION NOS. OF ABOVE PERSONS (ENTITIES ONLY)

Citigroup Global Markets Holdings Inc.

(2) CHECK THE APPROPRIATE BOX IF A MEMBER OF A GROUP (SEE INSTRUCTIONS)

(a) / /
(b) / /

(3) SEC USE ONLY

(4) CITIZENSHIP OR PLACE OF ORGANIZATION New York

NUMBER OF	(5) SOLE VOTING POWER	0
SHARES		
BENEFICIALLY	(6) SHARED VOTING POWER	0
OWNED BY		
EACH	(7) SOLE DISPOSITIVE POWER	0
REPORTING		
PERSON	(8) SHARED DISPOSITIVE POWER	0
WITH:		

(9) AGGREGATE AMOUNT BENEFICIALLY OWNED BY EACH REPORTING PERSON 0

(10) CHECK IF THE AGGREGATE AMOUNT IN ROW (9) EXCLUDES CERTAIN SHARES (SEE INSTRUCTIONS) / /

(11) PERCENT OF CLASS REPRESENTED BY AMOUNT IN ROW (9) 0.0%

 (12) TYPE OF REPORTING PERSON (SEE INSTRUCTIONS) HC

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(See Item 2(e))

 (1) NAMES OF REPORTING PERSONS
 I.R.S. IDENTIFICATION NOS. OF ABOVE PERSONS (ENTITIES ONLY)

Citigroup Inc.

 (2) CHECK THE APPROPRIATE BOX IF A MEMBER OF A GROUP (SEE INSTRUCTIONS)

(a) / /
 (b) / /

 (3) SEC USE ONLY

 (4) CITIZENSHIP OR PLACE OF ORGANIZATION Delaware

NUMBER OF	(5) SOLE VOTING POWER	0
SHARES		
BENEFICIALLY	(6) SHARED VOTING POWER	0
OWNED BY		
EACH	(7) SOLE DISPOSITIVE POWER	0
REPORTING		
PERSON	(8) SHARED DISPOSITIVE POWER	0
WITH:		

 (9) AGGREGATE AMOUNT BENEFICIALLY OWNED BY EACH REPORTING PERSON 0

 (10) CHECK IF THE AGGREGATE AMOUNT IN ROW (9) EXCLUDES CERTAIN SHARES (SEE
 INSTRUCTIONS) / /

(11) PERCENT OF CLASS REPRESENTED BY AMOUNT IN ROW (9) 0.0%

(12) TYPE OF REPORTING PERSON (SEE INSTRUCTIONS) HC

Item 1(a). Name of Issuer:

NUVEEN CALIFORNIA DIVIDEND ADVANTAGE MUNICIPAL FUND 2

Item 1(b). Address of Issuer's Principal Executive Offices:

John Nuveen & Co.
333 West Wacker Drive
Chicago, IL 60606

Item 2(a). Name of Person Filing:

Citigroup Global Markets Inc. ("CGM")
Citigroup Financial Products Inc. ("CFP")
Citigroup Global Markets Holdings Inc. ("CGM Holdings")
Citigroup Inc. ("Citigroup")

Item 2(b). Address of the Principal Business Office or, if none, Residence:

The address of the principal business office of each of
CGM, CFP and CGM Holdings is:

388 Greenwich Street
New York, NY 10013

The address of the principal business office of Citigroup is:

399 Park Avenue
New York, NY 10043

Item 2(c). Citizenship:

CGM and CGM Holdings are New York corporations.

CFP and Citigroup are Delaware corporations.

Item 2(d). Title of Class of Securities:

Auction Rate Preferred

Item 2(e). CUSIP Number:

67069X-20-3
67069X-30-2

- Item 3. If This Statement Is Filed Pursuant to Sections 240.13d-1(b) or 240.13d-2(b) or (c), Check Whether the Person Filing Is a(n):
- (a) Broker or dealer registered under Section 15 of the Act (15 U.S.C. 78o);
 - (b) Bank as defined in Section 3(a)(6) of the Act (15 U.S.C. 78c);
 - (c) Insurance company as defined in Section 3(a)(19) of the Act (15 U.S.C. 78c);
 - (d) Investment company registered under Section 8 of the Investment Company Act of 1940 (15 U.S.C. 80a-8);
 - (e) Investment adviser in accordance with Section 240.13d-1(b)(1)(ii)(E);
 - (f) Employee benefit plan or endowment fund in accordance with Section 240.13d-1(b)(1)(ii)(F);
 - (g) Parent holding company or control person in accordance with Section 240.13d-1(b)(1)(ii)(G);
 - (h) Savings association as defined in Section 3(b) of the Federal Deposit Insurance Act (12 U.S.C. 1813);
 - (i) Church plan that is excluded from the definition of an investment company under Section 3(c)(14) of the Investment Company Act of 1940 (15 U.S.C. 80a-3);
 - (j) A non-U.S. institution in accordance with Section 240.13d-1(b)(1)(ii)(J);
 - (k) Group, in accordance with Section 240.13d-1(b)(1)(ii)(K). If filing as a non-U.S. institution in accordance with Section 240.13d-1(b)(1)(ii)(J), please specify the type of institution: _____ .

Item 4. Ownership. (as of April 30, 2011)

These Shares represent the Reporting Person's combined holdings in multiple series of auction rate preferred securities of the issuer which are treated herein as one class of securities consistent with the Reporting Person's prior Section 13 filings made in respect of the issuer.

- (a) Amount beneficially owned: See item 9 of cover pages
- (b) Percent of class: See item 11 of cover pages
- (c) Number of shares as to which the person has:
 - (i) Sole power to vote or to direct the vote:
 - (ii) Shared power to vote or to direct the vote:
 - (iii) Sole power to dispose or to direct the disposition of:

(iv) Shared power to dispose or to direct the disposition of:

See Items 5-8 of cover pages

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Item 5. Ownership of Five Percent or Less of a Class.

If this statement is being filed to report the fact that as of the date hereof the reporting person has ceased to be the beneficial owner of more than five percent of the class of securities, check the following [X].

Item 6. Ownership of More Than Five Percent on Behalf of Another Person.

Not Applicable.

Item 7. Identification and Classification of the Subsidiary Which Acquired the Security Being Reported on by the Parent Holding Company.

CFP is the sole stockholder of CGM. CGM Holdings is the sole stockholder of CFP. Citigroup is the sole stockholder of CGM Holdings.

Item 8. Identification and Classification of Members of the Group.

Not Applicable.

Item 9. Notice of Dissolution of Group.

Not Applicable.

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Item 10. Certification.

By signing below I certify that, to the best of my knowledge and belief, the securities referred to above were acquired and are held in the ordinary course of business and were not acquired and are not held for the purpose of or with the effect of changing or influencing the control of the issuer of the securities and were not acquired and are not held in connection with or as a participant in any transaction having that purpose or effect.

SIGNATURE.

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

Dated: May 9, 2011

CITIGROUP GLOBAL MARKETS INC.

By: /s/ Ali L. Karshan

Name: Ali L. Karshan
Title: Assistant Secretary

CITIGROUP FINANCIAL PRODUCTS INC.

By: /s/ Ali L. Karshan

Name: Ali L. Karshan
Title: Assistant Secretary

CITIGROUP GLOBAL MARKETS HOLDINGS INC.

By: /s/ Ali L. Karshan

Name: Ali L. Karshan
Title: Assistant Secretary

CITIGROUP INC.

By: /s/ Ali L. Karshan

Name: Ali L. Karshan
Title: Assistant Secretary

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of 9 Pages

EXHIBIT INDEX TO SCHEDULE 13G

EXHIBIT 1

Agreement among CGM, CFP, CGM Holdings and Citigroup as to joint filing of
Schedule 13G

Opt">We have the ability to issue indenture securities with terms different from those of indenture securities previously issued and, without the consent of the holders thereof, to reopen a previous issue of a series of indenture securities and issue additional indenture securities of that series unless the reopening was restricted when that series was created.

Conversion and Exchange

If any debt securities are convertible into or exchangeable for other securities, the prospectus supplement will explain the terms and conditions of the conversion or exchange, including the conversion price or exchange ratio (or the calculation method), the conversion or exchange period (or how the period will be determined), if conversion or exchange will be mandatory or at the option of the holder or us, provisions for adjusting the conversion price or the exchange ratio and provisions affecting conversion or exchange in the event of the redemption of the underlying debt securities. These terms may also include provisions under which the number or amount of other securities to be received by the holders of the debt securities upon conversion or exchange would be calculated according to the market price of the other securities as of a time stated in the prospectus supplement.

Issuance of Securities in Registered Form

We may issue the debt securities in registered form, in which case we may issue them either in book-entry form only or in certificated form. Debt securities issued in book-entry form will be represented by global securities. We expect that we will usually issue debt securities in book-entry only form represented by global securities.

Book-Entry Holders

We will issue registered debt securities in book-entry form only, unless we specify otherwise in the applicable prospectus supplement. This means debt securities will be represented by one or more global securities registered in the name of a depositary that will hold them on behalf of financial institutions that participate in the depositary's book-entry system. These participating institutions, in turn, hold beneficial interests in the debt securities held by the depositary or its nominee. These institutions may hold these interests on behalf of themselves or customers.

Under the indenture, only the person in whose name a debt security is registered is recognized as the holder of that debt security. Consequently, for debt securities issued in book-entry form, we will recognize only the depositary as the holder of the debt securities and we will make all payments on the debt securities to the depositary. The depositary will then pass along the payments it receives to its participants, which in turn will pass the payments along to their customers who are the beneficial owners. The depositary and its participants do so under agreements they have made with one another or with their customers; they are not obligated to do so under the terms of the debt securities.

As a result, investors will not own debt securities directly. Instead, they will own beneficial interests in a global security, through a bank, broker or other financial institution that participates in the depositary's book-entry system or holds an interest through a participant. As long as the debt securities are represented by one or more global securities, investors will be indirect holders, and not holders, of the debt securities.

Street Name Holders

In the future, we may issue debt securities in certificated form or terminate a global security. In these cases, investors may choose to hold their debt securities in their own names or in street name. Debt securities held in street name are registered in the name of a bank, broker or other financial institution chosen by the investor, and the investor would hold a beneficial interest in those debt securities through the account he or she maintains at that institution.

For debt securities held in street name, we will recognize only the intermediary banks, brokers and other financial institutions in whose names the debt securities are registered as the holders of those debt securities,

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and we will make all payments on those debt securities to them. These institutions will pass along the payments they receive to their customers who are the beneficial owners, but only because they agree to do so in their customer agreements or because they are legally required to do so. Investors who hold debt securities in street name will be indirect holders, and not holders, of the debt securities.

Legal Holders

Our obligations, as well as the obligations of the applicable trustee and those of any third parties employed by us or the applicable trustee, run only to the legal holders of the debt securities. We do not have obligations to investors who hold beneficial interests in global securities, in street name or by any other indirect means. This will be the case whether an investor chooses to be an indirect holder of a debt security or has no choice because we are issuing the debt securities only in book-entry form.

For example, once we make a payment or give a notice to the holder, we have no further responsibility for the payment or notice even if that holder is required, under agreements with depository participants or customers or by law, to pass it along to the indirect holders but does not do so. Similarly, if we want to obtain the approval of the holders for any purpose (for example, to amend an indenture or to relieve us of the consequences of a default or of our obligation to comply with a particular provision of an indenture), we would seek the approval only from the holders, and not the indirect holders, of the debt securities. Whether and how the holders contact the indirect holders is up to the holders.

When we refer to you in this Description of Our Debt Securities, we mean those who invest in the debt securities being offered by this prospectus, whether they are the holders or only indirect holders of those debt securities. When we refer to your debt securities, we mean the debt securities in which you hold a direct or indirect interest.

Special Considerations for Indirect Holders

If you hold debt securities through a bank, broker or other financial institution, either in book-entry form or in street name, we urge you to check with that institution to find out:

- how it handles securities payments and notices;
- whether it imposes fees or charges;
- how it would handle a request for the holders' consent, if ever required;
- whether and how you can instruct it to send you debt securities registered in your own name so you can be a holder, if that is permitted in the future for a particular series of debt securities;
- how it would exercise rights under the debt securities if there were a default or other event triggering the need for holders to act to protect their interests; and
- if the debt securities are in book-entry form, how the depository's rules and procedures will affect these matters.

Global Securities

As noted above, we usually will issue debt securities as registered securities in book-entry form only. A global security represents one or any other number of individual debt securities. Generally, all debt securities represented by the same global securities will have the same terms.

Each debt security issued in book-entry form will be represented by a global security that we deposit with and register in the name of a financial institution or its nominee that we select. The financial institution that we select for this purpose is called the depository. Unless we specify otherwise in the applicable prospectus supplement, The Depository

Trust Company, New York, New York, known as DTC, will be the depositary for all debt securities issued in book-entry form.

A global security may not be transferred to or registered in the name of anyone other than the depositary or its nominee, unless special termination situations arise. We describe those situations below under Termination of a Global Security. As a result of these arrangements, the depositary, or its nominee, will be the sole registered owner and holder of all debt securities represented by a global security, and investors

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will be permitted to own only beneficial interests in a global security. Beneficial interests must be held by means of an account with a broker, bank or other financial institution that in turn has an account with the depository or with another institution that has an account with the depository. Thus, an investor whose security is represented by a global security will not be a holder of the debt security, but only an indirect holder of a beneficial interest in the global security.

Special Considerations for Global Securities

As an indirect holder, an investor's rights relating to a global security will be governed by the account rules of the investor's financial institution and of the depository, as well as general laws relating to securities transfers. The depository that holds the global security will be considered the holder of the debt securities represented by the global security.

If debt securities are issued only in the form of a global security, an investor should be aware of the following:

- an investor cannot cause the debt securities to be registered in his or her name and cannot obtain certificates for his or her interest in the debt securities, except in the special situations we describe below;
- an investor will be an indirect holder and must look to his or her own bank or broker for payments on the debt securities and protection of his or her legal rights relating to the debt securities, as we describe under Issuance of Securities in Registered Form above;
- an investor may not be able to sell interests in the debt securities to some insurance companies and other institutions that are required by law to own their securities in non-book-entry form;
- an investor may not be able to pledge his or her interest in a global security in circumstances where certificates representing the debt securities must be delivered to the lender or other beneficiary of the pledge in order for the pledge to be effective;
- the depository's policies, which may change from time to time, will govern payments, transfers, exchanges and other matters relating to an investor's interest in a global security. We and the trustee have no responsibility for any aspect of the depository's actions or for its records of ownership interests in a global security. We and the trustee also do not supervise the depository in any way;
- if we redeem less than all the debt securities of a particular series being redeemed, DTC's practice is to determine by lot the amount to be redeemed from each of its participants holding that series;
- an investor is required to give notice of exercise of any option to elect repayment of its debt securities, through its participant, to the applicable trustee and to deliver the related debt securities by causing its participant to transfer its interest in those debt securities, on DTC's records, to the applicable trustee;
- DTC requires that those who purchase and sell interests in a global security deposited in its book-entry system use immediately available funds, your broker or bank may also require you to use immediately available funds when purchasing or selling interests in a global security; and
- financial institutions that participate in the depository's book-entry system, and through which an investor holds its interest in a global security, may also have their own policies affecting payments, notices and other matters relating to the debt securities; there may be more than one financial intermediary in the chain of ownership for an investor; we do not monitor and are not responsible for the actions of any of those intermediaries.

Termination of a Global Security

If a global security is terminated for any reason, interests in it will be exchanged for certificates in non-book-entry form (certificated securities). After that exchange, the choice of whether to hold the certificated debt securities directly or in street name will be up to the investor. Investors must consult their own banks or brokers to find out how to have their interests in a global security transferred on termination to their own names, so that they will be holders. We have described the rights of legal holders and street name investors under Issuance of Securities in Registered Form above.

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The prospectus supplement may list situations for terminating a global security that would apply only to the particular series of debt securities covered by the prospectus supplement. If a global security is terminated, only the depositary, and not we or the applicable trustee, is responsible for deciding the investors in whose names the debt securities represented by the global security will be registered and, therefore, who will be the holders of those debt securities.

