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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549  
**FORM 10-Q**

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **June 30, 2014**

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **814-61**

**CAPITAL SOUTHWEST CORPORATION**

(Exact name of registrant as specified in its charter)

**Texas**

(State or other jurisdiction of incorporation or organization)

**75-1072796**

(I.R.S. Employer Identification No.)

**12900 Preston Road, Suite 700, Dallas, Texas**

(Address of principal executive offices)

**75230**

(Zip Code)

**Registrant's telephone number, including area code: (972) 233-8242**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such filings). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

15,413,532 shares of Common Stock, \$0.25 value, as of August 5, 2014

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## PART I – FINANCIAL INFORMATION

## Item 1. Consolidated Financial Statements

## CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES

(In thousands, except per share data)

	June 30, 2014	March 31, 2014
	(Unaudited)	
<b>Assets</b>		
Investments at market or fair value		
Companies more than 25% owned (Cost: June 30, 2014 - \$12,396, March 31, 2014 - \$13,711)	\$ 422,153	\$ 400,824
Companies 5% to 25% owned (Cost: June 30, 2014 - \$13,891, March 31, 2014 - \$13,891)	218,707	218,480
Companies less than 5% owned (Cost: June 30, 2014 - \$53,840, March 31, 2014 - \$71,365)	55,138	58,616
Total investments (Cost: June 30, 2014 - \$80,127, March 31, 2014 - \$98,967)	695,998	677,920
Cash and cash equivalents	88,150	88,163
Receivables		
Dividends and interest	217	782
Affiliates	392	422
Income tax receivable	534	167
Pension assets	11,036	10,962
Other assets	217	278
Total assets	<u>\$ 796,544</u>	<u>\$ 778,694</u>
<b>Liabilities</b>		
Other liabilities	\$ 2,429	\$ 3,263
Accrued restoration plan liability	3,221	3,103
Deferred income taxes	2,210	1,940
Total liabilities	<u>7,860</u>	<u>8,306</u>
<b>Net Assets</b>		
Common stock, \$0.25 value: authorized, 25,000,000 shares; issued, 17,753,044 shares at June 30, 2014 and March 31, 2014	4,438	4,438
Additional capital	195,882	195,767
Accumulated net investment (loss) gain	(1,886)	1,138
Accumulated net realized (loss) gain	(1,684)	14,029
Unrealized appreciation of investments	615,871	578,953
Treasury stock - at cost on 2,339,512 shares	(23,937)	(23,937)
Total net assets	<u>788,684</u>	<u>770,388</u>
Total liabilities and net assets	<u>\$ 796,544</u>	<u>\$ 778,694</u>
Net asset value per share (15,413,532 shares outstanding at June 30, 2014 and March 31, 2014)	<u>\$ 51.17</u>	<u>\$ 49.98</u>

The accompanying Notes are an integral part of these Consolidated Financial Statements

## CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)  
(In thousands)

	Three Months Ended June 30,	
	2014	2013
Investment income:		
Interest	\$ 140	\$ 330
Dividends	500	545
Management fees and other income	140	180
	<u>780</u>	<u>1,055</u>
Operating expenses:		
Salaries	1,302	1,469
Stock option expense	116	174
Net pension expense (benefit)	44	(9)
Professional fees	390	225
Other operating expenses	478	446
	<u>2,330</u>	<u>2,305</u>
Loss before income taxes	(1,550)	(1,250)
Income tax benefit	(67)	(48)
	<u>(1,617)</u>	<u>(1,298)</u>
<b>Net investment loss</b>	<b>\$ (1,483)</b>	<b>\$ (1,202)</b>
Proceeds from disposition of investments	3,203	55
Cost of investments sold	(18,916)	-
<b>Net realized (loss) gain on investments</b>	<b>(15,713)</b>	<b>55</b>
<b>Net increase in unrealized appreciation of investments</b>	<b>36,917</b>	<b>10,392</b>
<b>Net realized and unrealized gain on investments</b>	<b>\$ 21,204</b>	<b>\$ 10,447</b>
<b>Increase in net assets from operations</b>	<b>\$ 19,721</b>	<b>\$ 9,245</b>

The accompanying Notes are an integral part of these Consolidated Financial Statements.

## CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

(Unaudited)

(In thousands)

	Three Months Ended June 30	
	2014	2013
Operations:		
Net investment loss	\$ (1,483)	\$ (1,202)
Net realized (loss) gain on investments	(15,713)	55
Net increase in unrealized appreciation of investments	36,917	10,392
Increase in net assets from operations	19,721	9,245
Distributions from:		
Undistributed net investment income	(1,541)	(1,524)
Undistributed net realized gain	-	-
Capital share transactions:		
Exercise of employee stock options	-	459
Stock option expense	116	174
Increase in net assets	18,296	8,354
Net assets, beginning of period	770,388	659,777
<b>Net assets, end of period</b>	<b>\$ 788,684</b>	<b>\$ 668,131</b>

The accompanying Notes are an integral part of these Consolidated Financial Statements.

## CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(In thousands)

	Three Months Ended June 30,	
	2014	2013
<b>Cash flows from operating activities</b>		
Increase in net assets from operations	\$ 19,721	\$ 9,245
Adjustments to reconcile increase in net assets from operations to net cash provided by (used in) operating activities:		
Net proceeds from disposition of investments	3,127	55
Return of capital on investments	76	-
Purchases of securities	(76)	(8,842)
Depreciation and amortization	2	6
Net pension benefit	44	(9)
Realized loss (gain) on investments before income tax	15,713	(55)
Net increase in unrealized appreciation of investments	(36,917)	(10,392)
Stock option expense	116	174
Decrease (increase) in dividend and interest receivable	565	(41)
Decrease in receivables from affiliates	30	201
Increase in income tax receivable	(367)	-
Decrease in other assets	58	32
Decrease in other liabilities	(834)	(916)
Increase in deferred income taxes	270	3
Net cash provided by (used in) operating activities	<u>1,528</u>	<u>(10,539)</u>
<b>Cash flows from financing activities</b>		
Distributions from undistributed net investment income	(1,541)	(1,524)
Proceeds from exercise of employee stock options	-	459
Net cash used in financing activities	<u>(1,541)</u>	<u>(1,065)</u>
Net decrease in cash and cash equivalents	(13)	(11,604)
Cash and cash equivalents at beginning of period	88,163	81,767
Cash and cash equivalents at end of period	<u>\$ 88,150</u>	<u>\$ 70,163</u>

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**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SCHEDULE OF INVESTMENTS**

