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Zacks Small-Cap Research

Sponsored – Impartial - Comprehensive

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Alcentra Capital (ABDC-NASDAQ)

ABDC: Alcentra Capital to Be Acquired By Crescent Capital for $11.02, or NAV, and Become Part of a New Public Company

We believe the stock should trade at $11.00 per share based on the offer to purchase the company by Crescent Capital.

OUTLOOK

Alcentra Capital is a business development company (BDC) with a disciplined portfolio approach and the benefit of an affiliation with BNY Mellon. The company's target market is the lower middle-market, which management believes traditional lenders underserve. Management has been pursuing strategic alternatives to reduce its discount to NAV, and today announced it had agreed to a merger with Crescent Capital to close in the fourth quarter.

Current Price (08/13/19)	$9.20
Valuation	**$11.00**

SUMMARY DATA

52-Week High	**$9.40**
52-Week Low	**$5.63**
One-Year Return (%)	**58.1**
Beta	**0.6**
Average Daily Volume (sh)	**19,263**
Shares Outstanding (mil)	**12.9**
Market Capitalization ($mil)	**$119**
Short Interest Ratio (days)	**1.3**
Institutional Ownership (%)	**36**
Insider Ownership (%)	**1**
Annual Cash Dividend	**$0.72**
Dividend Yield (%)	**8.8**
5-Yr. Historical Growth Rates	
Sales (%)	**1.8**
Earnings Per Share (%)	**-11.5**
Dividend (%)	**-15.4**
P/NII using TTM Price/NII	**10.1**
P/NII using 2019 Estimate	**11.5**
P/NII using 2020 Estimate	**11.5**
Zacks Rank	**N/A**

Risk Level	**Low**
Type of Stock	**Small Value**
Industry	**Fin-SBIC&Commercl**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	9.2 A	8.3 A	7.6 A	8.2 A	33.4 A
2018	8.2 A	7.3 A	6.6 A	7.0 A	29.0 A
2019	6.4 A	6.1 A	6.0 E	6.0 E	24.5 E
2020					24.5 E

Adjusted NII Per Share

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2017	$0.34 A	$0.36 A	$0.34 A	$0.28 A	$1.32 A
2018	$0.27 A	$0.25 A	$0.22 A	$0.27 A	$1.01 A
2019	$0.22 A	$0.20 A	$0.19 E	$0.19 E	$0.80 E
2020					$0.80 E

Zacks Projected EPS Growth Rate - Next 5 Years % **N/A**

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WHAT'S NEW

After months of pursing a strategic review looking for alternatives to increase the company's value, management has struck a deal to sell it. Today Crescent Capital BDC and Alcentra Capital announced that they have entered into a definitive merger agreement under which Crescent BDC will acquire Alcentra Capital for $11.02 per share (the portfolio's current NAV). This will be by a combination of $3.18 in cash, and stock in the new public company to be formed by the merger.

In detail, in exchange for approximately 12.9 million shares of Alcentra Capital common stock, Alcentra Capital's stockholders will receive approximately (i) $19.3 million in cash, or $1.50 per share, from Crescent BDC; (ii) 5.2 million shares of Crescent BDC common stock; and (iii) $21.6 million in cash, or $1.68 per share, from CBDC Advisors, LLC, Crescent BDC's investment adviser. Any final dividend that Alcentra Capital must pay in connection with the closing of the transaction to comply with applicable tax requirements that is in excess of Alcentra Capital's regular quarterly dividends will reduce the cash consideration to be paid by Crescent BDC on a dollar-for-dollar basis. The total cash and stock consideration to be received at closing is currently estimated to be approximately $141.9 million after taking into account certain post-closing adjustments.

The transaction is expected to close in the December quarter. The Committee of Independent Directors, the independent directors of Crescent BDC, and the boards of directors of both companies, have all unanimously approved it.

The combination should create a top-15, externally managed, publicly traded BDC with significantly increased market presence, and improved economies of scale. The merged company is estimated to have over $500 million of net assets and a portfolio in excess of $900 million. There will be enhanced portfolio diversification consistent with Crescent BDC's and Alcentra Capital's strategy of maintaining a senior secured first lien-focused portfolio. Management plans to facilitate a dividend policy designed to over-earn a **quarterly $0.41 dividend per share**, further strengthen Crescent BDC's balance sheet, and augment access to growth capital.