Payment and Paying Agents

We will pay interest to the person listed in the applicable trustee's records as the owner of the debt security at the close of business on a particular day in advance of each due date for interest, even if that person no longer owns the debt security on the interest due date. That day, usually about two weeks in advance of the interest due date, is called the record date. Because we will pay all the interest for an interest period to the holders on the record date, holders buying and selling debt securities must work out between themselves the appropriate purchase price. The most common manner is to adjust the sales price of the debt securities to prorate interest fairly between buyer and seller based on their respective ownership periods within the particular interest period. This prorated interest amount is called accrued interest.

Payments on Global Securities

We will make payments on a global security in accordance with the applicable policies of the depositary as in effect from time to time. Under those policies, we will make payments directly to the depositary, or its nominee, and not to any indirect holders who own beneficial interests in the global security. An indirect holder's right to those payments will be governed by the rules and practices of the depositary and its participants, as described under Special Considerations for Global Securities.

Payments on Certificated Securities

We will make payments on a certificated debt security as follows. We will pay interest that is due on an interest payment date to the holder of debt securities as shown on the trustee's records as of the close of business on the regular record date at our office and/or at other offices that may be specified in the prospectus supplement. We will make all payments of principal and premium, if any, by check at the office of the applicable trustee and/or at other offices that may be specified in the prospectus supplement or in a notice to holders against surrender of the debt security.

Alternatively, at our option, we may pay any cash interest that becomes due on the debt security by mailing a check to the holder at his, her or its address shown on the trustee's records as of the close of business on the regular record date or by transfer to an account at a bank in the United States, in either case, on the due date.

Payment When Offices Are Closed

If any payment is due on a debt security on a day that is not a business day, we will make the payment on the next day that is a business day. Payments made on the next business day in this situation will be treated under the indenture as if they were made on the original due date, except as otherwise indicated in the attached prospectus supplement. Such payment will not result in a default under any debt security or the indenture, and no interest will accrue on the payment amount from the original due date to the next day that is a business day.

Book-entry and other indirect holders should consult their banks or brokers for information on how they will receive payments on their debt securities.

Events of Default

You will have rights if an Event of Default occurs in respect of the debt securities of your series and is not cured, as described later in this subsection.

The term "Event of Default" in respect of the debt securities of your series means any of the following:

we do not pay the principal of, or any premium on, a debt security of the series within five days of its due date;
we do not pay interest on a debt security of the series within 30 days of its due date;

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we do not deposit any sinking fund payment in respect of debt securities of the series within five days of its due date; we remain in breach of a covenant in respect of debt securities of the series for 60 days after we receive a written notice of default stating we are in breach (the notice must be sent by either the trustee or holders of at least 25% of the principal amount of the outstanding debt securities of the series); we file for bankruptcy or certain other events of bankruptcy, insolvency or reorganization occur and remain undischarged or unstayed for a period of 90 days; the series of debt securities has an asset coverage, as such term is defined in the 1940 Act, of less than 100 per centum on the last business day of each of twenty-four consecutive calendar months, giving effect to any exemptive relief granted to the Company by the SEC; or any other Event of Default in respect of debt securities of the series described in the prospectus supplement occurs.

An Event of Default for a particular series of debt securities does not necessarily constitute an Event of Default for any other series of debt securities issued under the same or any other indenture. The trustee may withhold notice to the holders of debt securities of any default, except in the payment of principal, premium, interest, or sinking or purchase fund installment, if it in good faith considers the withholding of notice to be in the interest of the holders.

Remedies if an Event of Default Occurs

If an Event of Default has occurred and is continuing, the trustee or the holders of not less than 25% in principal amount of the outstanding debt securities of the affected series may (and the trustee shall at the request of such holders) declare the entire principal amount of all the debt securities of that series to be due and immediately payable. This is called a declaration of acceleration of maturity. A declaration of acceleration of maturity may be canceled by the holders of a majority in principal amount of the outstanding debt securities of the affected series if (1) we have deposited with the trustee all amounts due and owing with respect to the securities (other than principal that has become due solely by reason of such acceleration) and certain other amounts, and (2) any other Events of Default have been cured or waived.

The trustee is not required to take any action under the indenture at the request of any holders unless the holders offer the trustee protection from expenses and liability reasonably satisfactory to it (called an indemnity). If indemnity reasonably satisfactory to the trustee is provided, the holders of a majority in principal amount of the outstanding debt securities of the relevant series may direct the time, method and place of conducting any lawsuit or other formal legal action seeking any remedy available to the trustee. The trustee may refuse to follow those directions in certain circumstances. No delay or omission in exercising any right or remedy will be treated as a waiver of that right, remedy or Event of Default.

Before you are allowed to bypass your trustee and bring your own lawsuit or other formal legal action or take other steps to enforce your rights or protect your interests relating to the debt securities, the following must occur:

you must give the trustee written notice that an Event of Default with respect to the relevant series of debt securities has occurred and remains uncured; the holders of at least 25% in principal amount of all outstanding debt securities of the relevant series must make a written request that the trustee take action because of the default and must offer the trustee indemnity, security or both reasonably satisfactory to it against the costs, expenses and other liabilities of taking that action; the trustee must not have taken action for 60 days after receipt of the above notice and offer of indemnity and/or security; and the holders of a majority in principal amount of the outstanding debt securities of that series must not have given the trustee a direction inconsistent with the above notice during that 60-day period.

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However, you are entitled at any time to bring a lawsuit for the payment of money due on your debt securities on or after the due date.

Book-entry and other indirect holders should consult their banks or brokers for information on how to give notice or direction to or make a request of the trustee and how to declare or cancel an acceleration of maturity.

Each year, we will furnish to each trustee a written statement of certain of our officers certifying that to their knowledge we are in compliance with the indenture and the debt securities, or else specifying any default.

Waiver of Default

Holders of a majority in principal amount of the outstanding debt securities of the affected series may waive any past defaults other than a default

in the payment of principal, any premium or interest; or
in respect of a covenant that cannot be modified or amended without the consent of each holder.

Merger or Consolidation

Under the terms of the indenture, we are generally permitted to consolidate or merge with another entity. We are also permitted to sell all or substantially all of our assets to another entity. However, we may not take any of these actions unless all the following conditions are met:

where we merge out of existence or sell substantially all our assets, the resulting entity or transferee must agree to be legally responsible for our obligations under the debt securities;

the merger or sale of assets must not cause a default on the debt securities and we must not already be in default (unless the merger or sale would cure the default). For purposes of this no-default test, a default would include an Event of Default that has occurred and has not been cured, as described under Events of Default above. A default for this purpose would also include any event that would be an Event of Default if the requirements for giving us a notice of default or our default having to exist for a specific period of time were disregarded;

we must deliver certain certificates and documents to the trustee; and
we must satisfy any other requirements specified in the prospectus supplement relating to a particular series of debt securities.

Modification or Waiver

There are three types of changes we can make to the indenture and the debt securities issued thereunder.

Changes Requiring Your Approval

First, there are changes that we cannot make to your debt securities without your specific approval. The following is a list of those types of changes:

change the stated maturity of the principal of or interest on a debt security or the terms of any sinking fund with respect to any security;

reduce any amounts due on a debt security;

reduce the amount of principal payable upon acceleration of the maturity of an original issue discount or indexed security following a default or upon the redemption thereof or the amount thereof provable in a bankruptcy proceeding;

adversely affect any right of repayment at the holder's option;
change the place or currency of payment on a debt security (except as otherwise described in the prospectus or prospectus supplement);

impair your right to sue for payment;

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adversely affect any right to convert or exchange a debt security in accordance with its terms; modify the subordination provisions in the indenture in a manner that is adverse to outstanding holders of the debt securities;

reduce the percentage of holders of debt securities whose consent is needed to modify or amend the indenture; reduce the percentage of holders of debt securities whose consent is needed to waive compliance with certain provisions of the indenture or to waive certain defaults; modify any other aspect of the provisions of the indenture dealing with supplemental indentures with the consent of holders, waiver of past defaults, changes to the quorum or voting requirements or the waiver of certain covenants; and change any obligation we have to pay additional amounts.

Changes Not Requiring Approval

The second type of change does not require any vote by the holders of the debt securities. This type is limited to clarifications, establishment of the form or terms of new securities of any series as permitted by the indenture and certain other changes that would not adversely affect holders of the outstanding debt securities in any material respect. We also do not need any approval to make any change that affects only debt securities to be issued under the indenture after the change takes effect.

Changes Requiring Majority Approval

Any other change to the indenture and the debt securities would require the following approval:

if the change affects only one series of debt securities, it must be approved by the holders of a majority in principal amount of that series; and
if the change affects more than one series of debt securities issued under the same indenture, it must be approved by the holders of a majority in principal amount of all of the series affected by the change, with all affected series voting together as one class for this purpose.

In each case, the required approval must be given by written consent.

The holders of a majority in principal amount of a series of debt securities issued under the indenture, voting together as one class for this purpose, may waive our compliance with some of our covenants applicable to that series of debt securities. However, we cannot obtain a waiver of a payment default or of any of the matters covered by the bullet points included above under Changes Requiring Your Approval.

Further Details Concerning Voting

When taking a vote, we will use the following rules to decide how much principal to attribute to a debt security:

for original issue discount securities, we will use the principal amount that would be due and payable on the voting date if the maturity of these debt securities were accelerated to that date because of a default;
for debt securities whose principal amount is not known (for example, because it is based on an index), we will use the principal face amount at original issuance or a special rule for that debt security described in the prospectus supplement; and

for debt securities denominated in one or more foreign currencies, we will use the U.S. dollar equivalent. Debt securities will not be considered outstanding, and therefore not eligible to vote, if we have deposited or set aside in trust money for their payment or redemption or if we, any other obligor, or any affiliate of us or any obligor own such debt securities. Debt securities will also not be eligible to vote if they have been fully defeased as described later under Defeasance Full Defeasance.

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We will generally be entitled to set any day as a record date for the purpose of determining the holders of outstanding indenture securities that are entitled to vote or take other action under the indenture. However, the record date may not be more than 30 days before the date of the first solicitation of holders to vote on or take such action. If we set a record date for a vote or other action to be taken by holders of one or more series, that vote or action may be taken only by persons who are holders of outstanding indenture securities of those series on the record date and must be taken within eleven months following the record date.

Book-entry and other indirect holders should consult their banks or brokers for information on how approval may be granted or denied if we seek to change the indenture or the debt securities or request a waiver.

Defeasance

The following provisions will be applicable to each series of debt securities unless we state in the applicable prospectus supplement that the provisions of covenant defeasance and full defeasance will not be applicable to that series.

Covenant Defeasance

Under current U.S. federal tax law and the indenture, we can make the deposit described below and be released from some of the restrictive covenants in the indenture under which the particular series was issued. This is called covenant defeasance. In that event, you would lose the protection of those restrictive covenants but would gain the protection of having money and government securities set aside in trust to repay your debt securities. If we achieved covenant defeasance and your debt securities were subordinated as described under Indenture Provisions Subordination below, such subordination would not prevent the trustee under the indenture from applying the funds available to it from the deposit described in the first bullet below to the payment of amounts due in respect of such debt securities for the benefit of the subordinated debt holders. In order to achieve covenant defeasance, we must do the following:

we must deposit in trust for the benefit of all holders of a series of debt securities a combination of cash (in such currency in which such securities are then specified as payable at stated maturity) or government obligations applicable to such securities (determined on the basis of the currency in which such securities are then specified as payable at stated maturity) that will generate enough cash to make interest, principal and any other payments on the debt securities on their various due dates and any mandatory sinking fund payments or analogous payments;

we must deliver to the trustee a legal opinion of our counsel confirming that, under current U.S. federal income tax law, we may make the above deposit without causing you to be taxed on the debt securities any differently than if we did not make the deposit;

we must deliver to the trustee a legal opinion of our counsel stating that the above deposit does not require registration by us under the 1940 Act, as amended, and a legal opinion and officers certificate stating that all conditions precedent to covenant defeasance have been complied with;

defeasance must not result in a breach or violation of, or result in a default under, of the indenture or any of our other material agreements or instruments;

no default or event of default with respect to such debt securities shall have occurred and be continuing and no defaults or events of default related to bankruptcy, insolvency or reorganization shall occur during the next 90 days;

and

satisfy the conditions for covenant defeasance contained in any supplemental indentures.

If we accomplish covenant defeasance, you can still look to us for repayment of the debt securities if there were a shortfall in the trust deposit or the trustee is prevented from making payment. For example, if one of the remaining Events of Default occurred (such as our bankruptcy) and the debt securities became immediately due and payable,

there might be such a shortfall. However, there is no assurance that we would have sufficient funds to make payment of the shortfall.

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Full Defeasance

If there is a change in U.S. federal tax law or we obtain an IRS ruling, as described in the second bullet below, we can legally release ourselves from all payment and other obligations on the debt securities of a particular series (called full defeasance) if we put in place the following other arrangements for you to be repaid:

we must deposit in trust for the benefit of all holders of a series of debt securities a combination of cash (in such currency in which such securities are then specified as payable at stated maturity) or government obligations applicable to such securities (determined on the basis of the currency in which such securities are then specified as payable at stated maturity) that will generate enough cash to make interest, principal and any other payments on the debt securities on their various due dates and any mandatory sinking fund payments or analogous payments;

we must deliver to the trustee a legal opinion confirming that there has been a change in current U.S. federal tax law or an IRS ruling that allows us to make the above deposit without causing you to be taxed on the debt securities any differently than if we did not make the deposit. Under current U.S. federal tax law, the deposit and our legal release from the debt securities would be treated as though we paid you your share of the cash and notes or bonds at the time the cash and notes or bonds were deposited in trust in exchange for your debt securities and you would recognize gain or loss on the debt securities at the time of the deposit;

we must deliver to the trustee a legal opinion of our counsel stating that the above deposit does not require registration by us under the 1940 Act, as amended, and a legal opinion and officers certificate stating that all conditions precedent to defeasance have been complied with;

defeasance must not result in a breach or violation of, or constitute a default under, of the indenture or any of our other material agreements or instruments;

no default or event of default with respect to such debt securities shall have occurred and be continuing and no defaults or events of default related to bankruptcy, insolvency or reorganization shall occur during the next 90 days;

and

satisfy the conditions for full defeasance contained in any supplemental indentures.

If we ever did accomplish full defeasance, as described above, you would have to rely solely on the trust deposit for repayment of the debt securities. You could not look to us for repayment in the unlikely event of any shortfall. Conversely, the trust deposit would most likely be protected from claims of our lenders and other creditors if we ever became bankrupt or insolvent. If your debt securities were subordinated as described later under Indenture Provisions Subordination , such subordination would not prevent the trustee under the indenture from applying the funds available to it from the deposit referred to in the first bullet of the preceding paragraph to the payment of amounts due in respect of such debt securities for the benefit of the subordinated debt holders.

Form, Exchange and Transfer of Certificated Registered Securities

If registered debt securities cease to be issued in book-entry form, they will be issued:

only in fully registered certificated form;
without interest coupons; and

unless we indicate otherwise in the prospectus supplement, in denominations of \$1,000 and amounts that are multiples of \$1,000.

Holders may exchange their certificated securities for debt securities of smaller denominations or combined into fewer debt securities of larger denominations, as long as the total principal amount is not changed and as long as the denomination is greater than the minimum denomination for such securities.

Holders may exchange or transfer their certificated securities at the office of the trustee. We have appointed the trustee to act as our agent for registering debt securities in the names of holders transferring debt securities. We may appoint another entity to perform these functions or perform them ourselves.

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Holders will not be required to pay a service charge to transfer or exchange their certificated securities, but they may be required to pay any tax or other governmental charge associated with the transfer or exchange. The transfer or exchange will be made only if our transfer agent is satisfied with the holder's proof of legal ownership.