**(Unaudited)**

June 30, 2014

<b>Company</b>	<b>Equity (a)</b>	<b>Investment (b)</b>	<b>Cost</b>	<b>Value (c)</b>
<b>*†ALAMO GROUP INC.</b> <b>Seguin, Texas</b> Tractor-mounted mowing and mobile excavation equipment for governmental, industrial and agricultural markets; street-sweeping equipment for municipalities.	22.0%	‡2,831,976 shares of common stock (acquired 4-1-73 thru 5-09-14)	\$ 2,190,937	\$ 153,181,582
<b>ATLANTIC CAPITAL BANCSHARES, INC</b> <b>Atlanta, Georgia</b> Holding company of Atlantic Capital Bank, a full service commercial bank.	1.9%	300,000 shares of common stock (acquired 4-10-07)	3,000,000	3,964,000
<b>¥BALCO, INC.</b> <b>Wichita, Kansas</b> Specialty architectural products used in the construction and remodeling of commercial and institutional buildings.	95.7%	445,000 shares of common stock and 60,920 shares Class B non-voting common stock (acquired 10-25-83 and 5-30-02)	624,920	5,100,000
<b>*BOXX TECHNOLOGIES, INC.</b> <b>Austin, Texas</b> Workstations for computer graphic imaging and design.	14.9%	3,125,354 shares of Series B Convertible Preferred Stock, convertible into 3,125,354 shares of common stock at \$0.50 per share (acquired 8-20-99 thru 8-8-01)	1,500,000	1,240,000
<b>¥CAPSTAR HOLDINGS CORPORATION</b> <b>Dallas, Texas</b> Acquire, hold and manage real estate for potential development and sale.	100%	500 shares of common stock (acquired 6-10-10) and 1,000,000 shares of preferred stock (acquired 12-17-12)	4,703,619	7,340,000
<b>DEEPWATER CORROSION SERVICES, INC.</b> <b>Houston, Texas</b> full-service corrosion control company providing the oil and gas industry with expertise in cathodic protection and asset integrity management.	31.3%	127,004 shares of Series A convertible preferred stock, convertible into 127,004 shares of common stock at \$1.00 per shares (acquired 4-9-13)	8,000,000	9,055,000
<b>*†ENCORE WIRE CORPORATION</b> <b>McKinney, Texas</b> Electric wire and cable for residential, commercial and industrial construction use.	6.2%	‡1,312,500 shares of common stock (acquired 9-10-92 thru 10-15-98)	5,200,000	64,260,000
<b>¡MEMORIES, INC.</b> <b>Scottsdale, Arizona</b> Enables online video and photo sharing and DVD creation for home movies recorded in analog and new digital format.	23.3%	17,391,304 shares of Series B Convertible Preferred Stock, convertible into 19,891,304 shares of common stock at \$0.23 per share (acquired 7-10-09) 4,684,967 shares of Series C Convertible Preferred Stock, convertible into 4,684,967 shares of common stock at \$0.23 per share (acquired 7-20-11) Warrants to purchase 8,396,000 shares of common stock at \$0.01 per share, expiring 9-26-23 (acquired 9-13-10 to 9-26-13) 10% convertible notes, \$308,000 principal due 7-31-14 (acquired 9-7-12) 10% convertible notes, \$400,000 principal due 7-31-14 (acquired 3-15-13)	4,000,000   1,078,479  308,000 880,000	–   –  153,000 438,000
			<u>6,266,479</u>	<u>591,000</u>

†Publicly-owned company ¥ Control investment \* Affiliated investment ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SCHEDULE OF INVESTMENTS**

**(Unaudited)**

June 30, 2014

<b>Company</b>	<b>Equity (a)</b>	<b>Investment (b)</b>	<b>Cost</b>	<b>Value (c)</b>
<b>INSTAWARES HOLDING COMPANY, LLC</b> <b>Atlanta, Georgia</b> Provides services to the restaurant industry via its five subsidiary companies.	4.3%	3,846,154 Class D Convertible Preferred Stock (acquired 5-20-11)	5,000,000	1,052,000
<b>KBI BIOPHARMA, INC.</b> <b>Durham, North Carolina</b> Provides fully-integrated, outsourced drug development and bio-manufacturing services.	17.1%	10,204,082 shares of Series B-2 Convertible Preferred Stock, convertible into 10,204,802 shares of common stock at \$0.49 per share (acquired 9-08-09) Warrants to purchase 94,510 shares of Series B preferred stock at \$ 0.70 per share, acquired 1-26-12	5,000,000  -	6,700,000  -
			5,000,000	6,700,000
<b>¥MEDIA RECOVERY, INC.</b> <b>Dallas, Texas</b> Computer datacenter and office automation supplies and accessories; impact, tilt monitoring and temperature sensing devices to detect mishandling shipments; dunnage for protecting shipments.	97.9%	800,000 shares of Series A Convertible Preferred Stock, convertible into 800,000 shares of common stock at \$1.00 per share (acquired 11-4-97) 4,000,002 shares of common stock (acquired 11-4-97)	800,000 4,615,000	4,100,000 20,400,000
			5,415,000	24,500,000
<b>¥THE RECTORSEAL CORPORATION</b> <b>Houston, Texas</b> Specialty chemicals for plumbing, HVAC, electrical, construction, industrial, oil field and automotive applications; smoke containment systems for building fires; also owns 20% of The Whitmore Manufacturing Company.	100.0%	27,907 shares of common stock (acquired 1-5-73 and 3-31-73)	52,600	289,400,000
<b>TITANLINER, INC.</b> <b>Midland, Texas</b> Manufactures, installs and rents spill containment system for oilfield applications.	31.2%	217,038 shares of Series A Convertible Preferred Stock convertible into 217,038 shares of Series A Preferred Stock at \$14.76 per share (acquired 6-29-12) 7% senior subordinated secured promissory note, due 6-30-17 (acquired 6-29-12) Warrants to purchase 122,239 shares of Series A Preferred Stock at \$ 0.01 per share, expiring 12-31-22	3,203,000 2,747,000 -	- 2,014,000 -
			5,950,000	2,014,000
<b>TRAX HOLDINGS, INC.</b> <b>Scottsdale, Arizona</b> Provides a comprehensive set of solutions to improve the transportation validation, accounting, payment and information management process.	28.4%	475,430 shares of Series B convertible Preferred Stock convertible into 475,430 shares of common stock at \$8.41 per share(acquired 12-5-12)  1,061,279 shares of Series A Convertible Preferred Stock, convertible into 1,061,279 shares of common stock at \$4.71 per share (acquired 12-8-08 and 2-17-09)	4,000,000  5,000,000	7,600,000  12,900,000
			9,000,000	20,500,000

†Publicly-owned company    ¥ Control investment    \* Affiliated investment    ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*



**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**
**CONSOLIDATED SCHEDULE OF INVESTMENTS**
**(Unaudited)**

June 30, 2014

Company	Equity (a)	Investment (b)	Cost	Value (c)
<b>*WELLOGIX, INC.</b>	19.0%	4,788,371 shares of Series A-1	5,000,000	25,000
<b>Houston, Texas</b>		Convertible Participating Preferred		
Developer and supporter of software used by the oil and gas industry.		Stock, convertible into 4,788,371 shares of common stock at \$1.04 per share (acquired 8-19-05 thru 6-15-08)		
<b>¥THE WHITMORE MANUFACTURING COMPANY</b>	80.0%	80 shares of common stock (acquired 8-31-79)	1,600,000	95,600,000
<b>Rockwall, Texas</b>				
Specialized surface mining, railroad and industrial lubricants; coatings for automobiles and primary metals; fluid contamination control devices.				
<b>MISCELLANEOUS</b>	–	Ballast Point Ventures II, L.P. 2.2% limited partnership interest (acquired 8-4-08 thru 2-15-13)	2,334,790	3,167,000
	–	BankCap Partners Fund I, L.P. 5.5% limited partnership interest (acquired 7-14-06 thru 11-16-12)	6,000,000	5,532,000
	–	†Capitala Finance Corporation 108,105 shares of common stock (acquired 9-25-13)	1,363,799	2,042,103
	–	CapitalSouth Partners Fund III, L.P. 1.9% limited partnership interest (acquired 1-22-08 and 11-16-11)	467,457	277,000
	–	Diamond State Ventures, L.P. 1.4% limited partnership interest (acquired 10-12-99 thru 8-26-05)	-	16,000
	–	First Capital Group of Texas III, L.P. 3.0% limited partnership interest (acquired 12-26-00 thru 8-12-05)	778,895	117,000
	100%	¥Humac Company 1,041,000 shares of common stock (acquired 1-31-75 and 12-31-75)	–	213,000
	–	STARTech Seed Fund II 3.2% limited partnership interest (acquired 4-28-00 thru 2-23-05)	678,621	111,000
<b>TOTAL INVESTMENTS</b>			<b>\$ 80,127,117</b>	<b>\$ 695,997,685</b>