It will be run under best-in-class fee structure with reduced base management fee rates and increased hurdle rates:

- Annual base management fee rate reduced from 1.50% to 1.25%;
- Six quarters of base management fee waivers, so that only 0.75% will be charged for such time period;
- Annualized incentive fee hurdle increased from 6% to 7% while maintaining a 17.5% income incentive fee;
- Six quarters of full waivers of the income-based portion of the incentive fee.

Crescent BDC and Alcentra Capital will be holding a joint conference call to discuss the transaction today, August 13, 2019, at 4:15 p.m. ET.

KEY POINTS

- Alcentra Capital is a business development company (BDC) with a disciplined portfolio approach and the benefit of an affiliation with BNY Mellon.

- The company originally targeted the lower middle-market, but new management has rotated the portfolio to larger middle-market private equity backed transactions. It considers the middle market $15 million - $75 million in EBITDA.

- As of June 30, the company's $219 million portfolio was composed of 29 investments, comprised of 28 companies, and one rated CLO debt instrument. It was invested 93% in debt and 7% in equity.

- At $9.20, the shares trade at a **16.5% discount to the company's $11.02 NAV** (net asset value) per share and the Crescent Capital offer price. At its current price, Alcentra's dividend yield, not including the special dividend is 7.8%, still below the average of 10.0%. Management plans to facilitate a dividend policy designed to over-earn a **quarterly $0.41 dividend per share** for the merged company.

VALUATION



Alcentra is outperforming the BDC index. As noted on the following table, on an NAV basis, BDC industry shares trade at an average 9.4% premium to share price. There is a wide valuation gap among the BDCs as shown below. Alcentra stock currently trades at a lower than average dividend yield of 7.8% versus the average at 9.9% when not including special dividends.

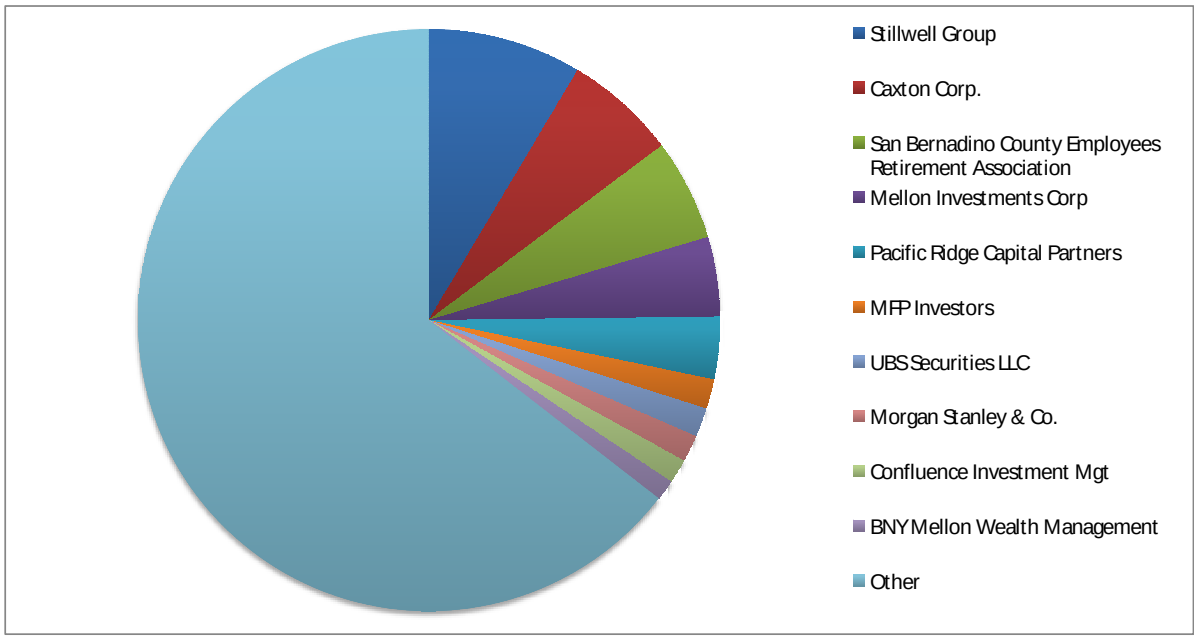
BDCs			52-Week		Annualized			
Company	Ticker	Price	High	Low	Div.	Yield	NAV	Disc to NAV
Alcentra Capital	ABDC	$9.20	$9.40	$5.58	$0.72	7.8%	$11.02	16.5%
Apollo Investment Corp	AINV	16.23	17.82	12.05	$1.80	11.1%	19.00	14.6%
Ares Capital Corp	ARCC	18.31	18.83	14.50	$1.68	9.2%	17.27	-6.0%
BlackRock Capital Investm	BKCC	5.42	6.64	5.06	$0.72	13.3%	6.82	20.5%
Fidus Investment Corp.	FDUS	14.88	16.50	11.48	$1.56	10.5%	16.29	8.7%
Garrsion Capital Inc.	GARS	7.00	8.84	6.03	$0.92	13.1%	8.23	14.9%
Gladstone Capital Corp.	GLAD	9.35	8.84	6.03	$0.84	9.0%	8.11	-15.3%
Main Street Capital Corp.	MAIN	42.50	42.93	31.95	$2.46	5.8%	24.41	-74.1%
Newtek Business Services	NEWT	21.26	24.24	15.59	$1.60	7.5%	15.31	-38.9%
TriplePoint Venture Growth	TPVG	15.48	15.37	10.25	$1.44	9.3%	14.19	-9.1%
Average					$1.45	9.9%	$14.40	-9.4%