If we have designated additional transfer agents for your debt security, they will be named in the prospectus supplement. We may appoint additional transfer agents or cancel the appointment of any particular transfer agent. We may also approve a change in the office through which any transfer agent acts.

If any certificated securities of a particular series are redeemable and we redeem less than all the debt securities of that series, we may block the transfer or exchange of those debt securities during the period beginning 15 days before the day we mail the notice of redemption and ending on the day of that mailing, in order to freeze the list of holders to prepare the mailing. We may also refuse to register transfers or exchanges of any certificated securities selected for redemption, except that we will continue to permit transfers and exchanges of the unredeemed portion of any debt security that will be partially redeemed.

If a registered debt security is issued in book-entry form, only the depository will be entitled to transfer and exchange the debt security as described in this subsection, since it will be the sole holder of the debt security.

Resignation of Trustee

Each trustee may resign or be removed with respect to one or more series of indenture securities provided that a successor trustee is appointed to act with respect to these series and has accepted such appointment. In the event that two or more persons are acting as trustee with respect to different series of indenture securities under the indenture, each of the trustees will be a trustee of a trust separate and apart from the trust administered by any other trustee.

Indenture Provisions Subordination

Upon any distribution of our assets upon our dissolution, winding up, liquidation or reorganization, the payment of the principal of (and premium, if any) and interest, if any, on any indenture securities denominated as subordinated debt securities is to be subordinated to the extent provided in the indenture in right of payment to the prior payment in full of all Senior Indebtedness (as defined below), but our obligation to you to make payment of the principal of (and premium, if any) and interest, if any, on such subordinated debt securities will not otherwise be affected. In addition, no payment on account of principal (or premium, if any), sinking fund or interest, if any, may be made on such subordinated debt securities at any time unless full payment of all amounts due in respect of the principal (and premium, if any), sinking fund and interest on Senior Indebtedness has been made or duly provided for in money or money's worth.

In the event that, notwithstanding the foregoing, any payment by us is received by the trustee in respect of subordinated debt securities or by the holders of any of such subordinated debt securities, upon our dissolution, winding up, liquidation or reorganization before all Senior Indebtedness is paid in full, the payment or distribution received by the trustee in respect of such subordinated debt securities or by the holders of any of such subordinated debt securities must be paid over to the holders of the Senior Indebtedness or on their behalf for application to the payment of all the Senior Indebtedness remaining unpaid until all the Senior Indebtedness has been paid in full, after giving effect to any concurrent payment or distribution to the holders of the Senior Indebtedness. Subject to the payment in full of all Senior Indebtedness upon this distribution by us, the holders of such subordinated debt securities will be subrogated to the rights of the holders of the Senior Indebtedness to the extent of payments made to the holders of the Senior Indebtedness out of the distributive share of such subordinated debt securities.

By reason of this subordination, in the event of a distribution of our assets upon our insolvency, certain of our senior creditors may recover more, ratably, than holders of any subordinated debt securities or the holders of any indenture securities that are not Senior Indebtedness. The indenture provides that these subordination provisions will not apply to money and securities held in trust under the defeasance provisions of the indenture.

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Senior Indebtedness is defined in the indenture as the principal of (and premium, if any) and unpaid interest on:

our indebtedness (including indebtedness of others guaranteed by us), whenever created, incurred, assumed or guaranteed, for money borrowed, that we have designated as Senior Indebtedness for purposes of the indenture and in accordance with the terms of the indenture (including any indenture securities designated as Senior Indebtedness), and renewals, extensions, modifications and refinancings of any of this indebtedness.

If this prospectus is being delivered in connection with the offering of a series of indenture securities denominated as subordinated debt securities, the accompanying prospectus supplement will set forth the approximate amount of our Senior Indebtedness and of our other Indebtedness outstanding as of a recent date.

Secured Indebtedness and Ranking

Certain of our indebtedness, including certain series of indenture securities, may be secured. The prospectus supplement for each series of indenture securities will describe the terms of any security interest for such series and will indicate the approximate amount of our secured indebtedness as of a recent date. Any unsecured indenture securities will effectively rank junior to any secured indebtedness, including any secured indenture securities, that we incur in the future to the extent of the value of the assets securing such future secured indebtedness. The debt securities, whether secured or unsecured, of the Company will rank structurally junior to all existing and future indebtedness (including trade payables) incurred by our subsidiaries, financing vehicles or similar facilities.

In the event of our bankruptcy, liquidation, reorganization or other winding up, any of our assets that secure secured debt will be available to pay obligations on unsecured debt securities only after all indebtedness under such secured debt has been repaid in full from such assets. We advise you that there may not be sufficient assets remaining to pay amounts due on any or all unsecured debt securities then outstanding after fulfillment of this obligation. As a result, the holders of unsecured indenture securities may recover less, ratably, than holders of any of our secured indebtedness.

The Trustee under the Indenture

U.S. Bank National Association serves as the trustee under the indenture.

Certain Considerations Relating to Foreign Currencies

Debt securities denominated or payable in foreign currencies may entail significant risks. These risks include the possibility of significant fluctuations in the foreign currency markets, the imposition or modification of foreign exchange controls and potential illiquidity in the secondary market. These risks will vary depending upon the currency or currencies involved and will be more fully described in the applicable prospectus supplement.

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DESCRIPTION OF OUR WARRANTS

The following is a general description of the terms of the warrants we may issue from time to time. Particular terms of any warrants we offer will be described in the prospectus supplement relating to such warrants.

We may issue warrants to purchase shares of our common stock, shares of our preferred stock or debt securities. Such warrants may be issued independently or together with shares of common or preferred stock or a specified principal amount of debt securities and may be attached or separate from such securities. We will issue each series of warrants under a separate warrant agreement to be entered into between us and a warrant agent. The warrant agent will act solely as our agent and will not assume any obligation or relationship of agency for or with holders or beneficial owners of warrants.

A prospectus supplement will describe the particular terms of any series of warrants we may issue, including the following:

- the title of such warrants;
- the aggregate number of such warrants;
- the price or prices at which such warrants will be issued;
- the currency or currencies, including composite currencies, in which the price of such warrants may be payable;
- if applicable, the designation and terms of the securities with which the warrants are issued and the number of warrants issued with each such security or each principal amount of such security;
- in the case of warrants to purchase debt securities, the principal amount of debt securities purchasable upon exercise of one warrant and the price at which and the currency or currencies, including composite currencies, in which this principal amount of debt securities may be purchased upon such exercise;
- in the case of warrants to purchase common stock or preferred stock, the number of shares of common stock or preferred stock, as the case may be, purchasable upon exercise of one warrant and the price at which and the currency or currencies, including composite currencies, in which these shares may be purchased upon such exercise;
- the date on which the right to exercise such warrants shall commence and the date on which such right will expire;
- whether such warrants will be issued in registered form or bearer form;
- if applicable, the minimum or maximum amount of such warrants which may be exercised at any one time;
- if applicable, the date on and after which such warrants and the related securities will be separately transferable;
- information with respect to book-entry procedures, if any;
- the terms of the securities issuable upon exercise of the warrants;
- if applicable, a discussion of certain U.S. federal income tax considerations; and

any other terms of such warrants, including terms, procedures and limitations relating to the exchange and exercise of such warrants.

We and the warrant agent may amend or supplement the warrant agreement for a series of warrants without the consent of the holders of the warrants issued thereunder to effect changes that are not inconsistent with the provisions of the warrants and that do not materially and adversely affect the interests of the holders of the warrants.

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Prior to exercising their warrants, holders of warrants will not have any of the rights of holders of the securities purchasable upon such exercise, including, in the case of warrants to purchase debt securities, the right to receive principal, premium, if any, or interest payments, on the debt securities purchasable upon exercise or to enforce covenants in the applicable indenture or, in the case of warrants to purchase common stock or preferred stock, the right to receive distributions, if any, or payments upon our liquidation, dissolution or winding up or to exercise any voting rights.

Under the 1940 Act, we may generally only offer warrants provided that (1) the warrants expire by their terms within ten years; (2) the exercise or conversion price is not less than the current market value at the date of issuance; (3) our stockholders authorize the proposal to issue such warrants, and our board of directors approves such issuance on the basis that the issuance is in our best interests and our stockholders; and (4) if the warrants are accompanied by other securities, the warrants are not separately transferable unless no class of such warrants and the securities accompanying them has been publicly distributed.

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REGULATION

We are a BDC under the 1940 Act that has elected to be treated as a RIC under the Code. The 1940 Act contains prohibitions and restrictions relating to transactions between business development companies and their affiliates (including any investment advisers), principal underwriters and affiliates of those affiliates or underwriters and requires that a majority of the directors be persons other than interested persons, as that term is defined in the 1940 Act. In addition, the 1940 Act provides that we may not change the nature of our business so as to cease to be, or to withdraw our election as, a BDC unless approved by a majority of our outstanding voting securities.

We may invest up to 100% of our assets in securities acquired directly from issuers in privately negotiated transactions. With respect to such securities, we may, for the purpose of public resale, be deemed an underwriter as that term is defined in the Securities Act. Our intention is to not write (sell) or buy put or call options to manage risks associated with the publicly traded securities of our portfolio companies, except that we may enter into hedging transactions to manage the risks associated with interest rate fluctuations. However, we may purchase or otherwise receive warrants to purchase the common stock of our portfolio companies in connection with acquisition financing or other investments. Similarly, in connection with an acquisition, we may acquire rights to require the issuers of acquired securities or their affiliates to repurchase them under certain circumstances. We also do not intend to acquire securities issued by any investment company that exceed the limits imposed by the 1940 Act. Under these limits, we generally cannot acquire more than 3% of the voting stock of any registered investment company, invest more than 5% of the value of our total assets in the securities of one investment company or invest more than 10% of the value of our total assets in the securities of more than one investment company. With regard to that portion of our portfolio invested in securities issued by investment companies, it should be noted that such investments might subject our stockholders to additional expenses. None of these policies is fundamental and may be changed without stockholder approval upon 60 days prior written notice to stockholders.

Qualifying Assets

Under the 1940 Act, a BDC may not acquire any asset other than assets of the type listed in section 55(a) of the 1940 Act, which are referred to as qualifying assets, unless, at the time the acquisition is made, qualifying assets represent at least 70% of the company's total assets. The principal categories of qualifying assets relevant to our proposed business are the following:

- Securities purchased in transactions not involving any public offering from the issuer of such securities, which issuer (subject to certain limited exceptions) is an eligible portfolio company, or from any person who is, or has been during the preceding 13 months, an affiliated person of an eligible portfolio company, or from any other person, subject to such rules as may be prescribed by the SEC. Under the 1940 Act and the rules thereunder,
- (1) eligible portfolio companies include (1) private domestic operating companies, (2) public domestic operating companies whose securities are not listed on a national securities exchange (e.g., the New York Stock Exchange) or registered under the Exchange Act, and (3) public domestic operating companies having a market capitalization of less than \$250 million. Public domestic operating companies whose securities are quoted on the over-the-counter bulletin board or through Pink Sheets LLC are not listed on a national securities exchange and therefore are eligible portfolio companies.
 - (2) Securities of any eligible portfolio company which we control.
 - (3) Securities purchased in a private transaction from a U.S. issuer that is not an investment company or from an affiliated person of the issuer, or in transactions incident to such a private transaction, if the issuer is in bankruptcy and subject to reorganization or if the issuer, immediately prior to the purchase of its securities, was unable to meet

its obligations as they came due without material assistance other than conventional lending or financing arrangements.

- (4) Securities of an eligible portfolio company purchased from any person in a private transaction if there is no ready market for such securities and we already own 60% of the outstanding equity of the eligible portfolio company.

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(5) Securities received in exchange for or distributed on or with respect to securities described above, or pursuant to the exercise of warrants or rights relating to such securities.

(6) Cash, cash equivalents, U.S. government securities or high-quality debt securities that mature in one year or less from the date of investment.

The regulations defining qualifying assets may change over time. We may adjust our investment focus as needed to comply with and/or take advantage of any regulatory, legislative, administrative or judicial actions in this area.

Managerial Assistance to Portfolio Companies

In order to count portfolio securities as qualifying assets for the purpose of the 70% test, a BDC must either control the issuer of the securities or must offer to make available to the issuer of the securities significant managerial assistance. However, when the BDC purchases securities in conjunction with one or more other persons acting together, one of the other persons in the group may make available such managerial assistance. Making available managerial assistance means any arrangement whereby the BDC, through its directors, officers, employees or agents, offers to provide, and, if accepted, does so provide, significant guidance and counsel concerning the management, operations or business objectives and policies of a portfolio company. Stellus Capital Management will provide such managerial assistance on our behalf to portfolio companies that request this assistance.

Temporary Investments

Pending investment in other types of qualifying assets, as described above, our investments may consist of cash, cash equivalents, U.S. government securities, repurchase agreements and high-quality debt investments that mature in one year or less from the date of investment, which we refer to, collectively, as temporary investments, so that 70% of our assets are qualifying assets or temporary investments. Typically, we will invest in U.S. Treasury bills or in repurchase agreements, so long as the agreements are fully collateralized by cash or securities issued by the U.S. government or its agencies. A repurchase agreement involves the purchase by an investor, such as us, of a specified security and the simultaneous agreement by the seller to repurchase it at an agreed-upon future date and at a price that is greater than the purchase price by an amount that reflects an agreed-upon interest rate. There is no percentage restriction on the proportion of our assets that may be invested in such repurchase agreements. However, if more than 25% of our total assets constitute repurchase agreements from a single counterparty, we would not meet the Diversification Tests in order to maintain our qualification as a RIC for U.S. federal income tax purposes. Accordingly, we do not intend to enter into repurchase agreements with a single counterparty in excess of this limit. Stellus Capital Management will monitor the creditworthiness of the counterparties with which we enter into repurchase agreement transactions.

Senior Securities

We are permitted, under specified conditions, to issue multiple classes of indebtedness and one class of stock senior to our common stock if our asset coverage, as defined in the 1940 Act, is at least equal to 200% immediately after each such issuance. We may also borrow amounts up to 5% of the value of our total assets for temporary or emergency purposes without regard to asset coverage. For a discussion of the risks associated with leverage, see Risk Factors – Risks Relating to our Business and Structure. 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.

Common Stock

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 at a price below the current net asset value of the common stock if our board of directors determines that such sale is in our best interests and that of our stockholders, and our stockholders approve such sale. In any such case, the price at which our securities are to be issued and sold may not be less than a price which, in the determination of our board of directors, closely approximates the market value of such securities (less any distributing commission or discount). We would need approval from

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our stockholders to issue shares below the then current net asset value per share. We may also make rights offerings to our stockholders at prices per share less than the net asset value per share, subject to applicable requirements of the 1940 Act. See Risk Factors Risks Relating to this Offering Stockholders may incur dilution if 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.

Codes of Ethics

We and Stellus Capital Management have each adopted a code of ethics pursuant to Rule 17j-1 under the 1940 Act that establishes procedures for personal investments and restricts certain personal securities transactions. Personnel subject to each such code may invest in securities for their personal investment accounts, including securities that may be purchased or held by us, so long as such investments are made in accordance with such code's requirements. You may read and copy our code of ethics at the SEC's Public Reference Room in Washington, D.C. You may obtain information on the operation of the Public Reference Room by calling the SEC at (202) 551-8090. In addition, each code of ethics is available on the EDGAR Database on the SEC's website at www.sec.gov. You may also obtain copies of each code of ethics, after paying a duplicating fee, by electronic request at the following e-mail address: publicinfo@sec.gov, or by writing the SEC's Public Reference Section, 100 F Street, N.E., Washington, D.C. 20549.

Proxy Voting Policies and Procedures

We have delegated our proxy voting responsibility to Stellus Capital Management. The Proxy Voting Policies and Procedures of Stellus Capital Management are set out below. The guidelines will be reviewed periodically by Stellus Capital Management and our directors who are not interested persons, and, accordingly, are subject to change.

Introduction

As an investment adviser registered under the Advisers Act, Stellus Capital Management has a fiduciary duty to act solely in our best interests. As part of this duty, Stellus Capital Management recognizes that it must vote our securities in a timely manner free of conflicts of interest and in our best interests.