†Publicly-owned company    ¥ Control investment    \* Affiliated investment    ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SCHEDULE OF INVESTMENTS**

March 31, 2014

<b>Company</b>	<b>Equity (a)</b>	<b>Investment (b)</b>	<b>Cost</b>	<b>Value (c)</b>
*† <b>ALAMO GROUP INC.</b> <b>Seguin, Texas</b> Tractor-mounted mowing and mobile excavation equipment for governmental, industrial and agricultural markets; street-sweeping and snow removal equipment for municipalities.	22.0%	‡2,831,300 shares of common stock (acquired 4-1-73 thru 5-09-13)	\$ 2,190,937	\$ 153,824,529
<b>ATLANTIC CAPITAL BANCSHARES, INC</b> <b>Atlanta, Georgia</b> Holding company of Atlantic Capital Bank, a full service commercial bank.	1.9%	300,000 shares of common stock (acquired 4-10-07)	3,000,000	3,817,000
¥ <b>BALCO, INC.</b> <b>Wichita, Kansas</b> Specialty architectural products used in the construction and remodeling of commercial and institutional buildings.	95.7%	445,000 shares of common stock and 60,920 shares Class B non-voting common stock (acquired 10-25-83 and 5-30-02)	624,920	4,500,000
* <b>BOXX TECHNOLOGIES, INC.</b> <b>Austin, Texas</b> Workstations for computer graphic imaging and design.	14.9%	3,125,354 shares of Series B Convertible Preferred Stock, convertible into 3,125,354 shares of common stock at \$0.50 per share (acquired 8-20-99 thru 8-8-01)	1,500,000	1,040,000
¥ <b>CAPSTAR HOLDINGS CORPORATION</b> <b>Dallas, Texas</b> Acquires holds and manages real estate for potential development and sale.	100%	500 shares of common stock (acquired 6-10-10) and 1,000,000 shares of preferred stock (acquired 12-17-12)	4,703,619	7,514,000
<b>CINATRA CLEAN TECHNOLOGIES, INC.</b> <b>Houston, Texas</b> Cleans above ground oil storage tanks with a patented, automated system.	76.2%	12% subordinated secured promissory note, due 5-9-16 (acquired 5-19-10 thru 10-20-10)	779,278	1
		12% subordinated secured promissory note, due 5-9-17 (acquired 5-9-11 thru 10-26-11)	2,285,700	1
		12% subordinated secured promissory note, due 3-31-17 (acquired 9-9-11 and 10-26-11)	1,523,800	1
		10% subordinated secured promissory note, due 5-9-17 (acquired 7-14-08 thru 4-28-10)	921,588	1
		12% subordinated secured promissory note, due 10-31-17 (acquired 10-19-12)	499,997	1
		12% subordinated secured promissory note, due 9-30-14 (acquired 7-25-13)	1,157,850	1
		12% subordinated secured promissory note, due 9-30-14 (acquired 2-19-14)	152,394	1
		9,891,578 shares of Series A Convertible Preferred Stock, convertible into 9,891,578 shares of common stock at \$1.00 per share (acquired 7-14-08 thru 3-15-14)	9,891,578	1
		Warrants to purchase 1,436,499 shares of common stock at \$1.00 per share, expiring 10-31-2027 (acquired 5-9-11 thru 10-19-12)	–	–
			<u>17,212,185</u>	<u>8</u>

†Publicly-owned company ¥ Control investment \* Affiliated investment ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SCHEDULE OF INVESTMENTS**

March 31, 2014

<b>Company</b>	<b>Equity (a)</b>	<b>Investment (b)</b>	<b>Cost</b>	<b>Value (c)</b>
<b>DEEPWATER CORROSION SERVICES, INC.</b> <b>Houston, Texas</b> Full-service corrosion control company providing the oil and gas industry with expertise in cathodic protection and asset integrity management.	31.3%	127,004 shares of Series A convertible preferred stock, convertible into 127,004 shares of common stock at \$1.00 per shares (acquired 4-9-13)	8,000,000	8,000,000
<b>DISCOVERY ALLIANCE, LLC</b> <b>Dallas, Texas</b> Provides services related to intellectual property protection and development.	90%	90.0% limited liability company interest (acquired 9-12-08 thru 10-15-12)	1,315,000	400,000
<b>*†ENCORE WIRE CORPORATION</b> <b>McKinney, Texas</b> Electric wire and cable for residential, commercial and industrial construction use.	6.2%	‡1,312,500 shares of common stock (acquired 9-10-92 thru 10-15-98)	5,200,000	63,590,625
<b>MEMORIES, INC.</b> <b>Scottsdale, Arizona</b> Enables online video and photo sharing and DVD creation for home movies and photos recorded in analog and digital formats.	23.3%	17,391,304 shares of Series B Convertible Preferred Stock, convertible into 19,891,304 shares of common stock at \$0.23 per share (acquired 7-10-09) 4,684,967 shares of Series C Convertible Preferred Stock, convertible into 4,684,967 shares of common stock at \$0.23 per share (acquired 7-20-11) Warrants to purchase 8,396,000 shares of common stock at \$0.01 per share, expiring 9-26-23 (acquired 9-13-10 to 9-26-13) 10% convertible notes, \$308,000 principal due 7-31-14 (acquired 9-7-12) 10% convertible notes, \$880,000 principal due 7-31-14 (acquired from 3-15-13 to 9-26-13)	4,000,000 1,078,479 — 308,000 880,000	2 994,000 — 308,000 880,000
<b>INSTAWARES HOLDING COMPANY, LLC</b> <b>Atlanta, Georgia</b> Provides services and distributes equipment and supplies to the restaurant industry via its five subsidiary companies.	4.3%	3,846,154 Class D Convertible Preferred Stock (acquired 5-20-11)	5,000,000	3,354,000
<b>KBI BIOPHARMA, INC.</b> <b>Durham, North Carolina</b> Provides fully-integrated, outsourced drug development and bio-manufacturing services.	17.1%	10,204,082 shares of Series B-2 Convertible Preferred Stock, convertible into 10,204,802 shares of common stock at \$0.49 per share (acquired 9-08-09) Warrants to purchase 94,510 shares of Series B preferred stock at \$ 0.70 per share, acquired 1-26-12	5,000,000 —	7,000,000 —
			<u>6,266,479</u>	<u>2,182,002</u>
			<u>5,000,000</u>	<u>7,000,000</u>

