



FSK Lends Itself to Attractive Returns

Price \$22.86

Dividend Holding

October 15, 2021

- High 10.5% dividend yield.
- Compelling valuation, large institutional backing.
- 64% of investment portfolio is senior secured debt, with an average yield of 8.6%.
- >95% of investments are lead or co-lead lender, across 152 companies.

Investment Thesis

FS KKR Capital (FSK) is a business development company specializing primarily in private US middle-market companies' secured, first or second lien debt.

FS KKR was formed on a joint venture of FS investments, and KKR, two large asset managers and investment advisors. Their business development companies (BDCs), were merged to create one of the largest BDCs in the US, with nearly \$15 billion in assets under management, with an average yield of 8.6%.

With its compelling valuation, coupled with its dividend yield, we believe that FSK is an excellent choice to capitalize on the post-COVID-19 business boom.

Strategy

In addition to senior and secured loans, the market for lending to "middle-market" private companies in the United States is underserved by non-traditional bank financing. Middle market companies have revenues between \$5 million and \$1 billion per year and make up a large target market, representing a historically significant portion of US economic growth. Accordingly, FSK focuses on the "upper middle" market, firms with revenues between \$50 million and \$100 million.

Despite the size of the market, many banks are unwilling to underwrite loans of the size that these firms often require. This leaves limited investment competition for non-bank financial firms, as many are equally unwilling to partake in the due diligence required to lend to a smaller firm or unsuited to "micro-manage" a portfolio of such loans. What sets FSK apart is its ability to use 2-4 investment professional teams to screen, conduct due diligence,










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and decide on lending to firms. In addition, a team of credit analysts conducts ongoing assessments of the firms in the investment portfolio.

The typical investment for FSK is \$300-350 million in the capital, with a floating rate base interest rate that is currently around 1%, with spreads of 6%-9% over the floating rate. The firms FSK invests in have an average of \$100 million EBITDA for first-lien loans (meaning, FSK gets priority to collateral) and \$270 million EBITDA for second-lien loans.