RISKS

We believe the company faces risks that confront the overall BDC sector, but the merger will mitigate some of these risks by its size and diversity. These include:

- **Interest rate risk:** We believe the company faces the risk of a changing interest rate environment; it is currently suffering from a decline in rates, particularly LIBOR.
- **Credit risk:** Alcentra could make investments into companies that are not as creditworthy as management believes or some of the investments in its existing portfolio could experience deteriorating fundamental business results.
- **Default risk:** Potential deterioration in the underlying fundamentals of a portfolio company or companies could lead to a default on loans that Alcentra expects repaid.
- **Dividend sustainability:** If the company experiences some deterioration in its underlying performance, it might be forced to reduce its dividend.
- **Competitive risk:** The company competes with alternative lenders such as other BDCs and, in some cases, with traditional lenders. Competition within its target lower middle market has increased and the company anticipates future deals will have lower yields.

OWNERSHIP



INCOME STATEMENT

Dollars in Millions	2018				2019							
	31-Mar-18	30-Jun-18	30-Sep-18	31-Dec-18	31-Mar-19	30-Jun-19	30-Sep-19E	31-Dec-19E	2017	2018	2019E	2020E
Non-controlled, non-affiliated investments:												
Interest Income from portfolio investments	$5,742,386	$5,865,711	$5,676,759	$5,450,756	$5,806,309	$5,753,089	$5,600,000	$5,580,000	$23,917,956	$22,735,612	$22,739,398	$22,000,000
Paid in kind int inc. from portfolio investments	199,650	45,481	107,164	151,844	84,504	28,797	28,797	28,797	1,156,486	504,139	170,895	300,000
Other income from portfolio investments	1,507,304	611,812	94,668	738,206	107,757	177,118	200,000	200,000	2,228,104	2,951,990	684,875	500,000
Dividend income from portfolio investments	30,756	30,756	30,756	30,756	-	-	-	-	171,083	123,024	-	-
Non-controlled, affiliated investments:												
Interest income from portfolio investments	77,453	129,080	58,881	40,790	36,479	41,762	40,000	40,000	1,318,924	306,204	158,241	300,000
Paid in kind int inc. from portfolio investments	123,126	90,004	96,816	96,676	96,413	93,190	93,190	90,000	2,209,418	406,622	372,793	400,000
Other income from portfolio investments	-	-	-	-	-	-	-	-	-	-	-	-
From controlled, affiliated investments:												
Interest income from portfolio investments	500,890	481,106	488,036	470,357	208,538	-	-	-	1,665,409	1,940,389	208,538	1,000,000
Paid in kind int inc. from portfolio investments	-	-	-	-	-	-	-	-	684,129	-	-	-
Other income from portfolio investments	-	-	-	-	87,116	45,979	45,000	30,000	-	-	208,095	-
TOTAL INVESTMENT INCOME	**$8,181,565**	**$7,253,950**	**$6,553,080**	**$6,979,385**	**$6,427,116**	**$6,139,935**	**$6,006,987**	**$5,968,797**	**$33,351,509**	**$28,967,980**	**$24,542,835**	**$24,500,000**
Yr-to-yr growth	-11%	-13%	-14%	-15%	-21%	-15%	-8%	-14%	-17.9%	-13.1%	-15.3%	-0.2%
Costs and expenses:												