†Publicly-owned company    ¥ Control investment    \* Affiliated investment    ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED SCHEDULE OF INVESTMENTS**

March 31, 2014

<b>Company</b>	<b>Equity (a)</b>	<b>Investment (b)</b>	<b>Cost</b>	<b>Value (c)</b>
<b>¥MEDIA RECOVERY, INC.</b>	97.9%	800,000 shares of Series A Convertible Preferred Stock, convertible into 800,000 shares of common stock at \$1.00 per share (acquired 11-4-97)	800,000	4,000,000
<b>Dallas, Texas</b> Distributor of computer datacenter and office automation supplies and accessories; manufactures and distributes devices used to monitor and manage intransit inventory and dunnage products for protecting shipments.		4,000,002 shares of common stock (acquired 11-4-97)	4,615,000	19,900,000
			<u>5,415,000</u>	<u>23,900,000</u>
<b>¥THE RECTORSEAL CORPORATION</b>	100.0%	27,907 shares of common stock (acquired 1-5-73 and 3-31-73)	52,600	275,800,000
<b>Houston, Texas</b> Specialty chemicals, tools and products for plumbing, HVAC, electrical, construction, industrial, and oil field; smoke containment systems for building fires; also owns 20% of The Whitmore Manufacturing Company.				
<b>TITANLINER, INC.</b>	31.2%	217,038 shares of Series A Convertible Preferred Stock convertible into 217,038 shares of Series A Preferred Stock at \$14.76 per share (acquired 6-29-12)	3,203,000	1
<b>Midland, Texas</b> Manufactures, installs and rents spill containment system for oilfield applications.		7% senior subordinated secured promissory note, due 6-30-17 (acquired 6-29-12)	2,747,000	1,519,000
		Warrants to purchase 122,239 shares of Series A Preferred Stock at \$ 0.01 per share, expiring 12-31-22	-	-
			<u>5,950,000</u>	<u>1,519,001</u>
<b>TRAX HOLDINGS, INC.</b>	28.4%	475,430 shares of Series B convertible Preferred Stock convertible into 475,430 shares of common stock at \$8.41 per share (acquired 12-5-12)	4,000,000	7,700,000
<b>Scottsdale, Arizona</b> Provides a comprehensive set of solutions to improve the validation, accounting and payment of transportation-related invoices.		1,061,279 shares of Series A Convertible Preferred Stock, convertible into 1,061,279 shares of common stock at \$4.71 per share (acquired 12-8-08 and 2-17-09)	5,000,000	13,300,000
			<u>9,000,000</u>	<u>21,000,000</u>
<b>*WELLOGIX, INC.</b>	19.0%	4,788,371 shares of Series A-1 Convertible Participating Preferred Stock, convertible into 4,788,371 shares of common stock at \$1.04 per share (acquired 8-19-05 thru 6-15-08)	5,000,000	25,000
<b>Houston, Texas</b> Formerly a developer and supporter of business process software used by the oil and gas industry.				

†Publicly-owned company ¥ Control investment \* Affiliated investment ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

**CAPITAL SOUTHWEST CORPORATION AND SUBSIDIARIES**
**CONSOLIDATED SCHEDULE OF INVESTMENTS**

March 31, 2014

Company	Equity (a)	Investment (b)	Cost	Value (c)
<b>¥THE WHITMORE MANUFACTURING COMPANY</b> Rockwall, Texas Specialized surface mining, railroad and industrial lubricants; coatings for automobiles and primary metals; fluid contamination control devices.	80.0%	80 shares of common stock (acquired 8-31-79)	1,600,000	88,500,000
<b>MISCELLANEOUS</b>	-	Ballast Point Ventures II, L.P. 2.2% limited partnership interest (acquired 8-4-08 thru 2-15-13)	2,334,790	3,167,000
	-	BankCap Partners Fund I, L.P. 5.5% limited partnership interest (acquired 7-14-06 thru 11-16-12)	6,000,000	5,385,000
	-	†Capitala Finance Corporation 108,105 shares of common stock (acquired 9-25-13)	1,363,799	2,083,183
	-	CapitalSouth Partners Fund III, L.P. 1.9% limited partnership interest (acquired 1-22-08 and 11-16-11)	467,457	237,000
	-	Diamond State Ventures, L.P. 1.4% limited partnership interest (acquired 10-12-99 thru 8-26-05)	-	16,000
	-	First Capital Group of Texas III, L.P. 3.0% limited partnership interest (acquired 12-26-00 thru 8-12-05)	778,895	117,000
	100%	¥Humac Company 1,041,000 shares of common stock (acquired 1-31-75 and 12-31-75)	-	210,000
	-	†North American Energy Partners, Inc. 77,194 shares of common stock (acquired 8-20-12)	236,986	555,797
	-	STARTech Seed Fund II 3.2% limited partnership interest (acquired 4-28-00 thru 2-23-05)	754,327	183,000
<b>TOTAL INVESTMENTS</b>			<b>\$ 98,966,994</b>	<b>\$ 677,920,145</b>

†Publicly-owned company    ¥ Control investment    \* Affiliated investment    ‡Unrestricted securities as defined in Note (a)

*The accompanying Notes are an integral part of these Consolidated Financial Statements*

## Notes to Consolidated Schedule of Investments

### (a) Equity

The percentages in the “Equity” column express equity interests held collectively by Capital Southwest Corporation and Capital Southwest Venture Corporation (together, the “Company”) in each issuer. Each percentage represents the amount of the issuer’s common stock owned by the Company or which the Company has the right to acquire as a percentage of the issuer’s total outstanding common stock, on a fully diluted basis.

### (b) Investments

Unrestricted securities (indicated by ‡) are freely marketable securities having readily available market quotations. All other securities are restricted securities, which are subject to one or more restrictions on resale and are not freely marketable. At June 30, 2014, restricted securities represented approximately 68.5% of the value of the consolidated investment portfolio. At March 31, 2014, restricted securities represented approximately 67.5% of the value of the consolidated investment portfolio.

Our investments are carried at fair value in accordance with the Investment Company Act of 1940 (the “1940 Act”) and FASB Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures. In accordance with the 1940 Act, unrestricted minority-owned publicly traded securities, for which the market quotations are readily available, are valued at the closing sale price for the NYSE listed securities and the lower of the closing bid price or the last sale price for NASDAQ securities on the valuation date; privately held securities are valued as determined in good faith by our Board of Directors.

ASC 820 defines fair value in terms of the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the “exit price”) and excludes transaction costs. Under ASC 820, the fair value measurement also assumes that the transaction to sell an asset occurs in the principal market for the asset or, in the absence of a principal market, the most advantageous market for the asset. The principal market is the market in which the reporting entity would sell or transfer the asset with the greatest volume and level of activity for the asset. In determining the principal market for an asset or liability under ASC 820, it is assumed that the reporting entity has access to the market as of the measurement date.

### (c) Value

Debt Securities are generally valued on the basis of the price the security would command in order to provide a yield-to-maturity equivalent to the present yield of comparable debt instruments of similar quality. Issuers whose debt securities are judged to be of poor quality and doubtful collectability may instead be valued by assigning percentage discounts commensurate with the quality of such debt securities. Debt securities may also be valued based on the resulting value from the sale of the business at the estimated fair market value.

