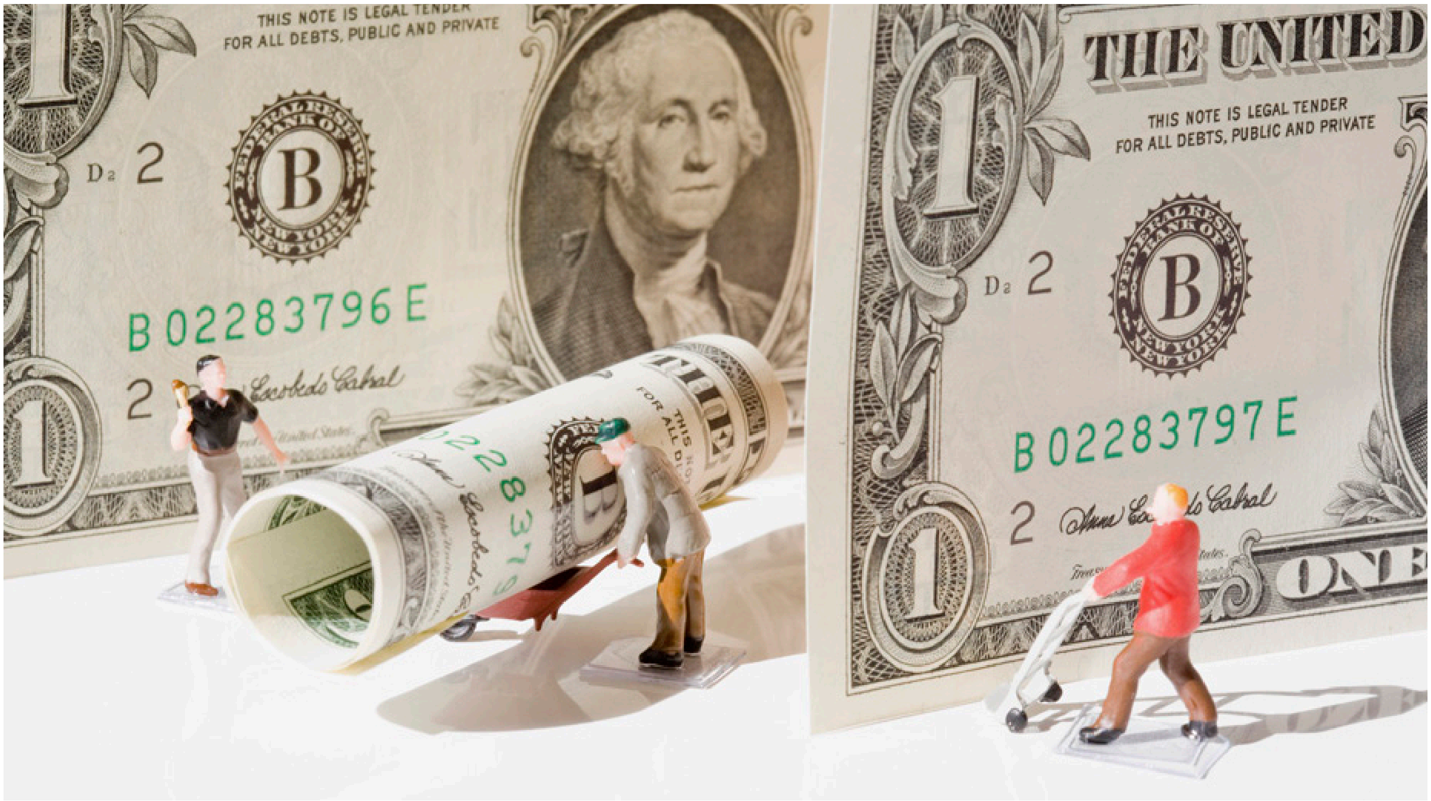

Prospect Capital Corporation Beats Expectations

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The value of Prospect Capital Corporation has been beaten down on negative sentiment and fear while results prove the BDC's ongoing success.

Fear And Loathing Drives PSEC Shares To New Low

I like to refer to Prospect Capital Corporation as the most hated stock in the market and recent activity only proves my point. Fears of a miss-mark of CLO valuation is the most recent cause of the ongoing decline in share value but like all fears is largely unfounded. The rumor is that there is an ongoing probe by the SEC into action by the company, a rumor that is as yet unsubstantiated. As of a December 2015 8-K filing a probe began in 2014 has been closed with no action taken, since then no other investigations have been disclosed by either PSEC or the SEC.

