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**KCAP**  
**FINANCIAL, INC.**

**Investor Presentation**

**Third Quarter 2013**

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This presentation includes forward-looking statements. The matters discussed in this presentation, as well as in future oral and written statements by management of KCAP Financial, Inc., that are forward-looking statements are based on current management expectations that involve substantial risks and uncertainties which could cause actual results to differ materially from the results expressed in, or implied by, these forward-looking statements. Forward-looking statements relate to future events or our future financial performance. We generally identify forward-looking statements by terminology such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these terms or other similar words. Important assumptions include our ability to acquire or originate new investments, achieve certain margins and levels of profitability, the availability of additional capital, and the ability to maintain certain debt to asset ratios. In light of these and other uncertainties, the inclusion of a projection or forward-looking statement in this presentation should not be regarded as a representation by us that our plans or objectives will be achieved.

There are a number of important risks and uncertainties that could cause our actual results to differ materially from those indicated by such forward-looking statements. You should not place undue reliance on these forward-looking statements. The forward-looking statements relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statement to reflect events or circumstances occurring after the date of this presentation.

# INVESTMENT HIGHLIGHTS

## Innovative Strategy and Platform

- ◆ Internally managed structure – Low expense ratio
- ◆ 100% ownership of Asset Manager Affiliates (Katonah Debt Advisors and Trimaran Advisors)

## Highly Experienced Management Team

- ◆ Seasoned management team with average industry tenure of 25+ years
- ◆ Managed loan portfolios through numerous cycles

## Dynamic Business Model

- ◆ Compelling middle market opportunities; multi-channel origination capabilities
- ◆ Enhanced portfolio yield through high returns on investments in CLO funds
- ◆ Disciplined investment process with seasoned credit professionals
- ◆ Recent demonstrated access to all capital markets

## Diversified Portfolio

- ◆ First lien / second lien / mezzanine and equity
- ◆ CLO Fund investments and management of these securities through Asset Manager Affiliates – Creating synergies and stable cash flows
- ◆ Both businesses primarily invest in floating rate securities - well positioned for rising rates

## Low Leverage

- ◆ \$195.6 million in borrowings as of September 30, 2013
- ◆ Asset coverage is 238%, above the minimum 200% (1:1) required for a BDC

## Alignment of Interests

- ◆ No external management fees
- ◆ Board members and management own in excess of 14% of shares

# OVERVIEW – BUSINESS MODEL

*Internally managed BDC with a diversified portfolio of corporate credit investments  
and an attractive asset management business*



## Principal Investing

### Corporate Loan Investments

- ◆ \$257 million in debt securities
- ◆ Average unlevered yield  $\approx$  6.8%
- ◆ Focus on secured investments (78.8%)

### CLO Fund Investments

- ◆ \$64 million investments in CLO Equity
- ◆ Average yield of  $\approx$  26% on fair value

## Managed Funds

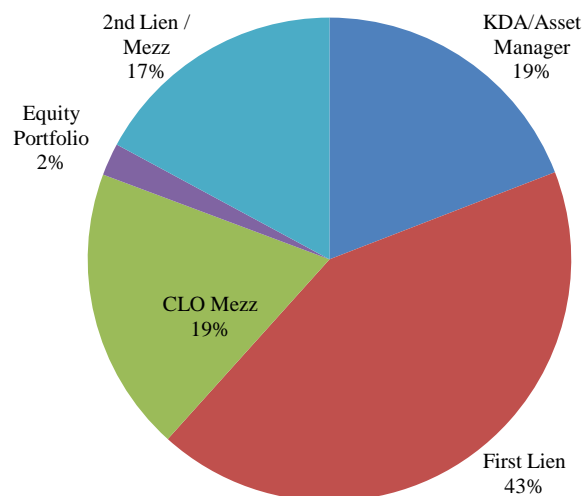
### Asset Managers Affiliates (AMA)