Partnership Interests, Preferred Equity and Common Equity, including unrestricted marketable securities, are valued at the closing sale price for the NYSE listed securities and the lower of the closing bid price or the last sale price for NASDAQ securities on the valuation date. For those without a principal market, our Board of Directors considers the financial condition and operating results of the issuer; the long-term potential of the business of the issuer; the market for and recent sales prices of the issuer’s securities; the values of similar securities issued by companies in similar businesses; and the proportion of the issuer’s securities owned by the Company. Investments in certain entities that calculate net asset value per share (or its equivalent) and for which fair market value is not readily determinable are valued using the net asset value per share (or its equivalent, such as member units or ownership interest in partners’ capital to which a proportionate share of net assets is attributed) of the investment.

Equity warrants are valued on the basis of the Black-Scholes model which defines the market value of a warrant in relation to the market price of the underlying common stock, share price volatility, and time to maturity.

(d) Agreements between Certain Issuers and the Company

Agreements between certain issuers and the Company provide that the issuer will bear substantially all costs in connection with the Company disposing of such common stock, including those costs involved in registration under the Securities Act of 1933, but excluding underwriting discounts and commissions. These agreements cover common stock owned at June 30, 2014 and common stock which may be acquired thereafter through the exercise of warrants and conversion of debentures and preferred stock. They apply to restricted securities of all issuers in the investment portfolio of the Company, except securities of the following issuers which are not obligated to bear registration costs: Humac Company and The Whitmore Manufacturing Company.

(e) Descriptions and Ownership Percentages

The descriptions of the companies and ownership percentages shown in the Consolidated Schedule of Investments were obtained from published reports and other sources believed to be reliable. Acquisition dates indicated are the dates specific securities were acquired, which may differ from the original investment dates. Certain securities were received in exchange for or upon conversion or exercise of other securities previously acquired.

## 1. ORGANIZATION AND BASIS OF PRESENTATION

### Organization

Capital Southwest Corporation (“CSWC”) is a publicly traded investment company whose objective is to achieve capital appreciation through long-term investments in privately held businesses. Our investment interests are focused on acquisitions and investments in a broad range of industry segments. We were organized as a Texas corporation on April 19, 1961. Until September 1969, CSWC operated as a licensee under the Small Business Investment Act of 1958. At that time, we transferred to our wholly-owned subsidiary, Capital Southwest Venture Corporation (“CSVC”), certain assets and our license as a small business investment company (“SBIC”). CSVC is a closed-end, non-diversified investment company registered under the Investment Company Act of 1940, as amended (the “1940 Act”). Prior to March 30, 1988, CSWC was registered as a closed-end, non-diversified investment company under the 1940 Act. On that date, CSWC elected to become a Business Development Company (“BDC”) subject to the provisions of the 1940 Act, as amended by the Small Business Incentive Act of 1980. Because CSWC wholly owns CSVC, the portfolios of both CSWC and CSVC are referred to collectively as “our,” “we” and “us.” Capital Southwest Management Company (“CSMC”), a wholly-owned subsidiary of CSWC, is the management company for CSWC and CSVC. CSMC generally incurs all normal operating and administrative expenses, including, but not limited to, salaries and related benefits, rent, equipment and other administrative costs required for its day-to-day operations.

Our portfolio consists of private companies in which we have controlling interests, private companies in which we have minority interests and marketable securities of publicly traded companies. We make available significant managerial assistance to the companies in which we invest and believe that providing managerial assistance to such investee companies is critical to their business development activities. CSMC receives a monthly fixed fee for management services provided to certain of its control portfolio companies.

### Basis of Presentation

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (GAAP). Under rules and regulations applicable to investment companies, we are precluded from consolidating any entity other than another investment company. An exception to this general principle occurs if the investment company has an investment in an operating company that provides services to the investment company. Accordingly, consolidated financial statements include CSMC, our management company.

On July 15, 2013, a four-for-one split of our common stock was approved by our shareholders. The stock split was payable on August 15, 2013 to shareholders of record at the close of business on July 31, 2013. Our common stock began trading at the split-adjusted price on August 16, 2013. All share numbers and per share amounts presented herein reflect the stock split.

### Portfolio Investment Classification

We classify our investments in accordance with the requirements of the 1940 Act. Under the 1940 Act, “Control Investments” are defined as investments in which we own more than 25% of the voting securities or have rights to maintain greater than 50% of the board representation; “Affiliated Investments” are defined as investments in which we own between 5% and 25% of the voting securities; and “Non-Control/Non-Affiliated Investments” are defined as investments that are neither “Control Investments” nor “Affiliated Investments.”



## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements of CSWC.

**Fair Value Measurements.** We adopted FASB ASC Topic 820 on April 1, 2008. ASC Topic 820 (1) creates a single definition of fair value, (2) establishes a framework for measuring fair value, and (3) expands disclosure requirements about items measured at fair value. The Statement applies to both items recognized and reported at fair value in the financial statements and items disclosed at fair value in the notes to the financial statements. The Statement does not change existing accounting rules governing what can or what must be recognized and reported at fair value in our financial statements, or disclosed at fair value in our notes to financial statements. Additionally, ASC Topic 820 does not eliminate practicability exceptions that exist in accounting pronouncements amended by this Statement when measuring fair value.

Fair value is generally determined based on quoted market prices in the active markets for identical assets or liabilities. If quoted market prices are not available, we use valuation techniques that place greater reliance on observable inputs and less reliance on unobservable inputs. Due to the inherent uncertainty in the valuation process, our estimate of fair value may differ materially from the values that would have been used had a ready market for the securities existed. In addition, changes in the market environment, portfolio company performance and other events may occur over the lives of the investments that may cause the gains or losses ultimately realized on these investments to be materially different than the valuations currently assigned. We determine the fair value of each individual investment and record changes in fair value as unrealized appreciation or depreciation.

Pursuant to our internal valuation process, each portfolio company is valued once a quarter. In addition to our internal valuation process, our Board of Directors retains a nationally recognized firm to provide limited scope third party valuation services on certain portfolio investments. Our Board of Directors retained Duff & Phelps to provide limited scope third party valuation services on three investments comprising 57.3% of our net asset value at March 31, 2014.

We believe our investments at June 30, 2014 and March 31, 2014 approximate fair value as of those dates based on the market in which we operate and other conditions in existence at those reporting periods.

**Investments.** Investments are stated at fair value determined by our Board of Directors as described in Notes to the Consolidated Schedule of Investments and Note 3 below. The average cost method is used in determining cost of investments sold. Investments are recorded on a trade date basis.

**Cash and Cash Equivalents.** Cash and cash equivalents consist of highly liquid investments with an original maturity of three months or less at the date of purchase. Cash and cash equivalents are carried at cost, which approximates fair value.

**Segment Information.** We operate and manage our business in a singular segment. As an investment company, we invest in portfolio companies in various industries and geographic areas as presented in the Consolidated Schedule of Investments.