Johnathon Bock, an analyst with Wells Fargo, has reiterated an underperform rating on the stock, citing an alleged conspiracy between the company(PSEC) and its third party valuation firm to over-inflate marks used to value the CLO portion of the portfolio. While a concern, we need to remember that Prospect Capital has long been a leader in the BDC field and set the standard by which others in the class are valued.

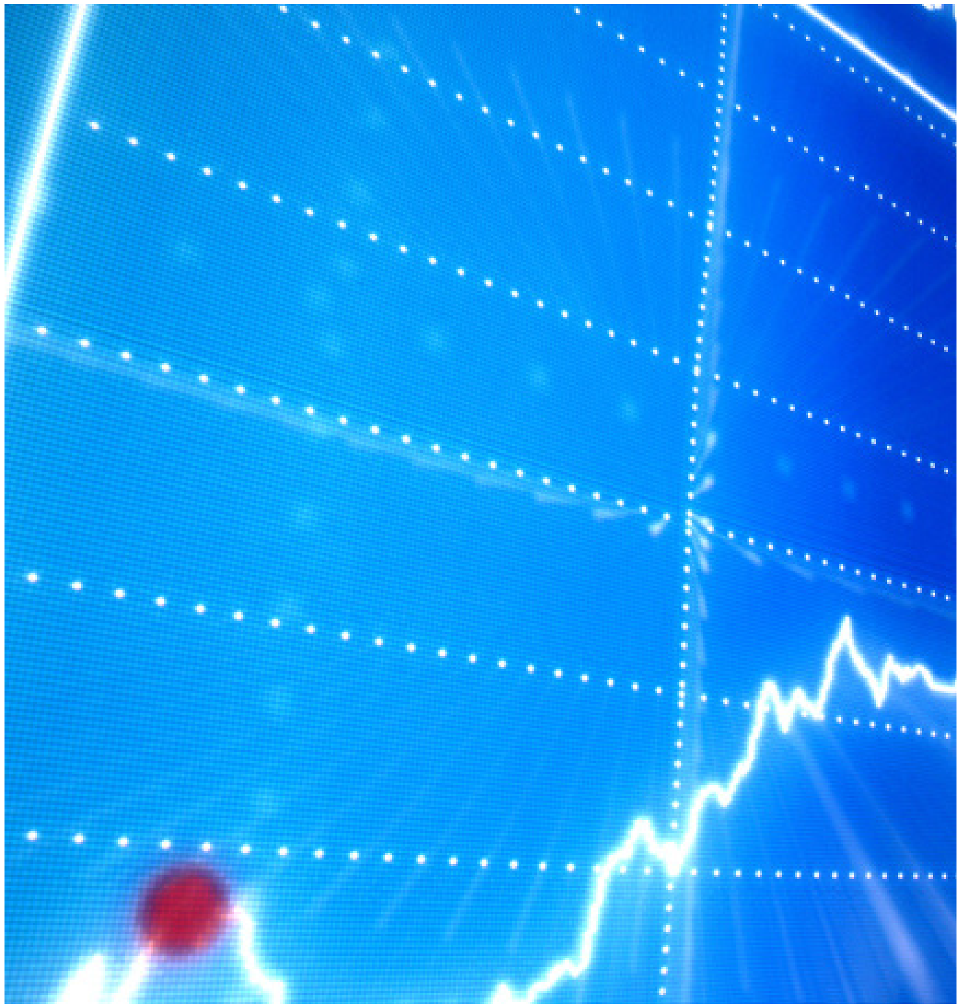
From the PSEC fiscal 2nd quarter earnings statement: "When determining the fair value of portfolio investments, the Audit Committee and the Board of Directors of the company, including our independent directors, consider not just recommendations from management but also a range of valuations from three independent valuation firms. The Board of Directors looks at several factors in determining where within the range to value each asset, including recent operating and financial trends for the asset, independent ratings obtained from third parties, comparable multiples for recent sales of companies within the industry, and discounted cash flow models. Final selected valuations have never been outside the range provided by third party valuation firms."