Stellus Capital Management's policies and procedures for voting proxies for its investment advisory clients are intended to comply with Section 206 of, and Rule 206(4)-6 under, the Advisers Act.

Proxy Policies

Stellus Capital Management votes proxies relating to our portfolio securities in what it perceives to be the best interest of our stockholders. Stellus Capital Management reviews on a case-by-case basis each proposal submitted to a stockholder vote to determine its effect on the portfolio securities we hold. In most cases Stellus Capital Management will vote in favor of proposals that Stellus Capital Management believes are likely to increase the value of the portfolio securities we hold. Although Stellus Capital Management will generally vote against proposals that may have a negative effect on our portfolio securities, Stellus Capital Management may vote for such a proposal if there exist compelling long-term reasons to do so.

Stellus Capital Management has established a proxy voting committee and adopted proxy voting guidelines and related procedures. The proxy voting committee establishes proxy voting guidelines and procedures, oversees the internal proxy voting process, and reviews proxy voting issues. To ensure that Stellus Capital Management's vote is

not the product of a conflict of interest, Stellus Capital Management requires that (1) anyone involved in the decision-making process disclose to our Chief Compliance Officer any potential conflict that he or she is aware of and any contact that he or she has had with any interested party regarding a proxy vote; and (2) employees involved in the decision-making process or vote administration are prohibited from revealing how Stellus Capital Management intends to vote on a proposal in order to reduce any attempted influence from interested parties. Where conflicts of interest may be present, Stellus Capital Management will disclose such conflicts to us, including our independent directors and may request guidance from us on how to vote such proxies.

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Proxy Voting Records

You may obtain information about how Stellus Capital Management voted proxies by making a written request for proxy voting information to: Stellus Capital Investment Corporation, Attention: Investor Relations, 4400 Post Oak Parkway, Suite 2200, Houston, TX 77027, or by calling us collect at (310) 235-5900. The SEC also maintains a website at www.sec.gov that contains this information.

Privacy Principles

We are committed to maintaining the privacy of our stockholders and to safeguarding their nonpublic personal information. The following information is provided to help you understand what personal information we collect, how we protect that information and why, in certain cases, we may share information with select other parties.

Generally, we do not receive any nonpublic personal information relating to our stockholders, although certain nonpublic personal information of our stockholders may become available to us. We do not disclose any nonpublic personal information about our stockholders or former stockholders to anyone, except as permitted by law or as is necessary in order to service stockholder accounts (for example, to a transfer agent or third-party administrator).

We restrict access to nonpublic personal information about our stockholders to employees of Stellus Capital Management and its affiliates with a legitimate business need for the information. We intend to maintain physical, electronic and procedural safeguards designed to protect the nonpublic personal information of our stockholders.

Other

We are required to provide and maintain a bond issued by a reputable fidelity insurance company to protect us against larceny and embezzlement. Furthermore, as a BDC, we are prohibited from protecting any director or officer against any liability to us or our stockholders arising from willful misfeasance, bad faith, gross negligence or reckless disregard of the duties involved in the conduct of such person's office.

We and Stellus Capital Management are each required to adopt and implement written policies and procedures reasonably designed to prevent violation of relevant federal securities laws, review these policies and procedures annually for their adequacy and the effectiveness of their implementation, and designate a chief compliance officer to be responsible for administering the policies and procedures.

We may also be prohibited under the 1940 Act from knowingly participating in certain transactions with our affiliates without the prior approval of our board of directors who are not interested persons and, in some cases, prior approval by the SEC. The SEC has interpreted the BDC prohibition on transactions with affiliates to prohibit all joint transactions between entities that share a common investment adviser. The staff of the SEC has granted no-action relief permitting purchases of a single class of privately placed securities provided that the adviser negotiates no term other than price and certain other conditions are met. As a result, we only expect to co-invest on a concurrent basis with investment funds, accounts or investment vehicles managed by Stellus Capital Management when each of us and such investment fund, account or investment vehicle will own the same securities of the issuer and when no term is negotiated other than price. Any such investment would be made, subject to compliance with existing regulatory guidance, applicable regulations and our allocation procedures. If opportunities arise that would otherwise be appropriate for us and for an investment fund, account or investment vehicle managed by Stellus Capital Management to invest in different securities of the same issuer, Stellus Capital Management will need to decide which fund will

proceed with the investment. Moreover, except in certain circumstances, we will be unable to invest in any issuer in which an investment fund, account or investment vehicle managed by Stellus Capital Management has previously invested.

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Sarbanes-Oxley Act of 2002

The Sarbanes-Oxley Act of 2002 imposes a wide variety of regulatory requirements on publicly held companies and their insiders. Many of these requirements affect us. For example:

pursuant to Rule 13a-14 under the Exchange Act, our principal executive officer and principal financial officer must certify the accuracy of the financial statements contained in our periodic reports;

pursuant to Item 307 under Regulation S-K, our periodic reports must disclose our conclusions about the effectiveness of our disclosure controls and procedures;

pursuant to Rule 13a-15 under the Exchange Act, our management must prepare an annual report regarding its assessment of our internal control over financial reporting; and

pursuant to Item 308 of Regulation S-K and Rule 13a-15 under the Exchange Act, our periodic reports must disclose whether there were significant changes in our internal controls over financial reporting or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

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PLAN OF DISTRIBUTION

We may offer, from time to time, in one or more offerings or series, up to \$200,000,000 of our common stock, preferred stock, debt securities, subscription rights or warrants to purchase common stock, preferred stock or debt securities, in one or more underwritten public offerings, at-the-market offerings, negotiated transactions, block trades, best efforts offerings or a combination of these methods. We may sell the securities through underwriters or dealers, directly to one or more purchasers through agents or through a combination of any such methods of sale. Any underwriter or agent involved in the offer and sale of the securities will be named in the applicable prospectus supplement.

The distribution of our securities may be effected from time to time in one or more transactions at a fixed price or prices, which may be changed, at prevailing market prices at the time of sale, at prices related to such prevailing market prices, or at negotiated prices, provided, however, that the offering price per share of our securities less any underwriting commissions or discounts must equal or exceed the net asset value per share of our securities except that we may sell shares of our securities at a price below net asset value per share if holders of a majority of the number of shares of our stock have approved such a sale or if the following conditions are met: (i) holders of a majority of our stock and a majority of our stock not held by affiliated persons have approved issuance at less than net asset value per share during the one year period prior to such sale; (ii) a majority of our directors who have no financial interest in the sale and a majority of such directors who are not interested persons of us have determined that such sale would be in our best interest and in the best interests of our stockholders; and (iii) a majority of our directors who have no financial interest in the sale and a majority of such directors who are not interested persons of us, in consultation with the underwriter or underwriters of the offering if it is to be underwritten, have determined in good faith, and as of a time immediately prior to the first solicitation by or on behalf of us of firm commitments to purchase such securities or immediately prior to the issuance of such securities, that the price at which such securities are to be sold is not less than a price which closely approximates the market value of those securities, less any distributing commission or discount.

In connection with the sale of our securities, underwriters or agents may receive compensation from us or from purchasers of our securities, for whom they may act as agents, in the form of discounts, concessions or commissions. Underwriters may sell our securities to or through dealers and such dealers may receive compensation in the form of discounts, concessions or commissions from the underwriters and/or commissions from the purchasers for whom they may act as agents. Underwriters, dealers and agents that participate in the distribution of our securities may be deemed to be underwriters under the Securities Act, and any discounts and commissions they receive from us and any profit realized by them on the resale of our securities may be deemed to be underwriting discounts and commissions under the Securities Act. Any such underwriter or agent will be identified and any such compensation received from us will be described in the applicable prospectus supplement.

We may enter into derivative transactions with third parties, or sell securities not covered by this prospectus to third parties in privately negotiated transactions. If the applicable prospectus supplement indicates, in connection with those derivatives, the third parties may sell securities covered by this prospectus and the applicable prospectus supplement, including in short sale transactions. If so, the third party may use securities pledged by us or borrowed from us or others to settle those sales or to close out any related open borrowings of stock, and may use securities received from us in settlement of those derivatives to close out any related open borrowings of stock. The third parties in such sale transactions will be underwriters and, if not identified in this prospectus, will be identified in the applicable prospectus supplement (or a post-effective amendment).

Any of our common stock sold pursuant to a prospectus supplement will be listed on the New York Stock Exchange, or another exchange on which our common stock is traded.

Under agreements into which we may enter, underwriters, dealers and agents who participate in the distribution of our securities may be entitled to indemnification by us against certain liabilities, including liabilities under the Securities Act. Underwriters, dealers and agents may engage in transactions with, or perform services for, us in the ordinary course of business.

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If so indicated in the applicable prospectus supplement, we will authorize underwriters or other persons acting as our agents to solicit offers by certain institutions to purchase our securities from us pursuant to contracts providing for payment and delivery on a future date. Institutions with which such contracts may be made include commercial and savings banks, insurance companies, pension funds, investment companies, educational and charitable institutions and others, but in all cases such institutions must be approved by us. The obligations of any purchaser under any such contract will be subject to the condition that the purchase of our securities shall not at the time of delivery be prohibited under the laws of the jurisdiction to which such purchaser is subject. The underwriters and such other agents will not have any responsibility in respect of the validity or performance of such contracts. Such contracts will be subject only to those conditions set forth in the prospectus supplement, and the prospectus supplement will set forth the commission payable for solicitation of such contracts.

In order to comply with the securities laws of certain states, if applicable, our securities offered hereby will be sold in such jurisdictions only through registered or licensed brokers or dealers. In addition, in certain states, our securities may not be sold unless they have been registered or qualified for sale in the applicable state or an exemption from the registration or qualification requirement is available and is complied with.

The maximum commission or discount to be received by any member of the Financial Industry Regulatory Authority, Inc. will not be greater than 10.0% for the sale of any securities being registered.

We will pay customary costs and expenses of the registration of the shares of common stock pursuant to the registration rights agreement, including SEC filing fees and expenses of compliance with state securities or blue sky laws.

CUSTODIAN, TRANSFER AND DIVIDEND PAYING AGENT AND REGISTRAR

Our securities are held by State Street Bank and Trust Company pursuant to a custody agreement. State Street Bank and Trust Company will also serve as our transfer agent, distribution paying agent and registrar. The principal business address of State Street Bank and Trust Company is 225 Franklin Street, Boston, Massachusetts 02110.

BROKERAGE ALLOCATION AND OTHER PRACTICES

Since we will acquire and dispose of many of our investments in privately negotiated transactions, many of the transactions that we engage in will not require the use of brokers or the payment of brokerage commissions. Subject to policies established by our board of directors, Stellus Capital Management will be primarily responsible for selecting brokers and dealers to execute transactions with respect to the publicly traded securities portion of our portfolio transactions and the allocation of brokerage commissions. Stellus Capital Management does not expect to execute transactions through any particular broker or dealer but will seek to obtain the best net results for us under the circumstances, taking into account such factors as price (including the applicable brokerage commission or dealer spread), size of order, difficulty of execution and operational facilities of the firm and the firm's risk and skill in positioning blocks of securities. Stellus Capital Management generally will seek reasonably competitive trade execution costs but will not necessarily pay the lowest spread or commission available. Subject to applicable legal requirements and consistent with Section 28(e) of the Exchange Act, Stellus Capital Management may select a broker based upon brokerage or research services provided to Stellus Capital Management and us and any other clients. In return for such services, we may pay a higher commission than other brokers would charge if Stellus Capital

Management determines in good faith that such commission is reasonable in relation to the services provided.

LEGAL MATTERS

Certain legal matters regarding the securities offered by this prospectus will be passed upon for us by Eversheds Sutherland (US) LLP, Washington, DC 20001. Certain legal matters will be passed upon for the underwriters, if any, by the counsel named in the prospectus supplement, if any.

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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, independent registered public accountants, as stated in their reports appearing herein. Grant Thornton LLP's principal business address is 171 N. Clark Street, Chicago, Illinois, 60601.

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 our shares of common stock offered by this prospectus. The registration statement contains additional information about us and our shares of common stock being offered by this prospectus.

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 Public Reference Room at 100 F Street, NE, Washington, D.C. 20549-0102. You may obtain information on the operation of the Public Reference Room by calling the SEC at (202) 551-8090.

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 publicly filed information available, free of charge, on or through our website. Information contained on our website is not incorporated into this prospectus, and you should not consider information on our website to be part of this 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, or by writing the SEC's Public Reference Section, 100 F Street, N.E., Washington, D.C. 20549-0102.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
Stellus Capital Investment Corporation

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 schedules of investments as of December 31, 2016 and 2015, and 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, 2016 and the financial highlights (see Note 8) for each of the four years in the period ended December 31, 2016 and for the period from Inception (May 18, 2012) through December 31, 2012. These financial statements and financial highlights are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included verification by confirmation of securities as of December 31, 2016 and 2015, 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.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Stellus Capital Investment Corporation and subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2016 and the financial highlights for each of the four years in the period ended December 31, 2016 and for the period from Inception (May 18, 2012) through December 31, 2012 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the Company adopted new accounting guidance in 2016, related to the presentation of debt issuance costs.

/s/ GRANT THORNTON LLP

Houston, Texas
March 9, 2017

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

	December 31, 2016	December 31, 2015
ASSETS		
Non-controlled, non-affiliated investments, at fair value (amortized cost of \$362,217,251 and \$364,212,459, respectively)	\$365,625,891	\$349,017,697
Cash and cash equivalents	9,194,129	10,875,790
Receivable for sales and repayments of investments		10,000
Interest receivable	4,601,742	4,720,031
Deferred offering costs		261,761
Accounts receivable	748	7,684
Prepaid expenses	456,219	475,449
Total Assets	\$379,878,729	\$365,368,412
LIABILITIES		
Notes Payable	\$24,565,891	\$24,381,108
Credit facility payable	115,171,208	108,197,373
SBA Debentures	63,342,036	63,015,846
Dividends payable	1,413,982	1,413,982
Base management fees payable	1,608,295	1,518,779
Incentive fees payable	1,353,271	607,956
Interest payable	973,812	570,189
Unearned revenue	19,955	36,877
Administrative services payable	272,511	397,799
Deferred Tax Liability	8,593	381,723
Other accrued expenses and liabilities	267,390	195,676
Total Liabilities	\$208,996,944	\$200,717,308
Net Assets	\$170,881,785	\$164,651,104
NET ASSETS		
Common Stock, par value \$0.01 per share (100,000,000 shares authorized, 12,479,959 and 12,479,960 shares issued and outstanding, respectively)	\$12,480	\$12,480
Paid-in capital	180,994,723	180,994,752
Accumulated net realized (loss)	(13,089,671)	
Distributions in excess of net investment income	(435,794)	(779,643)
Net unrealized appreciation (depreciation) on investments and cash equivalents, net of deferred tax liability of \$8,593 and \$381,723 as of December 31, 2016 and December 31, 2015, respectively ⁽¹⁾	3,400,047	(15,576,485)
Net Assets	\$170,881,785	\$164,651,104
Total Liabilities and Net Assets	\$379,878,729	\$365,368,412

Net Asset Value Per Share

\$13.69

\$13.19

(1)

See Note 13 for a discussion of Deferred Taxes.