**Use of Estimates.** The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

**Interest and Dividend Income.** Interest and dividend income is recorded on an accrual basis to the extent amounts are expected to be collected. Dividend income is recorded at the ex-dividend date for marketable securities and restricted securities. In accordance with our valuation policy, accrued interest and dividend income is evaluated periodically for collectability. When we do not expect the debtor to be able to service all of its debt or other obligations, we will generally establish a reserve against interest income, thereby placing the loan or debt security's status on a non-accrual basis, and cease to recognize interest income on that loan or debt security until the borrower has demonstrated the ability and intent to pay contractual amounts due. If a loan or debt security's status significantly improves regarding ability to service debt or other obligations, it will be restored to accrual basis.

**Federal Income Taxes.** CSWC and CSVC have elected and intend to comply with the requirements of the Internal Revenue Code ("IRC") necessary to qualify as regulated investment companies ("RICs"). By meeting these requirements, they will not be subject to corporate federal income taxes on ordinary income distributed to shareholders. In order to comply as a RIC, each company is required to timely distribute to its shareholders at least 90% of investment company taxable income, as defined by the IRC, each year. Investment company taxable income generally differs from net income for financial reporting purposes due to temporary and permanent differences in the recognition of income and expenses. Investment company taxable income generally excludes net unrealized appreciation or depreciation, as investment gains and losses are not included in investment company taxable income until they are realized.

In addition to the requirement that we must annually distribute at least 90% of our investment company taxable income, we may either distribute or retain our realized net capital gains from investments, but any net capital gains not distributed may be subject to corporate level tax. During the three months ended June 30, 2014, we did not distribute any capital gain dividends to our shareholders. When we retain the capital gains, they are classified as a "deemed distribution" to our shareholders and are subject to our corporate tax rate of 35%. As an investment company that qualifies as a RIC under the IRC, federal income taxes payable on security gains that we elect to retain are accrued only on the last day of our tax year, December 31. Any capital gains actually distributed to shareholders are generally taxable to the shareholders as long-term capital gains. See Note 4 for further discussion.

CSMC, a wholly owned subsidiary of CSWC, is not a RIC and is required to pay taxes at the current corporate rate of 35%.

We account for interest and penalties as part of operating expenses. There were no interest or penalties incurred during three months ended June 30, 2014 and 2013.

**Deferred Taxes.** CSMC sponsors a qualified defined benefit pension plan which covers its employees and employees of certain wholly owned portfolio companies. In addition, CSMC records phantom stock options and bonus accruals on a quarterly basis. Deferred taxes related to the qualified defined pension plan, phantom stock options and bonus accruals are recorded as incurred.

**Stock-Based Compensation.** We account for our stock-based compensation using the fair value method, as prescribed by ASC 718, *Compensation – Stock Compensation*. Accordingly, we recognize stock-based compensation cost over the straight-line method for all share-based payment awards granted to employees. The fair value of stock options are determined on the date of grant using the Black-Scholes pricing model and are expensed over the vesting period of the related stock options. For restricted stock awards, we measured the grant date fair value based upon the market price of our common stock on the date of the grant and will amortize this fair value to share based compensation expense over the vesting term. For phantom stock options, the option value of phantom stock awards is calculated based on the net asset value of our Corporation. We value the plan each quarter and either increase or decrease the liability based on the phantom option value. See Note 6 for further discussion.

**Retirement Plans.** We record annual amounts relating to the pension plans based on calculations and various actuarial assumptions. Material changes in pension costs could occur due to changes in the discount rate, changes in the expected long-term rate of return, changes in mortality table, and changes in level of contributions to the plans and other factors. The funded status of the qualified plan is the difference between the fair value of plan assets and the benefit obligation. We recognize changes in the funded status of the qualified plan in the Statement of Assets and Liabilities in the year in which the changes occur and measure its assets and obligations as of the date of the employer's fiscal year-end. In addition, CSWC also sponsors an unfunded Retirement Restoration Plan, which is a nonqualified plan that provides for the payment, upon retirement, of the difference between the maximum annual payment permissible under the qualified retirement plan pursuant to Federal limitations and the amount which would otherwise have been payable under the qualified plan. We presently use March 31 as the measurement date for retirement plans.

**Concentration of Risk.** We place our uninvested cash in financial institutions, and at times, such balances may be in excess of the federally insured limits.

### 3. INVESTMENTS

We record our investments at fair value as determined in good faith by our Board of Directors in accordance with GAAP. When available, we base the fair value of our investments on directly observable market prices or on market data derived for comparable assets. For all other investments, inputs used to measure fair value reflect management's best estimate of assumptions that would be used by market participants in pricing the investments in a hypothetical transaction.

The levels of fair value inputs used to measure our investments are characterized in accordance with the fair value hierarchy established by ASC. We use judgment and consider factors specific to the investment in determining the significance of an input to a fair value measurement. While management believes our valuation methodologies are appropriate and consistent with market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The three levels of the fair value hierarchy and investments that fall into each of the levels are described below:

- *Level 1:* Investments whose values are based on unadjusted quoted prices in active markets for identical assets or liabilities that we have the ability to access. We use Level 1 inputs for publicly traded unrestricted securities. Such investments are valued at the closing price for NYSE listed securities and at the lower of the closing bid price or the closing sale price for NASDAQ securities on the valuation date.
- *Level 2:* Investments whose values are based on observable inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs may include quoted prices for the identical instrument in non-active markets, quoted prices for similar instruments in active markets and similar data. We did not value any of our investments using Level 2 inputs as of June 30, 2014.

- *Level 3*: Investments whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect management's own assumptions about the assumptions a market participant would use in pricing the investment. We used Level 3 inputs for measuring the fair value of approximately 68.5% of our investments as of June 30, 2014. See "Notes to Consolidated Schedule of Investments" (c) on page 14 for the investment policy used to determine the fair value of these investments.

As required by ASC 820, when the inputs used to measure fair value fall within different levels of the hierarchy, the level within the fair value measurement is categorized based on the lowest level input that is significant to the fair value measurement which may include inputs that are observable (Levels 1 and 2) and unobservable (Level 3). Therefore, gains and losses for such investments categorized within the Level 3 table below may include changes in fair value that are attributable to both observable inputs (Levels 1 and 2) and unobservable (Level 3). We conduct reviews of fair value hierarchy classifications on a quarterly basis. Changes in the observability of valuation inputs may result in a reclassification of certain investments.

Unobservable inputs are those inputs for which little or no market data exists and, therefore, require an entity to develop its own assumptions. The fair value determination of each portfolio company requires one or more of the following unobservable inputs:

- Financial information obtained from each portfolio company, including audited and unaudited statements of operations and balance sheets for the most recent period available as compared to budgeted numbers;
- Current and projected financial condition of the portfolio company;
- Current and projected ability of the portfolio company to service its debt obligations;
- Projected operating results of the portfolio company;
- Current information regarding any offers to purchase the investment or recent private sales transactions;
- Current ability of the portfolio company to raise any additional financing as needed;
- Change in the economic environment which may have a material impact on the operating results of the portfolio company;
- Qualitative assessment of key management;
- Contractual rights, obligations or restrictions associated with the investment; and
- Other factors deemed relevant.