I have no doubt fears raised by Mr. Bock will persist, I also have no doubt that PSEC will continue to outperform its peers. At current share prices to say the stock is undervalued is an understatement; the stock is deeply undervalued with growing income, stable dividend payments and one of the highest yields in the market, close to 20% at current share prices. Once these fears alleviate shave value of PSEC stands to make a substantial comeback.

Fiscal Year 2016 2nd Quarter Earnings

Regardless of the fears, despite the naysayers, Prospect Capital Corporation produces results. In their most recent earnings report, released 2/9/2016, for the fiscal 2nd quarter of 2016 (calendar Q4 2015) the company beat expectations for net investment income. NII was reported as $0.28 per share, up 2 cents from the previous quarter, 3 cents better than expected and up from the comparable quarter in the previous year. Total investment income rose 5.2% on a year over year basis and, most importantly, more than covers dividend distributions in the period.

Net asset value declined in the period, down to $9.65 from the previously reported $10.17, due primarily to unrealized depreciation and volatility in the capital markets. According to the report roughly 74% of the decline is due to macro changes in the economy followed by an 18% decline attributed to energy and energy related companies and 8% to non-energy related issues. The decline contributed to a small increase in the debt to equity ratio,



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+1.9% from last report, but the ratio remains well within the margin required to maintain investment grade credit ratings with a stable forward outlook. Total leverage decreased to 4.19X from 4.36X.

PSEC 2nd Quarter Earnings Statement "We are pleased with the overall credit quality of our portfolio, with many of our companies generating [Y/Y and Q/Q] growth in top-line revenues and bottom-line profits ... The majority of our portfolio consists of sole agented middle-market loans that we have originated, selected, negotiated, structured, and closed."

Within the portfolio the mix of assets remains strong. Nearly 52% are 1st lien notes, 18.8% 2nd lien, 17.5% structured credit and 10.2% equity holdings. The annualized yield rose by 30 basis points and is evidence of the ongoing efforts of management to improve the balance sheet. Looking back over the past year annualized yield has risen 0.6%

in the last 6 months and 1% over the past 12 months. The real fear for high dividend payers at this time is exposure to the oil patch. Many of those companies are cutting or suspending dividends raising the specter of cuts in those businesses which rely on them for income. PSEC does not rely on energy companies for income, their portfolio exposure is roughly 3% of portfolio.

PSEC 2nd Quarter Earnings Statement "We are currently pursuing initiatives to lower our funding costs (including refinancing of existing liabilities at lower rates), opportunistically harvest certain controlled investments at a gain, optimize our origination strategy mix (including increasing our mix of online loans), repurchase shares at a discount to net asset value, and rotate our portfolio out of lower yielding assets into higher yielding assets while maintaining a significant focus on first lien senior secured lending."

Undervalued With Great Yield

Even with the decline in NAV reported this quarter the stock remains undervalued. Current discount to NAV remains near a historic low, near 40%, and well below the historic average which is close to 15%. This valuation provides a very attractive entry, and is backed up by an impressive dividend yield. At current share prices yield is close to 20% and safe compared to other issues with similarly high yield. Based on the historical perspective, the last time PSEC was selling at such at low valuation it returned in excess of 100% over the next 12 months.

> "At the very least it is highly unlikely the company will cut the dividend as so many other businesses have been doing of late"

As a BDC the company is required by law to distribute at least 90% of taxable income. Spillback dividends are allowed, but to date have not been needed to cover distributions. In fact, based on this quarters NII and taxable income, compounded with previous earnings, distributions are well below income and provide an increasing possibility for special dividends or an increased distribution in the not to distant future.

At the very least it is highly unlikely the company will cut the dividend as so many other businesses have been doing of late. Payments for the next 3 months have already been declared, in line with previous and equal to $1.00 per share annually. To put this into further perspective the company has earned more than half of this years distributions in the first half of the year alone, if they continue to perform as expected full year earnings will come in at the top end of the expected range near $1.10 per share leaving a full $0.10 per share available for additional distribution. No reason to expect a divided cut.

My Final Thoughts

Fears have driven share prices down to a historical low while at the same time company operations have been improving. Even if the CLO portion of the portfolio is devalued the dividend and its health remain, and the stock price has already taken that devaluation into account. Discount to NAV plus distributions, dividend health and forward outlook make this one interesting investment for dividend seekers, long and short term investors.

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