Management fees	1,234,863	1,036,122	943,360	918,791	865,618	841,566	780,908	775,944	4,975,349	4,133,136	3,264,036	3,185,000
% of Sales	15%	14%	14%	13%	13%	14%	13%	13%	15%	14%	13%	13%
Income-based incentive fee	-	-	(43,805)	(360,384)	(487,124)	(204,867)	(234,272)	(232,783)	638,244	(404,189)	(1,159,047)	(424,398)
	0%	0%	-0.7%	-5.2%	-7.6%	-3.3%	-3.9%	-3.9%				
Capital gains incentive fees	-	-	-	-	-	-	-	-	-	-	-	-
Professional fees	354,070	379,082	362,625	536,378	625,229	774,386	780,000	780,000	1,248,715	1,632,155	2,959,615	2,500,916
Valuation services	63,971	(10,038)	78,346	73,345	71,250	86,250	86,250	86,250	314,432	205,624	330,000	275,000
Interest and credit facility expense	1,694,887	1,745,485	1,705,992	1,503,203	1,417,450	1,322,878	1,300,000	1,300,000	6,434,924	6,649,567	5,340,328	5,340,328
Amortization of deferred financing costs	103,981	103,570	117,587	221,019	206,116	206,429	206,429	206,429	912,710	546,157	825,403	884,076
Director's fees	96,202	116,826	87,076	128,057	159,676	215,000	215,000	215,000	341,680	428,161	804,676	800,000
Insurance expense	55,988	56,519	57,076	57,075	55,835	91,492	91,492	91,492	239,048	226,658	330,311	240,000
Organization expense	-	-	-	-	-	-	-	-	-	-	-	-
Amortization of deferred note offering costs	126,694	119,267	97,478	95,293	133,363	109,340	109,340	109,340	473,768	438,732	461,383	400,000
Consulting fees	305,038	176,702	54,152	120,031	111,601	133,315	140,000	140,000		655,923	524,916	500,000
Excise tax	329,575	-	-	-	468,432	(78,019)	(78,019)	(78,019)			234,375	234,375
Other expenses	40,136	156,108	284,764	478,298	62,448	251,851	251,851	251,851	778,920	959,306	818,001	818,001
TOTAL EXPENSES	4,405,405	3,879,643	3,744,651	3,771,106	3,689,894	3,749,621	3,648,979	3,645,504	16,357,790	15,471,230	14,733,997	14,753,298
Waiver of income-based incentive fee	-	109,281	157,227	153,132	144,270	140,261	132,154	131,314	1,330,420	419,640	547,998	500,000
NET EXPENSES	**$4,405,405**	**$3,770,362**	**$3,587,424**	**$3,617,974**	**$3,545,624**	**$3,609,360**	**$3,516,825**	**$3,514,190**	**$15,027,370**	**$15,051,590**	**$14,185,999**	**$14,253,298**
NET INVESTMENT INCOME	**$3,776,160**	**$3,483,588**	**$2,965,656**	**$3,361,411**	**$2,881,492**	**$2,530,575**	**$2,490,162**	**$2,454,607**	**$18,324,139**	**$13,916,390**	**$10,356,836**	**$10,246,702**
% Change	-17%	-28%	-47%	-17%	-24%	-27%	-16%	-27%	-18.2%	-24.1%	-25.6%	-1.1%
Adjusted NII/share	**$0.27**	**$0.25**	**$0.22**	**$0.25**	**$0.22**	**$0.20**	**$0.19**	**$0.19**	**$1.32**	**$1.01**	**$0.80**	**$0.80**
% Change	-21%	-30%	-43%	-12%	-16%	-22%	-12%	-24%	**-21%**	**-23%**	**1%**	**-22%**
Dividend per share	$0.18	$0.18	$0.18	$0.18	$0.18	$0.18	$0.18	$0.18	$1.30	$0.72	$0.72	$0.72
EPS	$0.25	-$0.16	$0.23	$0.08	$0.15	$0.17			-$1.37	$0.40		
NAV/share	$11.22	$11.01	$11.08	$11.13	$11.17	$11.02	$11.08	$11.09	$11.06	$11.13	$11.29	$11.21
Avg shares outstanding	14,198,651	13,753,054	13,530,129	13,440,660	12,906,379	12,875,566	12,875,566	12,875,566	13,928,869	13,721,109	12,883,269	12,875,566