- ◆ Asset management business
- ◆ \$3.4 billion in AUM
- ◆ \$83 million fair value
- ◆ Current quarterly cash flow run rate: \$3M
- ◆ Distributions contribute to KCAP's net investment income

# INVESTMENT PORTFOLIO

*A balanced investment risk / return profile*

3Q13



<u>Investment</u>	<u>Yield</u>
First lien <sup>1</sup>	5.4%
Second lien / Mezz <sup>1</sup>	10.4%
CLO Securities <sup>1</sup>	26.3%
Asset Manager Affiliates <sup>1</sup>	17.1%
Equity Portfolio	--
<b>Approx. Weighted Average Yield on FV</b>	<b>12.3%</b>

<sup>1</sup> Yield based on Fair Value (FV)

## Portfolio Statistics

### Total Portfolio:

Fair value \$431 million

### Loan and Securities Portfolio:

Fair value \$257 million

Number of issuers 79

Average deal/issuer size \$3.3 million

In default <1%

Fixed rate 9%

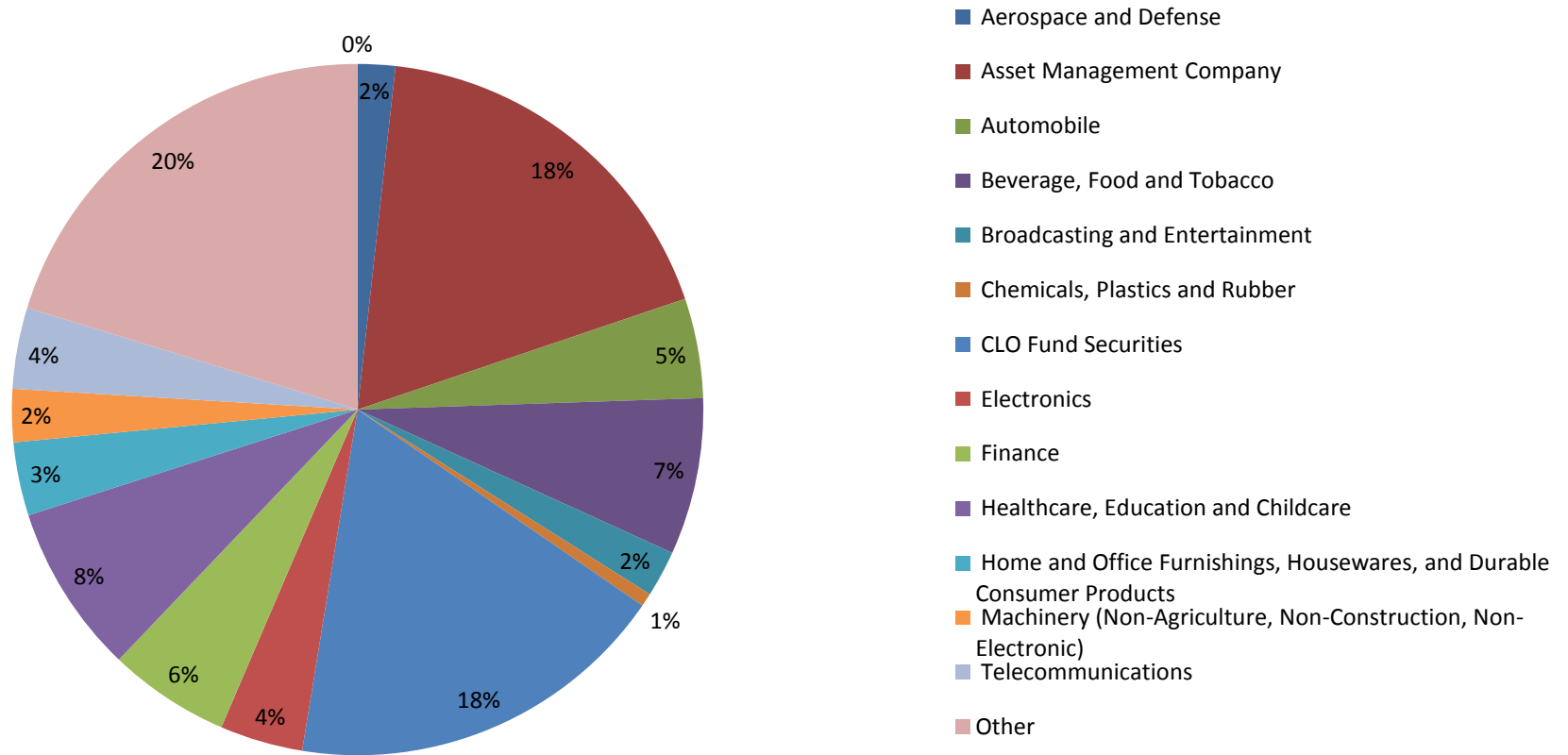
Floating rate 88%

Equity (neither fixed/floating) 3%

Note: Percentages to total fair value excluding AMA & CLO Securities

# PORTFOLIO HIGHLIGHTS

## PORTFOLIO DEBT SECURITIES – INDUSTRY DIVERSIFICATION



# STRONG CREDIT QUALITY

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*Experienced management team has led to strong credit performance in a challenging environment*

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- ◆ In a portfolio of 79 loans, only four were on non-accrual status (representing less than 1% of total investments at fair value)
- ◆ Portfolio assets continue to amortize or pay-off at par, in spite of mark-to-market unrealized losses
- ◆ 79% of the debt securities portfolio is secured

## *Understanding risks and return*

### Typical CLO Fund Structure

Remaining financing term	9.4 years
Current portfolio yield	L + 384 bps
W/A cost of debt capital	<u>L + 92 bps</u>
Net interest spread	<u>292 bps</u>
Fees and expenses	<u>55 bps</u>