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
INVESTMENT INCOME			
Interest income	\$38,176,617	\$34,643,791	\$31,637,094
Other income	1,313,580	514,768	687,753
Total Investment Income	\$39,490,197	\$35,158,559	\$32,324,847
OPERATING EXPENSES			
Management fees	\$6,281,863	5,841,267	5,202,990
Valuation fees	397,330	356,971	384,957
Administrative services expenses	1,045,648	1,029,368	1,195,566
Incentive fees	4,275,436	3,975,198	3,122,890
Professional fees	712,524	596,357	744,547
Directors fees	324,000	333,000	373,000
Insurance expense	471,427	473,963	482,963
Interest expense and other fees	7,992,185	6,177,015	5,315,325
Deferred offering costs	261,761		
Other general and administrative expenses	415,822	474,625	389,738
Total Operating Expenses	\$22,177,996	\$19,257,764	\$17,211,976
Waiver of Incentive Fees		(646,333)	(1,399,226)
Total expenses, net of fee waiver	22,177,996	18,611,431	15,812,750
Net Investment Income	\$17,312,201	\$16,547,128	\$16,512,097
Net Realized Gain (loss) on Investments and Cash Equivalents	(13,089,671)	421,726	445,157
Net Change in Unrealized Appreciation (Depreciation) on Investments and Cash Equivalents	18,603,401	(9,204,717)	(6,489,990)
Benefit (provision) for taxes on net realized loss or net unrealized gain on investments at Taxable Subsidiaries	373,131	(93,601)	(288,122)
Net Increase in Net Assets Resulting from Operations	\$23,199,062	\$7,670,536	\$10,179,142
Net Investment Income Per Share	\$1.39	\$1.33	\$1.34
Net Increase in Net Assets Resulting from Operations Per Share	\$1.86	\$0.61	\$0.83
Weighted Average Shares of Common Stock Outstanding	12,479,959	12,479,961	12,281,178
Distributions Per Share	\$1.36	\$1.36	\$1.43

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Increase in Net Assets Resulting from Operations			
Net investment income	\$ 17,312,201	\$ 16,547,128	\$ 16,512,097
Net realized gain (loss) on investments and cash equivalents	(13,089,671)	421,726	445,157
Net change in unrealized appreciation (depreciation) on investments and cash equivalents	18,603,401	(9,204,717)	(6,489,990)
Benefit (provision) for taxes on net realized loss or unrealized depreciation (appreciation) on investments at Taxable Subsidiaries	373,131	(93,601)	(288,122)
Net Increase in Net Assets Resulting from Operations	\$ 23,199,062	\$ 7,670,536	\$ 10,179,142
Stockholder distributions from:			
Net investment income	(16,968,350)	(16,547,158)	(16,029,081)
Net realized capital gains		(421,726)	(1,472,549)
Total Distributions	\$(16,968,350)	\$(16,968,884)	\$(17,501,630)
Capital share transactions			
Issuance of common stock			5,087,335
Reinvestments of stockholder distributions			398,505
Sales load			(75,510)
Offering costs			(29,904)
Partial Share Redemption	(31)		
Net increase in net assets resulting from capital share transactions	\$(31)	\$	\$ 5,380,426
Total increase (decrease) in net assets	\$ 6,230,681	\$(9,298,348)	\$(1,942,062)
Net assets at beginning of year/period	\$ 164,651,104	\$ 173,949,452	\$ 175,891,514
Net assets at end of year/period (includes \$435,794 and \$779,643 and \$779,643 of distributions in excess of net investment income, respectively)	\$ 170,881,785	\$ 164,651,104	\$ 173,949,452

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STELLUS CAPITAL INVESTMENT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Cash flows from operating activities			
Net increase in net assets resulting from operations	\$23,199,062	\$7,670,536	\$10,179,142
Adjustments to reconcile net increase in net assets resulting from operations to net cash used in operating activities:			
Purchases of investments	(65,661,034)	(133,661,491)	(97,954,324)
Proceeds from sales and repayments of investments	55,949,177	93,289,529	54,870,360
Net change in unrealized appreciation (depreciation) on investments	(18,603,401)	9,204,717	6,490,090
Deferred tax provision (benefit)	(373,131)	93,601	288,122
Increase in investments due to PIK	(243,766)	(439,052)	(730,036)
Amortization of premium and accretion of discount, net	(1,128,511)	(1,034,240)	(686,985)
Amortization of loan structure fees	523,835	472,003	607,404
Amortization of deferred financing costs	326,190	210,064	90,614
Amortization of loan fees on SBIC debentures	184,783	204,980	37,117
Net realized loss (gain) on investments	13,089,341	(421,726)	(450,031)
Deferred offering costs	261,761		
Changes in other assets and liabilities			
Decrease (increase) in interest receivable	118,289	362,634	(368,753)
Decrease in receivable for affiliated transaction			43,450
(Increase) Decrease in accounts receivable	6,936	(6,988)	(696)
Decrease (increase) in prepaid expenses and fees	19,230	(56,166)	(7,962)
Increase in Management Fees payable	89,516	158,760	183,289
Decrease in directors fees payable			(96,000)
Increase (decrease) in incentive fees payable	745,315	(513,600)	64,614
Increase (decrease) in administrative services payable	(125,288)	(193,945)	328,519
Increase in interest payable	403,623	223,985	112,153
Increase (decrease) in unearned revenue	(16,921)	(120,526)	10,438
Increase (decrease) in other accrued expenses and liabilities	71,714	112,224	(179,426)
Net cash provided by (used in) operating activities	\$8,836,720	\$(24,444,701)	\$(27,168,901)

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TABLE OF CONTENTS**STELLUS CAPITAL INVESTMENT CORPORATION****CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)**

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Cash flows from financing activities			
Proceeds from notes issued			25,000,000
Proceeds from SBA Debentures		47,567,813	15,855,937
Financing costs paid on notes issued			(919,570)
Financing costs paid on Credit Facility	(50,000)		(795,628)
Financing costs paid on SBA Debentures		(325,000)	(325,000)
Proceeds from the issuance of common stock			5,116,985
Sales load for common stock issued			(75,510)
Offering costs paid for common stock issued			(116,150)
Stockholder distributions paid	(16,968,350)	(16,968,885)	(15,689,142)
Borrowings under credit facility	56,500,000	105,000,000	105,250,000
Repayments of credit facility	(50,000,000)	(102,000,000)	(108,750,000)
Repayments of short-term loan			(9,000,000)
Partial Share Redemption	(31)		
Net cash provided by (used in) financing activities	\$(10,518,381)	\$33,273,928	\$15,551,922
Net increase (decrease) in cash and cash equivalents	(1,681,661)	8,829,227	(11,616,979)
Cash and cash equivalents balance at beginning of year/period	10,875,790	2,046,563	13,663,542
Cash and cash equivalents balance at end of year/period	\$9,194,129	\$10,875,790	\$2,046,563
Supplemental and non-cash financing activities			
Non-cash purchase of investment through repayment of investment	\$	\$4,251,032	\$
Fees paid on SBA Debentures through proceeds	\$	\$1,182,187	\$394,063
Shares issued pursuant to Dividend Reinvestment Plan	\$	\$	\$398,505
Interest expense paid	\$6,548,754	\$5,010,984	\$4,465,618

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December 31, 2016**

Footnotes	Lien	Coupon	LIBOR floor	Cash	PIK	Maturity	Headquarters/ Industry	Principal Amount/ Shares	Amortized Cost	Fair Value
(2)							Deer Park, TX			
(2)(3)	Second Lien	L+10.50%	1.00%	11.50%		3/5/2020	Chemicals, Plastics, & Rubber	\$5,325,237	\$5,252,426	\$5,252,426
(4)	Equity							375,000 units	375,000	399,000
									5,627,426	5,627,426
							Amsterdam, OH			
(4)	Equity						Environmental Industries	517 shares	517	525,000
(4)	Equity							517 shares	517,439	524,000
									517,956	525,000
							Denver, CO			
(3)	Second Lien	L+8.50 %	1.25 %	9.75 %		4/3/2019	Beverage, Food, & Tobacco	\$8,000,000	7,928,373	8,000,000
							Hauppauge, NY			
(4)(14)	Unsecured						Services: Consumer	\$1,000,000	1,000,000	722,000
							Rochester, NY			
(3)	Second	L+9.50 %	1.00%	10.50%		6/5/2019	Telecommunications	\$7,500,000	7,422,928	7,422,928

Lien

(4) Equity

8,932 units 525,000 152
7,947,928 7,5

Murrysville, PA

(12) First Lien L+8.50 % 0.50% 9.03 % 12/31/2020 Automotive \$101,911 100,207 101

(2)(12) First Lien L+8.50 % 0.50% 9.03 % 12/31/2020 \$7,949,027 7,785,147 7,9

(4) Equity

149,828 shares 149,828 250
8,035,182 8,3

Camden, NJ

(13) First Lien L+6.50 % 1.00% 8.99 % 7/16/2020 Education \$12,500,000 12,404,725 12,

New York, NY

(5) Unsecured 12.00 % 12.00% 5/31/2018 Finance \$12,500,000 12,401,505 12,

(5) Unsecured 12.00 % 12.00% 5/31/2018 \$2,000,000 1,980,173 1,9

(5) Unsecured 12.00 % 12.00% 5/31/2018 \$5,000,000 4,960,146 4,9

(4)(5) Equity

38,893 units 557,143 671
19,898,967 20,

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2016**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2016**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2016**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2016**

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2016

- (1) See Note 1 of the Notes to Financial Statements for a discussion of the methodologies used to value securities in the portfolio.
- The Company's obligations to the lenders of the Credit Facility are secured by a first priority security interest in all non-controlled nonaffiliated investments and cash and cash equivalents, but exclude \$3,457,351 of cash and cash equivalents and \$100,252,693 of investments (at par) that are held by Stellus Capital SBIC LP. See Note 1 of the Notes to the Consolidated Financial Statements for discussion.
- (2) These loans have LIBOR or Euro Floors which are higher than the current applicable LIBOR or Euro rates; therefore, the floors are in effect.
- (3) (4) Security is non-income producing.
- The investment is not a qualifying asset under the Investment Company Act of 1940, as amended. The Company (5) 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 85% of the Company's total assets.
- (6) Represents a payment-in-kind 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) Investment has been on non-accrual since December 1, 2016.
- (8) Investment is in payment default.
- Excluded from the investment is an undrawn revolver commitment in an amount not to exceed \$875,000, with an (9) interest rate of LIBOR plus 9.00% and a maturity of October 22, 2019. This investment is accruing an unused commitment fee of 0.50% per annum.
- Excluded from the investment is an undrawn commitment in an amount not to exceed \$1,000,000, with an interest (10) 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) Variable rate loans bear interest at a rate that may be determined by reference to either LIBOR (which can include one-, two-, three- or six month LIBOR) or an alternate base rate (which can include the

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2016

Federal Funds Effective Rate or the Prime Rate), at the borrower's option, which rates reset periodically based on the terms of the loan agreement.

(12) These loans have LIBOR floors which 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) In the fourth quarter of 2016 Binder, emerged from Chapter 11 Bankruptcy in the U.S. Bankruptcy Court, Southern District of New York. The investment's cost has been adjusted to reflect the court-approved unsecured claim distribution proceeds that have been awarded to the Company. As of this time we do not expect to receive any additional repayment other than what the court has awarded.

Abbreviation Legend

PIK Payment-In-Kind

L LIBOR

Euro Euro Dollar

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments
December 31, 2015**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2015**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2015**

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Stellus Capital Investment Corporation

**Consolidated Schedule of Investments (continued)
December 31, 2015**

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Stellus Capital Investment Corporation

Consolidated Schedule of Investments (continued) December 31, 2015

- (1) See Note 1 of the Notes to Financial Statements for a discussion of the methodologies used to value securities in the portfolio.
- (2) The Company's obligations to the lenders of the Credit Facility are secured by a first priority security interest in all non-controlled nonaffiliated investments and cash, but exclude \$3,012,259 of cash and \$95,531,697 of investments (at par) that are held by Stellus Capital SBIC LP. See Note 1 of the Notes to the Consolidated Financial Statements for discussion.
- (3) These loans have LIBOR Floors which are higher than the current applicable LIBOR 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 83% of the Company's total assets.
- (6) Represents a payment-in-kind 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.

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- (7) Investment has been on non-accrual status since January 1, 2014. The coupon rate on this investment includes 2% default interest.
- (8) Digital Payment Technologies Corp. amended its name to T2 Systems Canada, Inc. and is the Canadian co-borrower of the term loan of T2 Systems, Inc.
- (9) Excluded from the investment is an undrawn revolver commitment in an amount not to exceed \$1,250,000, with an interest rate of LIBOR plus 9.00% (0.50% LIBOR floor) and a maturity of October 22, 2019. 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 \$1,600,000, with an interest rate of LIBOR plus 7.50% and a maturity of September 30, 2018. This investment is accruing an unused commitment fee of 0.50% per annum.
- (11) Variable rate loans bear interest at a rate that may be determined by reference to either LIBOR (which can include one-, two-, three- or six month LIBOR) or an alternate base rate (which can include the Federal Funds Effective Rate or the Prime Rate), at the borrower's option, which rates reset periodically based on the terms of the loan agreement.
- (12) Excluded from the investment is an undrawn commitment in an amount not to exceed \$407,405, an interest rate of LIBOR Plus 8.00% and a maturity of May 22, 2020.
- (13) This loan has a Prime floor of 2.00% which is lower than the current applicable Prime rate.
- (14) These loans have LIBOR floors which are lower than the applicable LIBOR rates; therefore, the floors are not in effect.
- (15) The coupon rate on this investment includes 2% default interest.
- (16) These loans are last-out term loans with contractual rates higher than the applicable LIBOR rates; therefore, the floors are not in effect.

Abbreviation Legend

PIK Payment-In-Kind

L LIBOR

Euro Euro Dollar

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

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 November 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 (BDC) 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).

On November 7, 2012, the Company priced its initial public offering (the Offering), at a price of \$15.00 per share. In connection with the Offering, the Company sold 9,200,000 shares (including 1,200,000 shares pursuant to the underwriters exercise of the overallotment option) for gross proceeds of \$138,000,000. Including the Offering, the Company has raised \$151,250,000 including (i) \$500,010 of seed capital contributed by Stellus Capital and (ii) \$12,749,990 in a private placement to certain purchasers, including persons and entities associated with Stellus Capital. In addition, in connection with the acquisition of the Company s initial portfolio the Company issued \$29,159,145 in shares of the Company s common stock. The Company s shares are currently listed on the New York Stock Exchange under the symbol SCM .

The Company has established wholly owned subsidiaries: SCIC Consolidated Blocker 1, Inc., SCIC CC Blocker 1, Inc., SCIC ERC Blocker 1, Inc., SCIC SKP Blocker 1, Inc. and SCIC APE Blocker 1, Inc., SCIC HUF 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.

See footnote (2) of the Consolidated Schedule of Investments. SBA regulations currently limit the amount that an SBIC may borrow to a maximum of \$150 million when it has at least \$75 million 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, 2016, the SBIC subsidiary had \$32.5 million of regulatory capital, as such term

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STELLUS CAPITAL INVESTMENT CORPORATION

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

is defined by the SBA, and has received commitments from the SBA of \$65 million. As of both December 31, 2016 and December 31, 2015, the SBIC subsidiary had \$65.0 million of SBA-guaranteed debentures outstanding.

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, second lien, unitranche and mezzanine 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 accounting principles generally accepted in the United States of America (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, the Company does not consolidate portfolio company investments.

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

Portfolio Investment Classification

The Company classifies its portfolio investments with the requirements of the 1940 Act, (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, 2016, cash balances totaling \$3,589,409 exceeded FDIC insurance protection levels of \$250,000 by \$3,339,409, subjecting the Company to risk related to the uninsured balance. In addition, at December 31, 2016, the Company held \$5,604,720 in cash equivalents that were insured by the FDIC. 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 11). On December 31, 2016 and December 31, 2015, we held no U.S. Treasury Bills.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

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 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 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.

Deferred Offering Costs

Deferred offering costs consist of fees and expenses incurred in connection with the offer and sale of the Company's common stock and bonds, 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 becomes effective. During the quarter ended June 30, 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 in the second quarter of this year.

Investments

As a BDC, the Company will generally invest in illiquid loans and securities including debt and equity securities of middle-market companies. Under procedures established by the 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. 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 90 days of maturity will be valued at cost plus accreted discount, or minus amortized premium, which approximates value. With respect to unquoted securities, our board of directors, together with our independent valuation advisors, 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 will use the pricing indicated by the external event to corroborate and/or assist us in our valuation. Because the Company expects that there will not be a readily available market for many of the investments in our portfolio, the Company expects to value most of our 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.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

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

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. For loans and debt securities with contractual payment-in-kind (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 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.