Competitive Dynamics

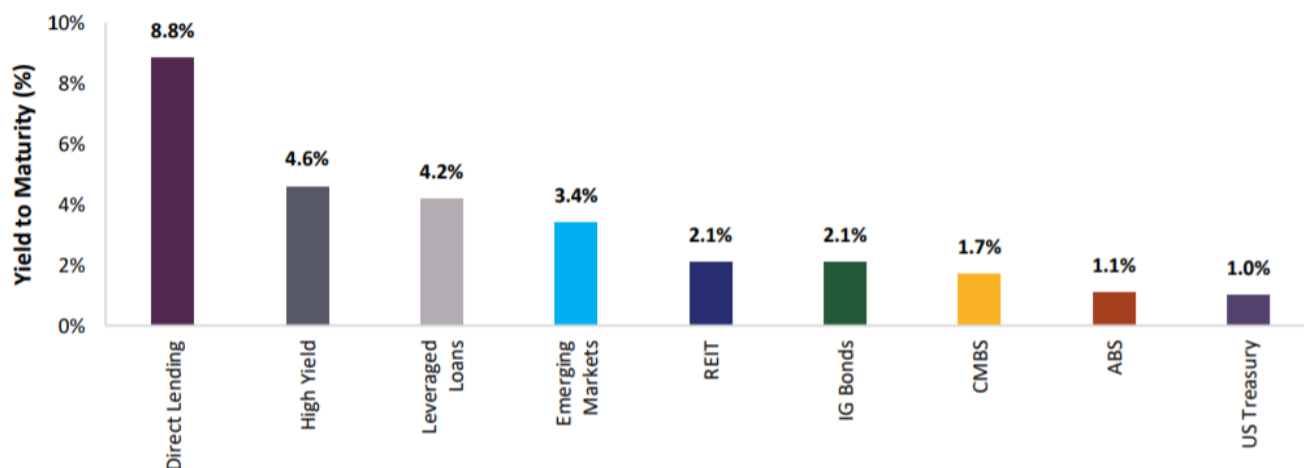
Market Participants

Lower MM	Middle MM	Upper MM	BSL Market
\$3–25mm EBITDA	\$25–50mm EBITDA	\$50–100mm+ EBITDA	\$100mm+ EBITDA
<ul style="list-style-type: none">Limited balance sheetsSingle scope product offeringsExtreme competition	<ul style="list-style-type: none">Highly structured financings with specific covenantsAbility to finance across the capital structureLess competition given size and scale required	<ul style="list-style-type: none">Commoditized financing structures and product offeringsTradable, liquid credit	
<ul style="list-style-type: none">Hundreds of community banks and “local” banks40-45 smaller BDCsNumerous small, private funds <div><div>BARINGS</div><div> BRIGHTWOOD</div><div> MADISON CAPITAL FUNDING</div><div>MAINST CAPITAL CORPORATION</div><div> Monroe Capital <i>Innovative Capital Creating Value</i></div><div>TCP CAPITAL CORP.  <i>An Angelo, Jordan Company</i></div></div>	<ul style="list-style-type: none">Limited number of large BDCsNon-BDC market participants on an ad hoc basis <div><div> ARES</div><div>FS KKR</div><div>GOLUB CAPITAL</div><div>Blackstone</div><div>OWL ROCK CAPITAL CORPORATION</div><div>HPS</div></div>	<ul style="list-style-type: none">Bulge bracket banksCLO fundsLoan mutual fundsInsurance companies <div>Morgan Stanley</div> <div>BANK OF AMERICA</div> <div> Prudential</div> <div> citi</div> <div>Goldman Sachs</div> <div>WELLS FARGO</div>	

Direct Lending

Direct lending to middle-market firms tends to be an attractive source of income in relation to other fixed-income options. For example, FSK has an average yield to maturity of 8.8% on direct loans, compared to 4.6% on high yield bonds, 2.1% on REITs, and only 1% on Treasuries.

Direct Lending continues to be an attractive source of income versus Fixed Income



Across the entire direct lending portfolio of all originations, KKR Credit maintains a relatively low annualized loss rate of 0.36% across \$40 billion in deployed assets. FSK additionally offers conditional restructuring, with requirements including increased reporting, performance targets, replacing management and board, and equitizing the business.

Asset-Based Finance

Asset-based finance implements a multi-strategy and multi-asset approach to diversify the holdings to ensure appropriate risk-adjusted returns. The estimated total addressable market for asset-based finance is over \$4.5 trillion and growing. Asset-based finance is a relatively safer method of income. All issuances are backed by assets that produce cash flows, therefore offering some protection from losing the principal value of the debt.

Risk

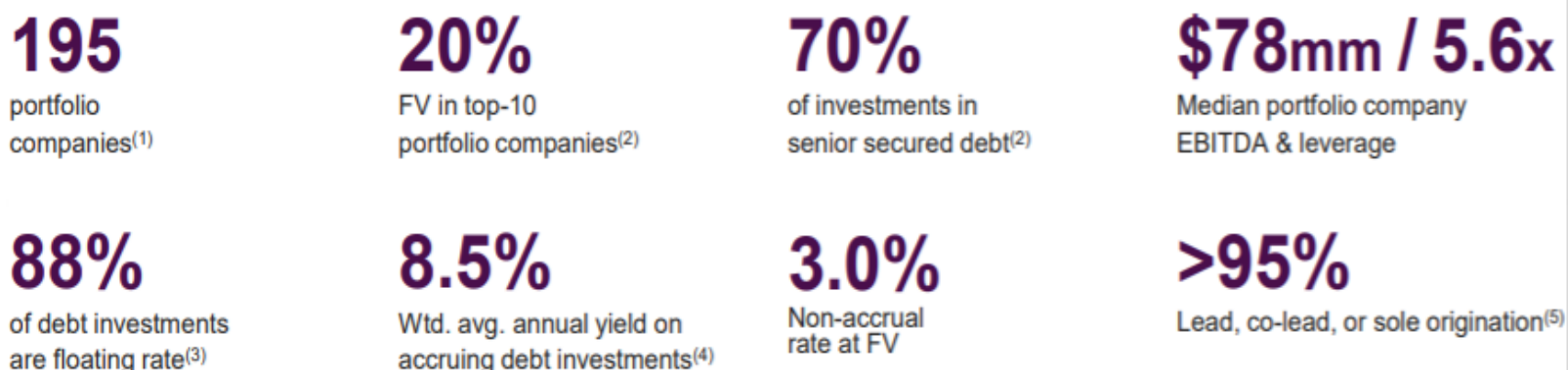
FSK does its best to mitigate risk through diversification, collateral, and due diligence. However, as with any financial firm, unforeseen economic or market movements could adversely affect the portfolio of FSK.