BALANCE SHEET

	June 30, 2019	March 31, 2019	Qtr-Qtr Growth %	June 30, 2018	Yr-Yr Growth %
ASSETS					
Portfolio investments, at fair value					
Non-controlled, non-affiliated at fair value	204,633,762	199,599,456	3%	212,917,961	-4%
Non-controlled, affiliated at fair value	14,573,438	14,149,845	3%	17,987,393	-19%
Controlled, affiliated at fair value	-	-	0%	15,254,506	-100%
Cash	7,796,536	4,362,418	79%	12,704,301	-39%
Dividends and interest receivable	1,404,187	1,241,095	13%	2,715,171	-48%
Receivable for investments sold	2,674,457	7,797,809	-66%	669,733	299%
Deferred financing costs	1,066,348	1,160,277	-8%	419,191	154%
Deferred tax asset	4,263,462	5,132,895	-17%	5,955,112	-28%
Income tax asset	-	-	0%	644,319	-100%
Prepaid expenses and other assets	354,583	46,075	670%	208,562	70%
TOTAL ASSETS	236,766,773	233,489,870	1%	269,476,249	-12%
LIABILITIES					
Credit facility payable	26,565,008	28,568,305	-7%	58,553,273	-55%
Notes payable	54,357,269	54,247,929	0%	53,963,795	1%
Payable for investments purchased	5,925,000	-	NM	-	NM
Other accrued expenses and liabiliities	251,183	466,521	-46%	523,720	-52%
Directors' fees payable	197,154	130,000	52%	36,125	446%
Professional fees payable	886,641	661,207	34%	643,322	38%
Interest and credit facility expense payable	1,176,846	1,529,992	-23%	1,158,173	2%
Management fee payable	701,305	721,348	-3%	926,841	-24%
Income-based incentive fees payable	198,805	403,672	-51%	1,294,985	-85%
Distributions payable	4,248,937	2,433,102	75%	2,449,591	73%
Unearned structuring fee revenue	-	59,540	-100%	331,680	-100%
Income tax liability	320,630	412,944	-22%	-	NA
Total Liabilities	94,828,778	89,634,560	6%	119,881,505	-21%
NET ASSETS					
Common stock	12,876	12,876	0%	13,583	-5%
Additional paid-in capital	197,118,476	197,118,476	0%	202,161,682	-2%
Distributable earnings (accumlated loss)	(55,193,357)	(53,276,042)	4%	(31,726,764)	74%
Total Net Assets	141,937,995	143,855,310	-1%	149,594,744	-5%
Total Liabilities and Net Assets	236,766,773	233,489,870	1%	269,476,249	-12%
Net Asset Value Per Share	**$11.02**	**$11.17**	-1%	**$11.01**	0%