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.

Payment-in-Kind Interest

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.

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.

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STELLUS CAPITAL INVESTMENT CORPORATION

**NOTES TO THE CONSOLIDATED FINANCIAL
STATEMENTS**

December 31, 2016

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

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 Internal Revenue Code of 1986, as amended, and to operate in a manner so as to qualify for the tax treatment applicable to RICs. In order to qualify 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 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 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 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. The Company incurred an excise tax expense for the year ended December 31, 2016 of \$22,663 and \$0 for the years ended December 31, 2015 and 2014.

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 in the applicable period.

As of December 31, 2016 and December 31, 2015, 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 general and administrative expenses. Any such expenses for the year ended December 31, 2016 were de minimis.

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 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.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

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

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.

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, 2016, 2015 and 2014, the Company recorded deferred income tax benefit (expense) of \$373,131, \$(93,601) and \$(288,122), respectively, related to the Taxable Subsidiaries. In addition, as of December 31, 2016 and December 31, 2015, the Company had a deferred tax liability of \$8,593 and \$381,723, respectively. See Note 13, Income Taxes, for a schedule of the deferred tax asset, 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 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. While the Company is currently assessing the impact of the guidance we do not expect the impact of this new standard on our consolidated financial statements to be material.

In August 2014, the FASB issued ASU No. 2014-15 Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. In connection with the preparation of interim and annual reports, the Company's management will evaluate whether conditions or events exist that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the date the financial statements are available to be issued, when applicable), and, if so, disclose that fact. Additionally, the Company's management must evaluate and disclose whether its plans will alleviate that doubt. The guidance was effective for the Company beginning January 1, 2016. The Company has adopted the guidance as of January 1, 2016 and there is no impact on its consolidated financial statement.

On April 8, 2015 the FASB issued ASU No. 2015-03 Simplifying the Presentation of Debt Issuance Costs was effective for the quarter ended March 31, 2016. The new guidance requires that debt issuance costs related to a recognized debt liability be presented as a deduction from the debt liability rather than as an asset. Accordingly, the Company has adopted the guidance as of January 1, 2016. Certain reclassifications have been

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STELLUS CAPITAL INVESTMENT CORPORATION

**NOTES TO THE CONSOLIDATED FINANCIAL
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December 31, 2016

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

made to prior period line items on the Company's Consolidated Statement of Assets and Liabilities as the new guidance requires retrospective application.

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 update is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, and early adoption is permitted. Entities are permitted to apply the amendments either prospectively or retrospectively. The Company believes that this guidance will not have an impact on its consolidated financial statements. 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 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. While the Company is currently assessing the impact of the guidance we do not expect the impact of this new standard on our consolidated financial statements to be material.

Additionally, in May 2016, the FASB issued ASU No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients, which includes amendments for enhanced clarification of the guidance. Earlier adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. While the Company is currently assessing the impact of the guidance we do not expect the impact of this new standard on our 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 this agreement, the Company has agreed to pay to Stellus Capital a base annual 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 annual incentive fee.

For the years ended December 31, 2016, 2015 and 2014, the Company recorded an expense for base management fees of \$6,281,863, \$5,841,267, and \$5,202,990, respectively. As of December 31, 2016 and December 31, 2015, respectively, \$1,608,295 and \$1,518,779 were payable to Stellus Capital.

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

Investment Income Incentive Fee

The investment income component (Investment Income Incentive Fee) is calculated, and payable, 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

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STELLUS CAPITAL INVESTMENT CORPORATION

**NOTES TO THE CONSOLIDATED FINANCIAL
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December 31, 2016

NOTE 2 RELATED PARTY ARRANGEMENTS (continued)

the Company's net assets attributable to the Company's common stock, for the immediately preceding calendar quarter, will have a 2.0% (which is 8.0% annualized) 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 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% (which is 10.0% annualized) 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% (10.0% annualized) 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 Investment 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, 2016, 2015 and 2014, the Company incurred \$4,275,436, \$3,975,198 and \$3,428,357, respectively, of Investment Income Incentive Fees. As of December 31, 2016 and 2015, \$1,353,271 and \$607,956, respectively, of such incentive fees were payable to the Advisor, of which \$1,162,714 and \$401,573, respectively, were currently payable (as explained below). As of December 31, 2016 and December 31, 2015, \$190,557 and \$206,383, 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 in cash.

While under no obligation to do so, the Advisor waived incentive fees of \$646,333 and \$1,399,226 for the years ended December 31, 2015 and December 31, 2014 to the extent required to support an annualized dividend yield of 9.0% based on the price per share of our common stock in connection with 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 year ended December 31, 2016.

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

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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.

GAAP requires that the incentive fee accrual considers the cumulative aggregate realized gains and losses and unrealized capital appreciation or depreciation of investments or other financial instruments in the calculation, as an incentive fee would be payable if such realized gains and losses and unrealized capital appreciation or depreciation were realized, even though such realized gains and losses and unrealized capital appreciation or depreciation is not permitted to be considered in calculating the fee actually payable under the investment management agreement (the Capital Gains Incentive Fee). There can be no assurance that unrealized appreciation or depreciation will be realized in the future. Accordingly, such fee, as calculated and accrued, would not necessarily be payable under the investment management agreement, and may never be paid based upon the computation of incentive fees in subsequent periods. For the years ended December 31, 2016 and 2015, the Company incurred no Capital Gains Incentive Fee. For the year ended December 31, 2014, the Company incurred \$(305,467) of incentive fees related to the Capital Gains Incentive Fee. As of December 31, 2016 and December 31, 2015, no Capital Gains Incentive Fees were payable to the Advisor, subject to the limitations set forth below.

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

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Investment Income Incentive Fee Incurred	\$ 4,275,436	\$ 3,975,198	\$ 3,428,357
Capital Gains Incentive Fee Incurred			\$ (305,467)
Incentive Fee Expense	\$ 4,275,436	\$ 3,975,198	\$ 3,122,890
Investment Income Incentive Fee Waived		(646,333)	(1,399,226)
Net Incentive Fee Expense	\$ 4,275,436	\$ 3,328,865	\$ 1,723,664
		December 31, 2016	December 31, 2015
Investment Income Incentive Fee Currently Payable		\$ 1,162,714	\$ 401,573
Investment Income Incentive Fee Deferred		190,557	206,383

Incentive Fee Payable

\$ 1,353,271 \$ 607,956

Director Fees

For the years ended December 31, 2016, 2015 and 2014, the Company recorded an expense relating to director fees of \$324,000, \$333,000, and \$373,000, respectively. As of December 31, 2016 and 2015, the Company owed its independent directors no unpaid director fees.

Co-Investments

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 (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

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

NOTE 2 RELATED PARTY ARRANGEMENTS (continued)

strategies. We intend to co-invest, subject to the conditions included in the exemptive order we received from the SEC, with a private credit fund managed by Stellus Capital Management that has 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.

License Agreement

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. Under this agreement, we have a right to use the Stellus Capital name for so long as Stellus Capital Management or one of its affiliates remains our investment adviser. Other than with respect to this limited license, we have no legal right to the Stellus Capital name. This license agreement will remain in effect for so long as the investment advisory agreement with Stellus Capital Management is in effect.

Administration Agreement

The Company entered into an administration agreement with Stellus Capital Management pursuant to which Stellus Capital Management 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 Management 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 year ended December 31, 2016, 2015 and 2014, the Company recorded expenses of \$922,531, \$744,657, and \$647,429, respectively, related to the administration agreement. As of December 31, 2016 and December 31, 2015, \$232,169 and \$195,221, respectively, remained payable to Stellus Capital relating to the administration agreement.

Indemnifications

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 Management 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 Management's services under the investment advisory agreement or otherwise as our investment adviser.

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Distributions are generally declared by the Company's board of directors each calendar quarter 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 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 dividends declared and paid or to be paid on its common stock:

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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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
Total			\$ 5.6850

Unless the stockholder elects to receive its distributions in cash, the Company intends to make such distributions in additional shares of the Company common stock under the Company's dividend reinvestment plan. 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 dividend reinvestment plan 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 dividend reinvestment plan will increase the Company's gross assets on which the base management fee and the incentive fee are determined and paid to Stellus Capital. No new shares were issued in connection with the distributions made during the years ended December 31, 2016 and 2015. During the year ended December 31, 2014, the Company issued 29,573 shares of common stock in connection with the stockholder distribution reinvestment plan.

NOTE 4 EQUITY OFFERINGS AND RELATED EXPENSES

On June 5, 2014, we established an at-the-market program through which we may sell, from time to time and at our sole discretion \$50 million of our common stock. There were no shares issued during the years ended December 31, 2016 and 2015 under the at-the-market program. The proceeds raised, the related underwriting fees, the offering expenses and the price at which these shares were issued from the period of June 5, 2014 through December 31, 2014 are as follows:

Issuance of Common Stock	Number of Shares	Gross Proceeds	Sales Load	Offering Expenses	Offering Price
Quarter ended June 30, 2014	230,242	\$ 3,334,474	\$ 50,017	\$ 17,467	\$ 14.48
Quarter ended September 30, 2014	121,123	1,752,861	25,943	12,437	\$ 14.47
Quarter ended December 31, 2014					
Total	351,365	\$ 5,087,335	\$ 75,960	\$ 29,904	

The Company issued no shares of common stock during the years ended December 31, 2016 and 2015 in connection with the stockholder distribution reinvestment plan.

The Company issued 29,573 shares of common stock during the year ended December 31, 2014 in connection with the stockholder distribution reinvestment plan.

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STATEMENTS****December 31, 2016****NOTE 4 EQUITY OFFERINGS AND RELATED EXPENSES
(continued)**

Issuance of Common Stock	Number of Shares	Gross Proceeds	Offering Price
January 24, 2014	2,603	\$ 36,619	\$ 14.07
February 14, 2014	4,646	64,121	13.80
March 14, 2014	3,257	45,233	13.89
June 16, 2014	3,055	41,519	13.59
July 15, 2014	3,029	41,895	13.83
August 15, 2014	3,090	41,690	13.49
September 30, 2014	3,226	42,036	13.04
October 15, 2014	3,536	42,405	11.99
November 14, 2014	3,131	42,987	13.72
Total	29,573	\$ 398,505	

**NOTE 5 NET INCREASE (DECREASE) IN NET ASSETS PER
COMMON SHARE**

The following information sets forth the computation of net increase (decrease) in net assets resulting from operations per common share for the years ended December 31, 2016, 2015 and 2014.

	For the year ended December 31, 2016	For the year ended December 31, 2015	For the year ended December 31, 2014
Net increase in net assets resulting from operations	\$ 23,199,062	\$ 7,670,536	\$ 10,179,142
Average common shares	12,479,959	12,479,961	12,281,178
Basic and diluted earnings per common share	\$ 1.86	\$ 0.61	\$ 0.83

NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE

In accordance with the authoritative guidance on fair value measurements and disclosures under 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

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

**NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE
(continued)**

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.

At December 31, 2016, the Company had investments in 45 portfolio companies. The total cost and fair value of the investments were \$362,217,251 and \$365,625,891 respectively. The composition of our investments as of December 31, 2016 is as follows:

	Cost	Fair Value
Senior Secured First Lien	\$ 113,264,200	\$ 113,482,205
Senior Secured Second Lien	163,112,172	162,486,388
Unsecured Debt	70,919,986	70,725,412
Equity	14,920,893	18,931,886
Total Investments	\$ 362,217,251	\$ 365,625,891

At December 31, 2015, the Company had investments in 39 portfolio companies. The total cost and fair value of the investments were \$364,212,459 and \$349,017,697, respectively. The composition of our investments as of December 31, 2015 is as follows:

	Cost	Fair Value
Senior Secured First Lien	\$ 133,344,891	\$ 131,908,961
Senior Secured Second Lien	136,853,644	131,972,581
Unsecured Debt	81,492,139	72,212,282
Equity	12,521,785	12,923,873
Total Investments	\$ 364,212,459	\$ 349,017,697

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, 2016 and December 31, 2015, the Company had two and three such investments with aggregate unfunded commitments of \$1,875,000 and \$3,257,405, respectively. The Company maintains sufficient liquidity to fund such unfunded loan commitments should the need arise.

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, 2016 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	\$	\$	\$ 113,482,205	\$ 113,482,205
Senior Secured Second Lien		17,965,000	144,521,388	162,486,388
Unsecured Debt			70,725,412	70,725,412
Equity			18,931,886	18,931,886
Total Investments	\$	\$ 17,965,000	\$ 347,660,891	\$ 365,625,891

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(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, 2015 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	\$	\$	\$ 131,908,961	\$ 131,908,961
Senior Secured Second Lien			131,972,581	131,972,581
Unsecured Debt			72,212,282	72,212,282
Equity			12,923,873	12,923,873
Total Investments	\$	\$	\$ 349,017,697	\$ 349,017,697

The aggregate values of Level 3 portfolio investments changed during the year ended December 31, 2016 are as follows:

	Senior Secured Loans-First Lien	Senior Secured Loans-Second Lien	Unsecured Debt	Equity	Total
Fair value at beginning of period	\$ 131,908,961	\$ 131,972,581	\$ 72,212,282	\$ 12,923,873	\$ 349,017,697
Purchases of investments	25,009,310	35,664,883	1,354,073	3,632,768	65,661,034
Payment-in-kind interest	112,952	22,874	107,940		243,766
Sales and Redemptions	(44,947,647)	(9,850,061)	(122,094)	(1,019,375)	(55,939,177)
Net Realized Losses	(674,702)		(12,200,353)	(214,286)	(13,089,341)
Change in unrealized depreciation included in earnings	1,653,933	2,684,245	9,085,283	3,608,906	17,032,367
Amortization of premium and accretion of discount, net	419,398	392,196	288,281		1,099,875
Transfer to Level 2		(16,365,330)			(16,365,330)
Fair value at end of period	\$ 113,482,205	\$ 144,521,388	\$ 70,725,412	\$ 18,931,886	\$ 347,660,891

Change in unrealized depreciation

on Level 3 investments still held as of December 31, 2016	\$1,399,408	\$2,588,122	\$9,084,789	\$3,686,972	\$16,759,291
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During the year ended December 31, 2016, there were two transfers from Level 3 to Level 2 as additional broker quotes became available. During the year ended December 31, 2015, there was one transfer from Level 2 to Level 3 as additional valuation methods were considered when determining the fair value of this investment.

Transfers are reflected at the value of the securities at the beginning of the period.