Preferred Stock and Common Stock

The significant unobservable inputs used in the fair value measurement of our equity securities are EBITDA multiples, revenue multiples, net book values, tangible book value multiples, and the weighted average costs of capital (“WACC”). Generally, increases or decreases in EBITDA or revenue multiple inputs result in a higher or lower fair value measurement, respectively. Generally, increases or decreases in WACC result in a lower or higher fair value measurement, respectively. However, due to the nature of certain investments, fair value measurements may be based on other criteria, such as third party-appraisals. For recent investments, we generally rely on our cost basis to determine the fair value unless fair value is deemed to have departed from this level.

Debt Securities

The significant unobservable inputs used in the fair value measurement of our debt securities are risk adjusted discount factors used in the yield valuation technique and probability of principal recovery. A significant increase or decrease in any of these valuation inputs in isolation would result in a significantly lower or higher fair value measurement. However, due to the nature of certain investments, fair value measurements may be based on other criteria, such as third party inputs.

Limited Partnership or Limited Liability Company Interests

For recent investments, we generally evaluate limited partnership or limited liability company interests at cost, which is deemed to represent market value, unless or until there is substantive evidence that cost does not correspond to fair value. Thereafter, these securities are generally valued at our percentage interest of the fund or company’s calculated net asset value, unless there is substantive evidence that the net asset value does not correspond to fair value. All investments of each fund are valued by each fund in accordance with ASC 820.

The table below presents the valuation technique and quantitative information about the significant unobservable inputs utilized by the Company to value our Level 3 investments as of June 30, 2014 and March 31, 2014. Unobservable inputs are those inputs for which little or no market data exists and therefore require an entity to develop its own assumptions. The table is not intended to be all inclusive, but instead captures the significant unobservable inputs relevant to our determination of fair value

Type	Valuation Technique	Fair Value at 6/30/2014 (in millions)	Unobservable Input	Range	Weighted Average
Preferred & Common Equity	Market Approach	\$ 432.6	EBITDA Multiple	3.00x – 7.75x	6.98x
	Market Approach	20.5	Revenue Multiple	0.41x – 2.50x	2.50x
	Market Approach	7.4	Cash and Asset Value	NA	NA
	Market Approach	4.0	Multiple of Tangible Book Value	1.57x	1.57x
	Market Approach	0.2	Market Value of Held Securities	NA	NA
		<u>464.7</u>			
Debt	Liquidation Value	0.6	Cash and Asset Value	NA	NA
	Market Approach	2.0	Discount to Face Value	27.00%	27.00%
		<u>2.6</u>			
Partnership Interests	Net Asset Value	9.2	Fund Value	NA	NA
	<b>Total</b>	<b>\$ 476.5</b>			

Type	Valuation Technique	Fair Value at 3/31/2014 (in millions)	Unobservable Input	Range	Weighted Average
Preferred & Common Equity	Market Approach	\$ 404.1	EBITDA Multiple	3.50x – 7.78x	7.00x
	Market Approach	22.0	Revenue Multiple	1.53x – 2.50x	2.46x
	Market Approach	8.0	Recent Transaction Price	NA	NA
	Market Approach	7.6	Cash and Asset Value	NA	NA
	Market Approach	3.8	Multiple of Tangible Book Value	1.54x	1.54x
	Market Approach	0.2	Market Value of Held Securities	NA	NA
		<u>445.7</u>			
Debt	Discounted Cash Flow	1.5	Discount Rate	11.69%	11.69%
	Recent Transaction Price	1.2	Recent Transaction Price	NA	NA
Partnership Interests		<u>2.7</u>			
	Net Asset Value	9.5	Fund Value	NA	NA
	<b>Total</b>	<b>\$ 457.9</b>			

\* All funds are valued in accordance with ASC 820.

As of June 30, 2014 and March 31, 2014, 68.5% and 67.5%, respectively, of our portfolio investments were categorized as Level 3.

The following fair value hierarchy tables set forth our investment portfolio by level as of June 30, 2014 and March 31, 2014 (in millions):

Asset Category	Total	Fair Value Measurements at 6/30/14 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Debt	\$ 2.6	\$ –	\$ –	\$ 2.6
Partnership Interests	9.2	–	–	9.2
Preferred Equity	44.2	–	–	44.2
Common Equity	640.0	219.5	–	420.5
Total Investments	<u>\$ 696.0</u>	<u>\$ 219.5</u>	<u>\$ –</u>	<u>\$ 476.5</u>

Asset Category	Total	Fair Value Measurements at 3/31/14 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Debt	\$ 2.7	\$ –	\$ –	\$ 2.7
Partnership Interests	9.5	–	–	9.5
Preferred Equity	47.0	–	–	47.0
Common Equity	618.7	220.0	–	398.7
Total Investments	<u>\$ 677.9</u>	<u>\$ 220.0</u>	<u>\$ –</u>	<u>\$ 457.9</u>

The following table provides a summary of changes in the fair value of investments measured using Level 3 inputs during the quarter ended June 30, 2014 (in millions):

	Fair Value 3/31/14	Net Unrealized Appreciation (Depreciation)	New Investments	Divestitures	Conversion of Security from Debt to Equity	Fair Value at 6/30/2014
Debt	\$ 2.7	\$ (0.1)	\$ -	\$ -	\$ -	\$ 2.6
Partnership Interests	9.5	0.2	-	(0.5)	-	9.2
Preferred Equity	47.0	(2.8)	-	-	-	44.2
Common Equity	398.7	21.8	-	-	-	420.5
<b>Total Investments</b>	<b>\$ 457.9</b>	<b>\$ 19.1</b>	<b>\$ -</b>	<b>\$ (0.5)</b>	<b>\$ -</b>	<b>\$ 476.5</b>

#### 4. INCOME TAXES

We operate to qualify as a RIC under Subchapter M of the IRC and have a calendar tax year end of December 31. In order to qualify as a RIC, we must annually distribute at least 90% of our investment company taxable income, as defined by the IRC, to our shareholders in a timely manner. Investment company income generally includes net short-term capital gains but excludes net long-term capital gains. A RIC is not subject to federal income tax on the portion of its ordinary income and long-term capital gains that are distributed to its shareholders, including “deemed distributions” discussed below. As permitted by the Code, a RIC can designate dividends paid in the subsequent tax year as dividends of current year ordinary income and net long-term gains if those dividends are both declared by the extended due date of the RIC’s federal income tax return and paid to shareholders by the last day of the subsequent tax year.

We have distributed or intend to distribute sufficient dividends to eliminate taxable income for our completed tax years. If we fail to satisfy the 90% distribution requirement or otherwise fail to qualify as a RIC in any tax year, we would be subject to tax in such year on all of our taxable income, regardless of whether we made any distributions to our shareholders. For the tax years ended December 31, 2013 and 2012, we declared and paid ordinary dividends in the amounts of \$3,049,614 and \$3,025,032, respectively.

Additionally, we are subject to a nondeductible federal excise tax of 4% if we do not distribute at least 98% of our investment company ordinary taxable income before the end of our tax year. For the tax years ended December 31, 2013 and 2012, we distributed 100% of our investment company ordinary taxable income. As a result, we have made no tax provisions for income taxes on ordinary taxable income for the tax years ended December 31, 2013 and 2012.

A RIC may elect to retain its long-term capital gains by designating them as “deemed distribution” to its shareholders and paying a federal tax rate of 35% on the long-term capital gains for the benefit of its shareholders. Shareholders then report their share of the retained capital gains on their income tax returns as if it had been received and report a tax credit for tax paid on their behalf by the RIC. Shareholders then add the amount of the “deemed distribution” net of such tax, to the basis of their shares.