Net spread to equity	<u>237 bps</u>

#### Current Actual CLO Portfolio Performance:

-on current carrying value 26%

### AMA Managed CLO Fund Statistics

Fair value	\$77 million
AUM	\$3.4 billion
Number of CLOs	11
Average number of issuers	112
Average number of industries	25
Average position size	\$2.2 million



## *Typical Deal*

<u>KCAP</u>	
Equity Investment	\$9.4 million
Rate	14%
Annual	\$1.4 million

<u>Asset Manager Affiliate</u>	
AUM	\$3.4 billion
Net Fee	40 Bps
Annual	\$1.6 million

<u>Combined Return</u>	
Return	30%
Investment	\$10 million
Annual	\$3 million

- ◆ Debt-to-equity of 0.73x based on net asset value of \$265 million for the quarter ended September 30, 2013
- ◆ Asset coverage at 238% at September 30, 2013; BDC structure requires minimum asset coverage of 200%
- ◆ \$105.3 million in debt secured financing at approximately L+ 225
- ◆ \$41.4 million in unsecured notes at 7.375% with a 2019 maturity
- ◆ \$49 million in unsecured convertible notes at 8.75% with a 2016 maturity
- ◆ As of October 4, 2013 (post 3<sup>rd</sup> quarter dividend), convertible notes conversion price was \$7.92
- ◆ Blended Cost of Debt Capital was 5.12%

*Well positioned for a rising rate environment*

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- ◆ A majority of KCAP's investments are in floating rate assets
- ◆ Almost all the assets in the CLOs managed by our Asset Manager Affiliates are floating rate syndicated loans
- ◆ KCAP has a mix of fixed and floating rate securities which will be beneficial in a rising rate environment
- ◆ A 100 basis point increase in interest rates would increase NII by \$652,000 annually

# SUMMARY OF KCAP ATTRIBUTES

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*Dynamic business model generates sustainable dividends*