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(continued)**

The aggregate values of Level 3 portfolio investments changed during the year ended December 31, 2015 are as follows:

	Senior Secured Loans-First Lien	Senior Secured Loans-Second Lien	Unsecured Debt	Equity	Total
Fair value at beginning of period	\$75,529,963	\$93,184,398	\$129,276,255	\$9,602,318	\$307,592,934
Purchases of investments	69,339,674	58,891,000	5,028,391	4,653,457	137,912,522
Payment-in-kind interest	119,516		319,536		439,052
Sales and Redemptions	(12,893,129)	(24,713,777)	(59,935,102)	(8,552)	(97,550,560)
Realized Gains	137,793		283,933		421,726
Change in unrealized depreciation included in earnings	(776,936)	(4,084,525)	(3,019,906)	(1,323,350)	(9,204,717)
Amortization of premium and accretion of discount, net	452,080	322,985	259,175		1,034,240
Transfer from Level 2		8,372,500			8,372,500
Fair value at end of period	\$131,908,961	\$131,972,581	\$72,212,282	\$12,923,873	\$349,017,697
Change in unrealized depreciation on Level 3 investments still held as of December 31, 2015	\$(771,909)	\$(4,432,180)	\$(3,415,546)	\$(1,323,350)	\$(9,942,985)

The following is a summary of geographical concentration of our investment portfolio as of December 31, 2016:

	Cost	Fair Value	% of Total Investments	
Texas	\$ 74,433,626	\$ 73,576,277	20.13	%
New York	36,651,725	36,479,999	9.98	%
Colorado	27,855,053	28,979,651	7.93	%
California	28,298,845	28,606,727	7.82	%
Massachusetts	22,467,254	22,944,663	6.28	%
Georgia	20,626,735	22,469,217	6.15	%
New Jersey	20,710,728	20,804,704	5.69	%
Illinois	17,554,821	17,590,281	4.81	%

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Alabama	16,191,841	16,584,379	4.54	%
Missouri	14,096,725	14,441,599	3.95	%
Tennessee	12,310,883	12,045,701	3.29	%
Arkansas	9,912,815	10,102,283	2.76	%
Pennsylvania	8,035,182	8,301,104	2.27	%
Puerto Rico	8,712,537	8,229,054	2.25	%
Florida	7,453,847	7,431,820	2.03	%
Canada	6,765,448	6,692,648	1.83	%
Minnesota	6,362,834	6,374,800	1.74	%
New York	5,450,667	5,450,667	1.49	%
North Carolina	4,920,321	5,000,000	1.37	%
Washington	4,158,696	4,211,990	1.15	%
Virginia	4,029,530	4,060,519	1.11	%
Arizona	3,408,099	3,410,583	0.93	%
Utah	1,291,083	1,311,789	0.36	%
Ohio	517,956	525,436	0.14	%
	\$ 362,217,251	\$ 365,625,891	100.00	%

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(continued)**

The following is a summary of geographical concentration of our investment portfolio as of December 31, 2015:

	Cost	Fair Value	% of Total Investments	
New York	\$ 53,089,906	\$ 44,028,592	12.62	%
Texas	44,455,960	42,224,563	12.10	%
Colorado	27,775,081	28,719,072	8.23	%
California	28,079,435	27,836,262	7.97	%
Georgia	26,100,285	25,845,891	7.41	%
Massachusetts	22,407,217	21,363,609	6.12	%
New Jersey	21,285,356	20,943,875	6.00	%
Alabama	18,330,990	18,153,182	5.20	%
Illinois	17,514,510	17,452,318	5.00	%
Missouri	14,067,329	13,369,069	3.83	%
Tennessee	12,286,222	12,051,362	3.45	%
Ohio	10,593,407	10,593,407	3.04	%
Pennsylvania	9,827,328	9,827,328	2.82	%
Puerto Rico	8,702,074	8,602,868	2.46	%
Canada	9,411,185	8,300,280	2.38	%
Florida	7,592,824	7,390,241	2.12	%
Minnesota	6,881,287	6,839,308	1.96	%
North Carolina	4,909,192	4,760,844	1.36	%
Indiana	4,739,046	4,715,703	1.35	%
Kentucky	4,473,006	4,518,888	1.29	%
Washington	4,146,167	4,083,966	1.17	%
Virginia	4,016,918	3,962,905	1.14	%
Arizona	3,527,734	3,434,164	0.98	%
	\$ 364,212,459	\$ 349,017,697	100.00	%

The following is a summary of industry concentration of our investment portfolio as of December 31, 2016:

Cost	Fair Value	% of Total Investments
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Finance	\$ 56,663,586	\$ 57,504,930	15.73	%
Software	36,199,915	36,730,618	10.05	%
Media: Broadcasting & Subscription	36,001,876	36,637,803	10.02	%
Healthcare & Pharmaceuticals	35,002,051	35,583,505	9.73	%
Services: Business	24,105,217	25,884,879	7.08	%
Chemicals, Plastics, & Rubber	20,763,612	21,165,542	5.79	%
Consumer Goods: Durable	18,957,486	19,146,954	5.24	%
Retail	18,973,041	19,095,787	5.22	%
Education	17,325,046	17,498,701	4.79	%
Telecommunications	16,403,791	16,009,390	4.38	%
High Tech Industries	16,486,738	15,382,000	4.21	%
Consumer goods: non-durable	12,437,795	12,700,000	3.47%	

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TABLE OF CONTENTS**STELLUS CAPITAL INVESTMENT CORPORATION****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****December 31, 2016****NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE
(continued)**

	Cost	Fair Value	% of Total Investments	
Beverage, Food, & Tobacco	11,881,630	11,991,250	3.28	%
Automotive	8,035,182	8,301,104	2.27	%
Services: Consumer	8,453,847	8,153,879	2.23	%
Transportation: Cargo	6,765,448	6,692,648	1.83	%
Energy: Oil & Gas	7,320,058	6,654,662	1.82	%
Services: Government	4,029,530	4,060,519	1.11	%
Hotel, Gaming, & Leisure	3,408,099	3,410,583	0.93	%
Construction & Building	2,485,347	2,495,701	0.68	%
Environmental Industries	517,956	525,436	0.14	%
	\$ 362,217,251	\$ 365,625,891	100.00	%

The following is a summary of industry concentration of our investment portfolio as of December 31, 2015:

	Cost	Fair Value	% of Total Investments	
Finance	\$ 56,453,642	\$ 56,020,910	16.05	%
Services: Business	37,386,875	36,831,622	10.56	%
Healthcare & Pharmaceuticals	35,457,015	36,161,248	10.36	%
Retail	31,669,891	31,390,951	8.99	%
Media: Broadcasting & Subscription	30,987,416	30,220,742	8.66	%
Software	26,553,384	25,447,575	7.29	%
Services: Consumer	25,265,858	16,531,754	4.74	%
Telecommunications	16,369,463	14,347,366	4.11	%
Chemicals, Plastics, & Rubber	13,912,209	13,695,631	3.92	%
Consumer goods: non-durable	12,430,852	12,430,852	3.56	%
Education	12,383,339	12,081,063	3.46	%
Environmental Industries	10,593,407	10,593,407	3.04	%
Automotive	9,827,328	9,827,328	2.82	%
Beverage, Food, & Tobacco	7,901,427	8,000,000	2.29	%
Transportation & Logistics	7,403,404	7,355,239	2.11	%
High Tech Industries	6,644,181	6,581,989	1.89	%

Transportation: Cargo	6,746,827	5,660,744	1.62	%
Metals & Mining	4,473,006	4,518,888	1.29	%
Services: Government	4,016,918	3,962,905	1.14	%
Hotel, Gaming, & Leisure	3,527,734	3,434,164	0.98	%
Construction & Building	2,481,388	2,455,931	0.70	%
Energy: Oil & Gas	1,726,895	1,467,388	0.42	%
	\$ 364,212,459	\$ 349,017,697	100.00	%

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TABLE OF CONTENTS**STELLUS CAPITAL INVESTMENT CORPORATION****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****December 31, 2016****NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE
(continued)**

The following provides quantitative information about Level 3 fair value measurements as of December 31, 2016:

Description:	Fair Value	Valuation Technique	Unobservable Inputs	Range (Average) ⁽¹⁾
First lien debt	\$ 113,482,205	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	-2.01% to 0.69% (-0.66%) -0.21% to 0.83% (0.16%) 7x to 14x (10x) ⁽⁴⁾ -7.34% to 6.67%
Second lien debt	\$ 144,521,388	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	(0.00%) -0.60% to 0.79% (0.00%) 5x to 19x (11x) ⁽⁴⁾ -0.91% to 0.03% (-0.36%)
Unsecured debt	\$ 70,725,412	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	-0.36% to 0.95% (0.10%) 7x to 13x (10x) ⁽⁴⁾
Equity investments	\$ 18,931,886	Market approach ⁽⁵⁾	Underwriting multiple/ EBITDA Multiple	1x to 13x (9x)
Total Long Term Level 3 Investments	\$ 347,660,891			

(1) Weighted average based on fair value as of December 31, 2016.

(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. 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 -2.01% (201 basis points) to 0.69% (69 basis points). The average of all changes was -0.66%.

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

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 (5) 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.

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TABLE OF CONTENTS**STELLUS CAPITAL INVESTMENT CORPORATION****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****December 31, 2016****NOTE 6 PORTFOLIO INVESTMENTS AND FAIR VALUE
(continued)**

The following provides quantitative information about Level 3 fair value measurements as of December 31, 2015:

Description:	Fair Value	Valuation Technique	Unobservable Inputs	Range (Average) ⁽¹⁾⁽³⁾
First lien debt	\$ 131,908,961	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	0.00% to 2.83% (0.97%) -0.37% to 0.89% (-0.12%) 5x to 28x (11x) ⁽⁴⁾
Second lien debt	\$ 131,972,581	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	-4.48% to 5.01% (0.82%) -0.71% to 0.17% (-0.22%) 7x to 14x (10x) ⁽⁴⁾
Unsecured debt	\$ 72,212,282	Income/Market ⁽²⁾ approach	HY credit spreads, Risk free rates Market multiples	-3.86% to 0.74% (-0.25%) -0.46% to 0.36% (-0.10%) 9x to 12x (10x) ⁽⁴⁾
Equity investments	\$ 12,923,873	Market approach ⁽⁵⁾	Underwriting multiple/EBITDA Multiple	1x to 13x (7x)
Total Long Term Level 3 Investments	\$ 349,017,697			

(1) Weighted average based on fair value as of December 31, 2015.

(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 second 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 0.00% (0 basis points) to 2.83% (283 basis points). The average of all changes was 0.97%.

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

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 (5) 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.

TABLE OF CONTENTS**STELLUS CAPITAL INVESTMENT CORPORATION****NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****December 31, 2016****NOTE 7 COMMITMENTS AND CONTINGENCIES (continued)**

As of December 31, 2016, the Company had \$1,875,000 of unfunded commitments to provide debt financing to two of our portfolio companies. As of December 31, 2015 the Company had \$3,257,405 of unfunded commitments to provide debt financing to three of our portfolio companies.

NOTE 8 FINANCIAL HIGHLIGHTS

	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	For the period from Inception (May 18, 2012) through December 31, 2012
Per Share Data:⁽¹⁾					
Net asset value at beginning of year/period	\$13.19	\$13.94	\$14.54	\$14.45	\$15.00
Net investment income	1.39	1.33	1.34	1.33	0.11
Change in unrealized appreciation (depreciation)	1.49	(0.74)	(0.53)	0.03	(0.01)
Realized gain (loss)	(1.05)	0.03	0.04	0.09	
Benefit (Provision) for taxes on unrealized appreciation	0.03	(0.01)	(0.02)		
Total from investment operations	1.86	0.61	0.83	1.45	0.10
Issuance of common shares					0.01
Reinvestments of stockholder distributions ⁽²⁾					(0.41)
Sales Load			(0.01)		(0.07)
Stockholder distributions from:					
Net investment income	(1.36)	(1.33)	(1.31)	(1.36)	(0.18)
Net realized capital gains		(0.03)	(0.12)		
Other ⁽³⁾			0.01		
Net asset value at the end of year/period	\$13.69	\$13.19	\$13.94	\$14.54	\$14.45
	\$12.06	\$9.64	\$11.78	\$14.95	\$16.38

Per share market value at end of year/period										
Total return based on market value ⁽⁴⁾	42.83	%	(7.76)%	(13.09)%	0.42	%	10.48	%
Weighted average shares outstanding at the end of period	12,479,959		12,479,961		12,281,178		12,059,293		12,035,023	
Ratio/Supplemental Data:										
Net assets at the end of year/period	\$ 170,881,785		\$ 164,651,104		\$ 173,949,452		\$ 175,891,514		\$ 173,845,955	
Weighted average net assets	\$ 165,189,142		\$ 173,453,813		\$ 176,458,141		\$ 175,398,660		\$ 173,845,955	
Annualized ratio of gross operating expenses to net assets ⁽⁷⁾⁽⁸⁾	13.20	%	11.16	%	9.92	%	8.65	%	5.49	%
Annualized ratio of net operating expenses to net assets ⁽⁷⁾⁽⁸⁾	13.20	%	10.78	%	9.12	%	7.63	%	5.50	%
Annualized ratio of interest expense and other fees to net assets	4.84	%	3.56	%	3.01	%	1.78	%	0.26	%
Annualized ratio of net investment income before fee waiver to net assets ⁽⁷⁾	10.71	%	9.11	%	8.40	%	8.11	%	4.99	%
Annualized ratio of net investment income to net assets ⁽⁷⁾	10.71	%	9.49	%	9.19	%	9.13	%	4.99	%
Portfolio Turnover ⁽⁵⁾	16	%	29	%	19	%	41	%	35	%
Notes Payable	25,000,000		25,000,000		25,000,000		110,000,000		38,000,000	
Credit Facility Payable	116,000,000		109,500,000		106,500,000		9,000,000		45,000,943	
SBA Debentures	65,000,000		65,000,000		16,250,000					
Asset Coverage Ratio ⁽⁶⁾	2.21x		2.22x		2.32x		2.48x		4.57x	

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

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

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.
Includes the impact of different share amounts as a result of calculating certain per share data based on weighted
- (3) 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. The total returns are not annualized.
- (5) Calculated as the lesser of purchases or paydowns divided by average portfolio balance and is not annualized.
Asset coverage ratio is equal to (i) the sum of (a) net assets at the end of the period and (b) total debt outstanding at
- (6) the end of the period, divided by (ii) total debt outstanding at the end of the period. SBA-guaranteed debentures are excluded from the numerator and denominator.
These ratios include the impact of the benefit (provision) for income taxes related to net unrealized loss (gain) on certain investments of \$373,131, (\$93,601) and (\$288,122) for the years ended December 31, 2016, 2015 and 2014 respectively, which are not reflected in net investment income, gross operating expenses or net operating expenses.
- (7) 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, 2016 and 2015 is (0.16)%, 0.05% and 0.17%, respectively.
- (8) Deferred offering costs of \$261,761 for the year ended December 31, 2016 are not annualized.

NOTE 9 CREDIT FACILITY

On November 7, 2012, the Company entered into a revolving credit facility (the Credit Facility) with various lenders. SunTrust Bank, one of the lenders, serves as administrative agent under the Credit Facility. The Credit Facility, as amended on November 21, 2014 and August 31, 2016, provides for borrowings in an aggregate amount of \$120,000,000 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. There can be no assurances that existing lenders will agree to such an increase, or that additional lenders will join the Credit Facility to increase available borrowings.

Borrowings under the Credit Facility bear interest, subject to the Company's election, on a per annum basis equal to (i) LIBOR plus 2.625% with no LIBOR floor or (ii) 1.625% 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 1, 2018.

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 affirmative and negative covenants, including but not limited to: (i) maintaining a minimum liquidity test of at least 85% of adjusted borrowing base, (ii) maintaining an asset coverage ratio of at least 2.0 to 1.0, and (iii) maintaining a minimum shareholder's equity. As of December 31, 2016, the Company was in compliance with these covenants.

Additionally, the Credit Facility requires that the Company meet certain conditions in connection with incurring additional indebtedness under the Credit Facility, including that the Company have a minimum asset coverage ratio after giving effect to such borrowing. On August 31, 2016, the Credit Facility was amended to reduce asset coverage related to additional indebtedness from 2.25 to 2.20 to 1.0, as long as certain conditions are met. These conditions state that (i) the aggregate amount of PIK interest during the most recently ended fiscal quarter of the borrower does not exceed 2% of the aggregate amount of interest income that the borrower has received on all investments in the borrowing base during such fiscal quarter; (ii) the sum of the value of all non-accrual investments does not exceed 5% of the value of all

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STELLUS CAPITAL INVESTMENT CORPORATION

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December 31, 2016

NOTE 9 CREDIT FACILITY (continued)

investments in the borrowing base and (iii) the borrower maintains a minimum liquidity test of at least 80% of adjusted borrowing base. As of December 31, 2016, these conditions were met.

As of December 31, 2016 and December 31, 2015, the outstanding balance under the Credit Facility was \$116,000,000 and \$109,500,000, respectively. The carrying amount of the amount outstanding under the Credit Facility approximates its fair value. The Company incurred total costs of \$3,067,715 in connection with obtaining, amending, and maintaining the Credit Facility, which are being amortized over the life of the Credit Facility. As of December 31, 2016 and December 31, 2015, \$828,792 and \$1,302,627 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. See Note 1 for further discussion.