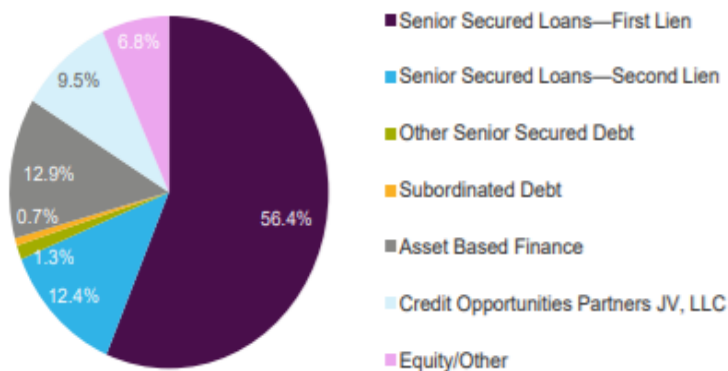
COVID-19 was detrimental to many businesses in the sector that FSK operates in. While FSK was able to weather the storm well, should the economic downturn experienced be longer in the future, it could inflict significant damage on the holdings of FSK.

Metrics

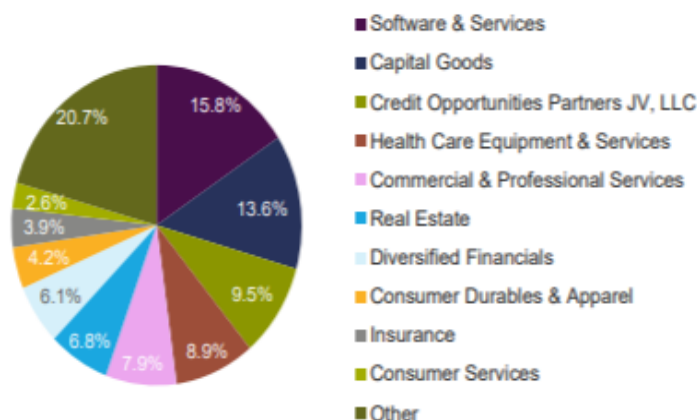
FSK maintains a high diversity portfolio, with its top 10 investments making up only around 20% of its net asset value.



Security Exposure (by fair value)



Sector Exposure (by fair value)



Note: All stats as of June 30, 2021 unless otherwise noted.

1. Does not look through to FSK's portfolio companies held solely in COPJV.

2. Figure excludes the impact of FSK's investment in COPJV.

3. See FSK's Quarterly Report on Form 10-Q for its definition of debt investments.

4. Excludes the impact of the Merger. See FSK's Quarterly Report on Form 10-Q for additional information on the calculation of weighted average annual yield on accruing debt investments. On a GAAP basis, FSK's weighted average annual yield on accruing debt investments was 9.9% as of June 30, 2021.

5. Figure based on count of Direct Origination investments only. KKR & BDC accounts' participation, KKR Capital Markets' involvement, and deal teams leading the negotiations / structuring are all considered when determining the Origination Role.