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- ✓ Sustainable, recurring revenues not dependent on capital gains
    - ◆ Recurring interest income from secured loan and CLO portfolios
    - ◆ Stable asset management fee income from Asset Manager Affiliates
  - ✓ New investments in current market environment provide higher returns and enhance portfolio yield
  - ✓ Not reliant on high leverage to generate returns
  - ✓ Floating rate assets, many with minimum index rate floors, provide NAV protection and increased earnings in a rising rate environment
  - ✓ Experienced credit managers with long track records
  - ✓ Interest aligned with shareholders – significant insider ownership and internally managed
  - ✓ KCAP has demonstrated its recent success accessing a variety of funding markets: equity, debt, loan securitizations and new CLO funds
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# SUBSEQUENT EVENTS

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- The Company has evaluated events and transactions occurring subsequent to the Balance Sheet date of September 30, 2013 for items that should potentially be recognized or disclosed in these financial statements. The Company did not identify any items which would require disclosure in or adjustment to the financial statements.

# FINANCIAL HIGHLIGHTS

	3Q13		2Q13		1Q13		4Q12		3Q12		2Q12	
Net investment income per share <sup>1</sup>	\$	0.23	\$	0.20	\$	0.24	\$	0.28	\$	0.27	\$	0.23
Net realized and unrealized gain (loss) per share <sup>1</sup>	\$	0.09	\$	0.11	\$	0.01	\$	0.28	\$	0.23	\$	(0.16)
Net asset value per share <sup>2</sup>	\$	7.96	\$	8.24	\$	8.33	\$	7.85	\$	7.82	\$	7.66
Dividend distribution per share <sup>2</sup>	\$	0.25	\$	0.28	\$	0.28	\$	0.28	\$	0.24	\$	0.24
Share Price												
High	\$	9.06	\$	11.26	\$	10.89	\$	9.67	\$	9.36	\$	7.47
Low	\$	8.81	\$	9.72	\$	9.41	\$	7.40	\$	7.27	\$	5.51
Close	\$	8.97	\$	11.26	\$	10.77	\$	9.19	\$	9.26	\$	7.26

<sup>1</sup> Based on average number of common shares outstanding for the period.

<sup>2</sup> Based on number of shares issued and outstanding at end of period.

# FINANCIAL HIGHLIGHTS

## NET ASSET VALUE

September 30, 2013	Fair Value	NAV per Share
<i>Investments at fair value:</i>		
Investments in time deposits	\$ —	\$ -
Investments in money market accounts	9,055,634	0.27
Investments in debt securities	257,359,908	7.73
Investments in CLO Fund securities	82,152,488	2.47
Investments in equity securities	9,385,053	0.28
Investments in Asset Manager Affiliates	<u>82,533,000</u>	<u>2.48</u>
Total Investments	440,486,083	13.23
Cash	9,721,704	0.29
Other assets	<u>17,805,135</u>	<u>0.53</u>
Total Assets	\$ <u>468,012,922</u>	\$ <u>14.05</u>
Borrowings	\$ 192,518,220	\$ 5.78
Other Liabilities	<u>10,411,973</u>	<u>0.31</u>
Total Liabilities	\$ <u>202,930,193</u>	\$ <u>6.09</u>
<b>NET ASSET VALUE</b>	\$ <u><b>265,082,729</b></u>	\$ <u><b>7.96</b></u>

## INVESTMENT PORTFOLIO

September 30, 2013	Cost	Fair Value
Time Deposits	\$ -	\$ -
Money Market Account	9,055,634	9,055,634
Senior Secured Loan	186,686,207	179,395,497
Junior Secured Loan	44,327,364	41,309,810
Senior Unsecured Loan	20,000,000	20,000,000
First Lien Bond	2,939,165	2,556,300
Senior Subordinated Bond	1,037,667	1,061,901
Senior Secured Bond	1,519,751	1,537,500
Senior Unsecured Bond	10,830,904	11,338,900
CLO Fund Securities	101,346,359	82,152,488
Equity Securities	18,655,209	9,385,053
Preferred Stock	400,000	160,000
Asset Manager Affiliates	<u>83,273,236</u>	<u>82,533,000</u>
<b>Total Assets</b>	\$ <u><b>480,071,496</b></u>	\$ <u><b>440,486,083</b></u>

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# Q & A

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