CASH FLOW

Cash Flows from Operating Activities	Year 2017	March 31, 2018	June 30, 2018	Sept 30, 2018	Dec 31, 2108	Year 2018	March 31, 2019	June 30, 2019
Net increase in net assets resulting from operations	(19,101,742)	$3,538,960	(2,239,011)	3,082,002	1,140,181	5,522,132	$1,962,295	2,144,935
Adjustments:								
Net realized (gain) loss from portfolio investments	11,434,891	14,815	20,275,794	38,933	15,076,636	35,406,178	522,300	(1,604,042)
Net change in unrealized (appreciation) depreciation of port inves	28,598,870	219,896	(13,533,478)	(744,922)	(12,522,955)	(26,581,459)	300,450	1,015,320
Deferred tax asset	(3,670,151)	2,489	(1,022,639)	589,643	(20,225)	(450,732)	252,799	869,433
Deferred tax liability	-	-	-	-	-	-	-	-
Paid in-kind interest income from portfolio investments	(4,050,033)	(322,776)	(135,485)	(203,980)	(248,520)	(910,761)	(180,917)	(121,987)
Accretion of discount on debt securities	(1,905,751)	(176,258)	(165,987)	(139,445)	(442,036)	(923,726)	(397,439)	(600,630)
Purchases of portfolio investments	(135,508,569)	(29,996,191)	(14,052,612)	(6,000,691)	(54,797,852)	(104,847,346)	(26,765,630)	(31,970,339)
Net proceeds from sales/return of capital of portfolio invest.	90,148,997	47,628,196	31,638,771	4,573,014	66,773,862	150,613,843	47,569,751	27,823,779
Amortization of deferred financing costs	912,710	103,981	103,570	117,587	221,019	546,157	206,116	206,429
Amortization of deferred note offering costs	473,768	126,694	119,267	97,478	95,293	438,732	133,363	109,340
(Increase) decrease in operating assets:								
Dividends and interest receivable	1,298,340	307,530	(1,080,401)	1,314,465	945,823	1,487,417	(786,212)	(163,092)
Receivable for investments sold	1,469,730	25,000	(25,000)	25,000	-	25,000	(7,153,076)	5,123,352
Income tax asset	(748,408)	79,077	25,012	29,538	614,781	748,408	-	-
Prepaid expenses and other assets	21,765	33,488	(163,045)	64,576	64,576	(405)	33,335	(308,508)
Increase (decrease) in operating liabilities:								
Payable for investments purchased	-	16,621,902	(16,621,902)	-	18,550,000	18,550,000	(18,550,000)	5,925,000
Other accrued expenses and liabilities	165,424	470,143	(394,012)	(152,276)	163,652	87,507	(68,575)	(215,338)
Due to affiliate	-	-	-	-	-	-	-	-
Directors' fees payable	(26,083)	3,333	(36,125)	42,375	(42,375)	(32,792)	93,875	67,154
Professional fees payable	216,588	3,483	91,384	(324,817)	235,668	5,718	828,382	(495,914)
Interest and credit facility expense payable	240,664	278,767	(369,385)	184,355	(273,389)	(179,652)	460,853	(353,146)
Management fee payable	(36,419)	(30,309)	(308,022)	786,133	(947,315)	(499,513)	(765,659)	701,305
Income-based incentive fees payable	(776,676)	-	-	(43,805)	(360,384)	(404,189)	(487,124)	(204,867)
Unearned structuring fee revenue	(449,666)	(64,670)	(329,303)	(56,660)	(193,377)	(644,010)	(22,103)	(59,540)
Income tax	(182,699)	43,149	(43,149)	-	379,155	379,155	33,789	(92,314)
Net cash used in operating activities	(31,474,450)	38,910,699	1,734,242	3,278,503	34,412,218	78,335,662	(2,779,427)	7,796,330
Cash Flows from Financing Activities:								
Issuance of common stock	10,853,602	-	-	-	(1,398,309)	(1,398,309)	-	-
Financing costs paid	(139,144)	-	(112,501)	(1,219,999)	1,332,500	-	-	(112,500)
Offering costs paid	(230,871)	-	(30,001)	(11,999)	-	(42,000)	(30,001)	-
Proceeds from credit facility payable	117,820,000	12,700,000	8,650,000	4,903,872	37,601,288	63,855,160	29,977,494	21,628,841
Repayments of credit facility payable	(67,250,000)	(47,000,000)	(5,500,000)	(9,000,000)	(63,457,704)	(124,957,704)	(30,059,997)	(23,504,221)
Proceeds from notes payable	-	-	-	-	-	-	-	-
Distributions paid to shareholders	(19,245,277)	(3,561,305)	(2,560,130)	(2,449,592)	(2,449,591)	(11,020,618)	(2,433,102)	(2,246,415)
Repurchase of common stock	(342,510)	(1,510,605)	(2,899,054)	(413,341)	(2,718,360)	(7,541,360)	(1,476,415)	-
Capital contributions received from partners	-	-	-	-	-	-	-	-
Cash distributions paid to partners	-	-	-	-	-	-	-	-
Net cash provided by (used in) financing activities	41,465,800	(39,371,910)	(2,451,686)	(8,191,059)	(31,090,176)	(81,104,831)	(4,022,021)	(4,234,295)
Effect of exchange rate changes on foreign cash	-	-	-	-	(64,288)	(64,288)	114,367	(127,917)
Increase (decrease) in cash and cash equivalents	9,991,350	(461,211)	(717,444)	(4,912,556)	3,257,754	(2,833,457)	(6,687,081)	3,434,118
Cash at beginning of period	3,891,606	13,882,956	13,421,745	12,704,301	7,791,745	13,882,956	11,049,499	4,362,418
Cash and Cash Equivalents at End of Period	13,882,956	13,421,745	12,704,301	7,791,745	11,049,499	11,049,499	4,362,418	**7,796,536**
Supplemental and non-cash financing activities:								
Cash paid during the period for interest	6,194,260	1,416,120	2,114,870	1,521,637	1,776,592	6,829,219	956,597	1,676,024
Accrued offering costs	2,485	2,485	-	-	-	2,485	2,485	-
Accrued distributions payable	3,561,305	2,560,130	(110,539)	-	(16,489)	2,433,102	2,433,102	1,815,835

HISTORICAL STOCK PRICE



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