Total Investments at Fair Value: \$14,734mm

Investment income saw a bump of 35% year over year, with the net increase in assets resulting from operations hitting \$865 million in Q2 compared to Q1.



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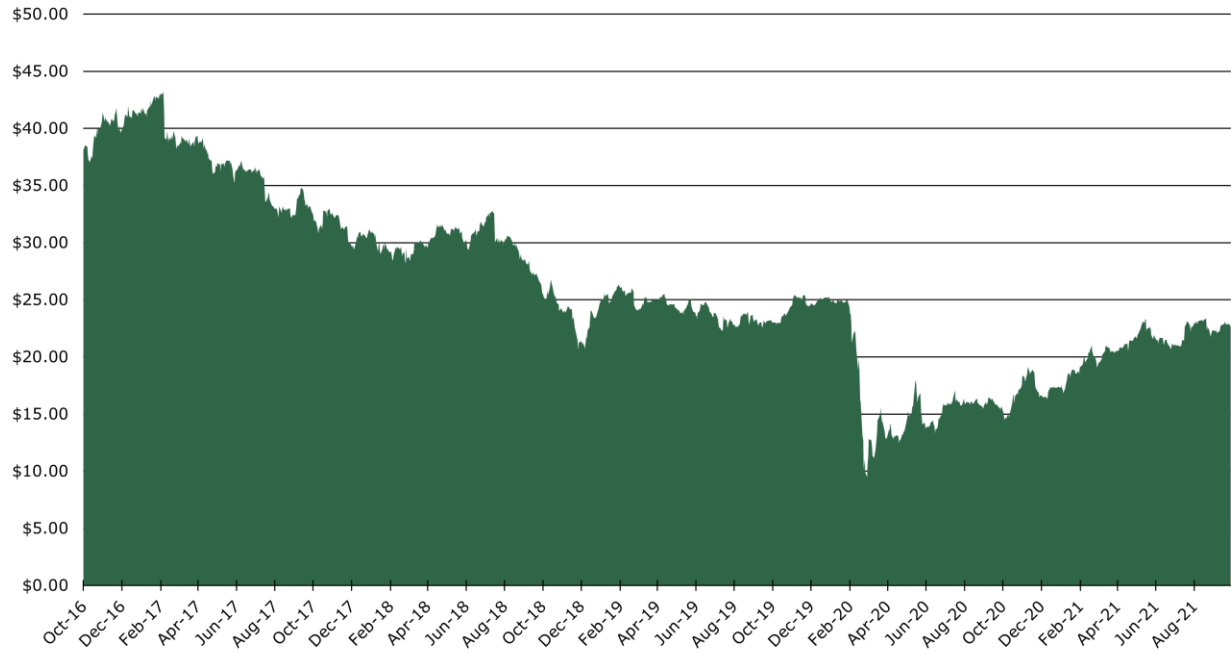
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FSK pays a quarterly dividend of .6-.65 per share, maintaining a dividend coverage ratio (amount of times FSK could pay its dividend obligations) of 123%.

FS KKR Capital (FSK)	FY2021	E2022	E2023
Price-to-Sales	6.4	4.7	4.7
Price-to-Earnings	8.9	8.8	8.8
EV/Sales	13.4	10.0	10.0

Estimated Next 12 Months	Dividend Yield	Price-to-Book	Price-to-Earnings
FS KKR Capital (FSK)	10.5%	0.85	8.99
Apollo Investment (AINV)	10.5%	0.83	9.56
Sixth Street Specialty Lending (TSLX)	8.9%	1.34	11.34
Owl Rock Capital (ORCC)	8.8%	0.96	11.12
Hercules Capital (HTGC)	8.6%	1.49	12.45
SLR Investment (SLRC)	8.4%	0.96	12.10
Ares Capital (ARCC)	7.8%	1.16	11.60

FS KKR (FSK)



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