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

	December 31, 2016	December 31, 2015
Credit Facility payable	\$ 116,000,000	\$ 109,500,000
Prepaid loan structure fees	828,792	1,302,627
Credit facility payable, net of prepaid loan structure fees	\$ 115,171,208	\$ 108,197,373

For the year ended December 31, 2016, the weighted average effective interest rate under the Credit Facility was approximately 3.2% (approximately 3.7% including commitment fees and other loan fees). Interest is paid quarterly in arrears. The Company recorded interest and fee expense on the Credit Facility of \$3,974,195 for the year ended December 31, 2016, of which \$3,383,572 was interest expense, \$471,501 was amortization of loan fees paid on the Credit Facility, \$66,787 related to commitment fees on the unused portion of the Credit Facility, and \$52,335 related to loan administration fees. The Company paid \$3,423,226 in interest expense and unused commitment fees for the year ended December 31, 2016. The average borrowings under the Credit Facility for the year ended December 31, 2016 were \$106,601,093.

For the year ended December 31, 2015, the weighted average effective interest rate under the Credit Facility was approximately 2.9% (approximately 3.5% including commitment fees and other loan fees). Interest is paid quarterly in arrears. The Company recorded interest and fee expense on the Credit Facility of \$3,571,940 for the year ended December 31, 2015, of which \$2,962,885 was interest expense, \$473,398 was amortization of loan fees paid on the Credit Facility, \$87,052 related to commitment fees on the unused portion of the Credit Facility, and \$48,605 related to loan administration fees. The Company paid \$3,096,966 in interest expense and unused commitment fees for the

year ended December 31, 2015. The average borrowings under the Credit Facility for the year ended December 31, 2015 were \$102,800,824.

For the year ended December 31, 2014, the weighted average effective interest rate under the Credit Facility was approximately 3.2% (approximately 3.9% including commitment fees on the unused portion and other loan fees for the Credit Facility). Interest is paid quarterly in arrears. The Company recorded interest and fee expense of \$4,094,945 for the year ended December 31, 2014, of which \$3,296,026 was interest expense, \$558,481 was amortization of loan fees paid on the Credit Facility, \$191,516 related to commitment fees on the unused portion of the Credit Facility, and \$48,922 related to loan administration fees. The Company paid \$3,607,979 in interest expense and unused commitment fees for the year ended December 31, 2014. The average borrowings under the Credit Facility for the year ended December 31, 2014 were \$103,714,726.

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, an SBIC

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STELLUS CAPITAL INVESTMENT CORPORATION

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December 31, 2016

NOTE 10 SBA-GUARANTEED DEBENTURES (continued)

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 both December 31, 2016 and December 31, 2015, the SBIC subsidiary had \$32.5 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 \$65 million (based on current regulatory capital, as such term is defined by the SBA, of \$32.5 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 \$106,280,627 and \$99,126,529 in assets at December 31, 2016 and December 31, 2015, respectively, which accounted for approximately 28.0% and 26.8% of our total consolidated assets at December 31, 2016 and December 31, 2015, 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 December 31, 2016 and December 31, 2015, the SBIC subsidiary had \$65,000,000 of SBA-guaranteed debentures outstanding, which mature ten years from issuance. The first maturity related to the SBIC-guaranteed debentures does not occur until 2025, and the remaining weighted average duration of all of our outstanding SBA-guaranteed debentures is approximately 8.9 years as of December 31, 2016.

As of December 31, 2016 and December 31, 2015, 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, 2016 and December 31, 2015 the SBA-guaranteed debentures would be deemed to be Level 3, as defined in Note 6.

As of December 31, 2016, the Company has incurred \$2,226,250 in financing costs related to the SBA-guaranteed debentures. As of December 31, 2016 and December 31, 2015, \$1,657,964 and \$1,984,154 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 is a summary of the SBA-guaranteed debentures, net of prepaid loan fees:

	December 31, 2016	December 31, 2015
SBA-guaranteed debentures payable	\$ 65,000,000	\$ 65,000,000
Prepaid loan fees	1,657,964	1,984,154
SBA-guaranteed debentures, net of prepaid loan fees	\$ 63,342,036	\$ 63,015,846

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

NOTE 10 SBA-GUARANTEED DEBENTURES (continued)

For the year ended December 31, 2016, the weighted average effective interest rate for the SBA-guaranteed debentures was approximately 2.9% (approximately 3.4% including loan fees). Interest is paid semi-annually. The Company recorded interest and fee expense on the SBA-guaranteed debentures of \$2,203,208 for the year ended December 31, 2016, of which \$1,877,017 was interest expense, and \$326,191 was amortization of loan fees. The Company paid \$1,500,528 of interest expense during the year ended December 31, 2016. The average borrowings of SBA-guaranteed debentures for the year ended December 31, 2016 were \$65,000,000.

For the year ended December 31, 2015, the weighted average effective interest rate for the SBA-guaranteed debentures was approximately 2.2% (approximately 3.0% including loan fees). Interest is paid semi-annually. The Company recorded interest and fee expense on the SBA-guaranteed debentures of \$765,011 for the year ended December 31, 2015, of which \$560,031 was interest expense, and \$204,980 was amortization of loan fees. The Company paid \$289,018 of interest expense during year ended December 31, 2015. The average borrowings of SBA-guaranteed debentures for the year ended December 31, 2015 were \$25,437,671.

For the year ended December 31, 2014, the weighted average effective interest rate for the SBA-guaranteed debentures was approximately 1.0% (approximately 2.3% including loan fees), which reflects a lower pre-pooling rate that increases when the SBA-guaranteed debentures pool in March and September. Interest is paid semi-annually. The Company recorded interest and fee expense on the SBA-guaranteed debentures of \$64,488 for the year ended December 31, 2014, of which \$27,372 was interest expense, and \$37,116 was amortization of loan fees. The company paid no interest expense during the year ended December 31, 2014. The average borrowings of SBA-guaranteed debentures for the year ended December 31, 2014 were \$13,082,278.

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 Notes). The Notes mature on April 30, 2019, 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 April 30, 2016. The Notes bear interest at a rate of 6.50% per year payable quarterly on February 15, May 15, August 15 and November 15, of each year. The Notes are unsecured obligations and rank pari passu with our current and future unsecured indebtedness; senior to any of our future indebtedness that expressly provides it is subordinated to the Notes; effectively subordinated to all of our existing and future secured indebtedness, to the extent of the value of the assets securing such indebtedness, including borrowings under our Credit Facility; and structurally subordinated to all existing and future indebtedness and other obligations of any of our subsidiaries, including without limitation, the indebtedness of the SBIC subsidiary. The net proceeds to the Company from the sale of the Notes, after underwriting discounts and offering expenses, were approximately \$24.1 million. The Company used all of the net proceeds from this offering to repay a portion of the amount outstanding

under the Credit Facility. On both December 31, 2016 and December 31, 2015, the carrying amount of the Notes was approximately \$25,000,000 and the fair value of the Notes was approximately \$25.2 million and \$24.6 million, respectively. The Notes are listed on New York Stock Exchange under the trading symbol SCQ . 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 of the Notes, we incurred \$929,570 of fees which are being amortized over the term of the Notes. As of December 31, 2016 and December 31, 2015 \$434,109 and \$618,892 of such prepaid loan structure fees and administration fees had yet to be amortized, 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. See Note 1 for further discussion.

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STELLUS CAPITAL INVESTMENT CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2016

NOTE 11 NOTES (continued)

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

	December 31, 2016	December 31, 2015
Notes payable	\$ 25,000,000	\$ 25,000,000
Deferred financing costs	434,109	618,892
Notes payable, net of deferred financing costs	\$ 24,565,891	\$ 24,381,108

For the year ended December 31, 2016, the Company incurred interest and fee expense on the Notes of \$1,814,783, of which \$1,625,000 was interest expense, \$184,933 was amortization of loan fees paid on the Notes, and \$4,850 related to administration fees. The Company paid \$1,625,000 in interest expense on the Notes during the period.

For the year ended December 31, 2015, the Company incurred interest and fee expense on the Notes of \$1,840,064, of which \$1,625,000 was interest expense, \$209,703 was amortization of loan fees paid on the Notes, and \$5,361 related to administration fees. The Company paid \$1,625,000 in interest expense on the Notes during the period.

For the period from May 5, 2014 to December 31, 2014, the Company incurred interest and fee expense on the Notes of \$1,155,892, of which \$1,065,278 was interest expense, \$89,676 was amortization of loan fees paid on the Notes, and \$938 related to administration fees. The Company paid \$857,639 in interest expense on the Notes during the period.

The indenture and supplements thereto relating to the 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.

NOTE 12 SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table sets forth the results of operations for the years ended December 31, 2016, 2015, and 2014. Results for any quarter are not necessarily indicative of results for the full year or for any future quarter.

	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

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	2015			
	Qtr. 1	Qtr. 2	Qtr. 3	Qtr. 4
Total Investment Income	\$8,714,091	\$8,690,462	\$8,602,813	\$9,151,193
Net Investment Income	\$3,843,415	\$3,995,487	\$3,819,631	\$4,888,595
Net Increase (decrease) in Net Assets from Operations	\$5,393,374	\$4,000,993	\$(624,337)	\$(1,099,494)
Total Investment Income per share ⁽¹⁾	\$0.70	\$0.70	\$0.69	\$0.73
Net Investment Income per share ⁽¹⁾	\$0.31	\$0.32	\$0.31	\$0.39
Net Increase (decrease) in Net Assets from Operations per share ⁽¹⁾	\$0.43	\$0.32	\$(0.05)	\$(0.09)

	2014			
	Qtr. 1	Qtr. 2	Qtr. 3	Qtr. 4
Total Investment Income	\$7,849,246	\$8,012,709	\$7,822,497	\$8,640,395
Net Investment Income	\$3,761,044	\$3,704,862	\$5,250,497	\$3,795,694
Net Increase in Net Assets from Operations	\$4,343,761	\$2,711,567	\$2,113,431	\$1,010,383
Total Investment Income per share ⁽¹⁾	\$0.65	\$0.66	\$0.63	\$0.69
Net Investment Income per share ⁽¹⁾	\$0.31	\$0.31	\$0.42	\$0.30
Net Increase in Net Assets from Operations per share ⁽¹⁾	\$0.36	\$0.22	\$0.17	\$0.08

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

NOTE 13 INCOME TAXES

As of both December 31, 2016 and December 31, 2015, the Company had \$1,307,452 and \$18,682, respectively, of undistributed ordinary income.⁽¹⁾ Undistributed capital gains were \$0 for the periods ended December 31, 2016 and December 31, 2015. All of the undistributed ordinary income as of December 31, 2016 will have been distributed 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, 2016. We will be 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 \$22,663 and \$0 of U.S.

federal excise tax for the years ended December 31, 2016 and December 31, 2015, respectively.

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, 2016 and 2015 was as follows:

	December 31, 2016	December 31, 2015
Ordinary income	\$ 16,968,350	\$ 16,203,494
Distributions of long-term capital gains ⁽²⁾		765,390
Total distributions accrued or paid to common stockholders	\$ 16,968,350	\$ 16,968,884

⁽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

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undistributed ordinary income and capital gains for each period carried forward for distribution in the following period, may be different than this estimate.

Distributions of long-term capital gains of \$765,390 as of December 31, 2015 differs from distributions of net (2) capital gains on the Consolidated Statement of Changes in Net Assets because certain prepayment gains are characterized differently for tax reporting purposes.

At December 31, 2016, 2015 and 2014, the components of undistributed earnings on a tax basis detailed below differ from the amounts reflected in the Company's Consolidated Balance Sheet as Distributions in excess of net investment income and Accumulated undistributed net realized gain. Differences for tax reporting arise from permanently disallowed items, as well as temporary differences in reporting primarily relating to the amortization of certain start-up and organizational costs and expenses incurred by the Taxable Subsidiaries included in the calculation of net investment income but excluded from the calculation of distributable taxable income.

	December 31, 2016	December 31, 2015	December 31, 2014
Distributions in excess of net investment income	\$(435,794)	\$(779,643)	\$(779,643)
Cumulative permanent differences related to net investment income	434,654	147,894	108,822
Cumulative temporary differences related to net investment income	1,308,592	650,431	763,310
Accumulated undistributed taxable income	\$1,307,452	\$18,682	\$92,489

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, 2016 and December 31, 2015 were as follows:

	2016	2015
Aggregate cost of portfolio securities for federal income tax purposes	\$362,217,251	\$364,212,459
Gross unrealized appreciation of portfolio company securities	7,011,949	2,007,549
Gross unrealized depreciation of portfolio company securities	(3,603,309)	(17,202,311)
Net unrealized appreciation (depreciation) of portfolio company securities	\$3,408,640	\$(15,194,762)

As of December 31, 2016, an unrealized loss and a capital loss carryover were generated in two Taxable Subsidiaries of SCIC, creating a deferred tax asset. Due to the nature of the entity a valuation allowance was established when management determined it is more likely than not that some of the deferred tax assets will not be realized. 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 \$4,092,120 for SCIC Consolidated Blocker, Inc. and \$52,597 for SCIC SKP Blocker 1, Inc. for a combined deferred tax asset valuation allowance of \$4,144,717. The Company has recorded a \$8,593 deferred tax liability associated with the unrealized gain in SCIC APE Blocker 1, Inc. which is reported on the Consolidated Statements of Assets and Liabilities.

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STELLUS CAPITAL INVESTMENT CORPORATION

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2016**

NOTE 13 INCOME TAXES (continued)

	2016	2015
Deferred Tax Asset	\$ 86,643	\$ 115,666
Capital Loss Carryover	4,442,403	
Deferred Tax Liability	\$ (392,922)	\$ (426,089)
Total Deferred Tax Asset (Liability) before Valuation Allowance	4,136,124	(310,423)
Deferred Tax Valuation Allowance	\$ (4,144,717)	\$ (71,300)
Net Deferred Tax Liability	\$ (8,593)	\$ (381,723)

Although the Company files federal and state tax returns, its major tax jurisdiction is federal. The 2013, 2014 and 2015 federal tax years for the Company remain subject to examination by the Internal Revenue Service.

NOTE 14 SUBSEQUENT EVENTS

Investment Portfolio

On January 5, 2017, the Company sold its position in Securus Technologies Holdings, Inc for proceeds of \$8.4 million. We realized a loss of \$41K upon the sale.

On January 25, 2017, the Company received full repayment on the first lien term loan of Momentum Telecom, Inc for proceeds of \$15.3 million, including a \$0.2 million premium.

On February 1, 2017, the Company's first lien term loan in Glori Energy Production, Inc was converted to an equity position at par equal to \$1.7 million.

On February 3, 2017, the Company invested \$6.3 million in the unsecured term loan of Time Manufacturing, Inc, a global manufacturer of vehicle-mounted aerial lift equipment. Additionally, the Company invested \$0.5 million in the equity of the company.

On February 8, 2017, the Company received full repayment on the second lien term loan of MTC Intermediate Holdco for proceeds of \$10.4 million, including a \$0.1 million prepayment fee. Additionally, the Company received a dividend of \$0.7 million in proceeds for the equity in MTC Parent, LP.

On March 1, 2017, the Company received full repayment on the first lien term loan of 360 Holdings Corp for proceeds of \$4.0 million.

Credit Facility

The outstanding balance under the Credit Facility as of March 8, 2017 was \$103.8 million.

Dividend Declared

On January 13, 2017, the Company's board of directors declared a regular monthly dividend for each of January 2017, February 2017 and March 2017 as follows:

Declared	Ex-Dividend Date	Record Date	Payment Date	Amount per Share
1/13/2017	1/27/2017	1/31/2017	2/15/2017	\$ 0.1133
1/13/2017	2/24/2017	2/28/2017	3/15/2017	\$ 0.1133
1/13/2017	3/29/2017	3/31/2017	4/14/2017	\$ 0.1133

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Stellus Capital Investment Corporation

3,000,000 Shares

PRELIMINARY PROSPECTUS SUPPLEMENT

RAYMOND JAMES

Keefe, Bruyette & Woods
A Stifel Company

April , 2017