During our tax year ended December 31, 2013, we sold 9,317,310 shares of common stock of Heelys, Inc. to Sequential Brands Group, Inc. and generated cash proceeds of \$20,963,948 and a capital gain of \$20,861,458. Subsequently, we distributed and paid \$0.69 per share or \$10,474,932 of Heely’s gain to our shareholders on March 28, 2013. For the tax year ended December 31, 2013, we had net long-term capital gains of \$10,819,079 for tax purposes and \$10,491,526 for book purposes, which we elected to retain and treat as deemed distributions to our shareholders.

In order to make the election to retain capital gains, we incurred federal taxes on behalf of our shareholders in the amount of \$3,786,678 for the tax year ended December 31, 2013. For the tax year ended December 31, 2012, we incurred federal taxes on behalf of our shareholders in the amount of \$1,125,092.

For the quarter ended June 30, 2014 and 2013, CSWC and CSVC qualified to be taxed as RICs. We intend to meet the applicable qualifications to be taxed as a RIC in future years. Management feels it is probable that we will maintain our RIC status for a period longer than one year. However, either company's ability to meet certain portfolio diversification requirements of RICs in future years may not be controllable by such company.

CSMC, a wholly owned subsidiary of CSWC, is not a RIC and is required to pay taxes at the current corporate rate. CSMC sponsors a qualified defined benefit pension plan which covers its employees and employees of certain wholly owned portfolio companies. In addition, CSMC records phantom stock option and bonus accruals on a quarterly basis. Deferred taxes related to the qualified defined benefit pension plan and phantom stock option and bonus accruals are recorded as incurred. As of June 30, 2014, CSMC has a deferred tax liability of \$2,210,265.

## 5. ACCUMULATED NET REALIZED GAINS (LOSSES) ON INVESTMENTS

Distributions made by RICs often differ from aggregate GAAP-basis undistributed net investment income and accumulated net realized gains (total GAAP-basis net realized gains). The principal cause is that required minimum fund distributions are based on income and gain amounts determined in accordance with federal income tax regulations, rather than GAAP. The differences created can be temporary, meaning that they will reverse in the future, or they can be permanent. In subsequent periods, when all or a portion of a temporary difference becomes a permanent difference, the amount of the permanent difference will be reclassified to "additional capital."

We incur federal taxes on behalf of our shareholders as a result of our election to retain long-term capital gains. We had \$1,684,285 of accumulated long term capital loss at June 30, 2014 and \$14,029,087 of accumulated long term capital gains at March 31, 2014, respectively.

## 6. EMPLOYEE STOCK BASED COMPENSATION PLANS

### Stock Options

On July 20, 2009, shareholders approved our 2009 Stock Incentive Plan (the "2009 Plan"), which provides for the granting of stock options to employees and officers and authorizes the issuance of common stock upon exercise of such options for up to 560,000 shares. All options are granted at or above market price, generally expire up to 10 years from the date of grant and are generally exercisable on or after the first anniversary of the date of grant in five annual installments. Options to purchase 155,000 shares at a price of \$19.19 per share (market price at the time of grant) were granted on October 19, 2009. Additionally, options to purchase 80,000 shares at a price of \$23.95 per share (market price at time of grant) were granted on March 22, 2010, options to purchase 60,000 shares at a price of \$22.05 per share were granted on July 19, 2010 and options to purchase 40,000 shares at a price of \$24.23 per share were granted on July 18, 2011. Options to purchase 30,000 shares at a price of \$37.02 per share, 25,000 shares at a price of \$33.52 and 30,000 shares at a price of \$34.91 were granted on July 15, 2013, January 20, 2014 and March 17, 2014, respectively. At June 30, 2014, there are options to acquire 123,800 shares of common stock outstanding and options to acquire 259,000 shares of common stock available for grant under the 2009 Plan.



We previously granted stock options under our 1999 Stock Option Plan (the “1999 Plan”), as approved by shareholders on July 19, 1999. The 1999 Plan expired on April 19, 2009. Options previously granted under our 1999 Stock Option Plan and outstanding on July 20, 2009 continue in effect and are governed by the provisions of the 1999 Plan. All options granted under the 1999 Plan were granted at or above market price, generally expire up to 10 years from the date of grant and are generally exercisable on or after the first anniversary of the date of grant in five to ten annual installments. At June 30, 2014, there are options to acquired 38,000 shares of common stock outstanding under the 1999 Plan.

We recognize compensation cost over the straight-line method for all share-based payments granted on or after that date and for all awards granted to employees prior to April 1, 2006 that remain unvested on that date. The fair value of stock options are determined on the date of grant using the Black-Scholes pricing model and are expensed over the vesting period of the related stock options. Share-based compensation cost for stock options is measured based on the closing fair market value of our Company’s common stock on the date of the grant. Accordingly, for the quarters ended June 30, 2014 and 2013, we recognized stock option compensation expense of \$73,103 and \$143,161, respectively.

As of June 30, 2014, the total remaining unrecognized compensation cost related to non-vested stock options was \$806,864, which will be amortized over the weighted-average service period of approximately 2.7 years.

The following table summarizes the 2009 Plan and the 1999 Plan exercise price per option at grant date using the Black-Scholes pricing model:

Date of Issuance	Weighted Average Fair Value	Black-Scholes Pricing Model Assumptions			Expected Life (in years)
		Expected Dividend Yield	Risk- Free Interest Rate	Expected Volatility	
<b>2009 Plan</b>					
July 18, 2011	\$ 8.27	0.83%	1.45%	40.0%	5
July 19, 2010	\$ 7.15	0.91%	1.73%	37.5%	5
March 22, 2010	\$ 8.14	0.84%	2.43%	37.8%	5
October 19, 2009	\$ 6.34	1.04%	2.36%	37.6%	5
July 15, 2013	\$ 11.82	0.54%	1.40%	36.1%	5
January 20, 2014	\$ 8.37	0.60%	1.64%	27.0%	5
March 17, 2014	\$ 7.04	0.57%	1.58%	21.1%	5
<b>1999 Plan</b>					
July 30, 2008	\$ 7.48	0.62%	3.36%	20.2%	5
July 21, 2008	\$ 6.84	0.67%	3.41%	20.2%	5
July 16, 2007	\$ 10.44	0.39%	4.95%	19.9%	5
July 17, 2006	\$ 8.26	0.61%	5.04%	21.2%	7
May 15, 2006	\$ 7.82	0.64%	5.08%	21.1%	7

The following table summarizes activity in the 2009 Plan and the 1999 Plan as of June 30, 2014:

	Number of Shares	Weighted Average Exercise Price
<b>2009 Plan</b>		
Balance at March 31, 2012	335,000	\$ 21.44
Granted	—	—
Exercised	(108,092)	19.96
Canceled/Forfeited	(56,000)	21.44
Balance at March 31, 2013	170,908	22.37
Granted	85,000	35.25
Exercised	(69,108)	22.27
Canceled/Forfeited	(63,000)	22.08
Balance at March 31, 2014	123,800	31.40
Granted	—	—
Exercised	—	—
Canceled/Forfeited	—	—
Balance at June 30, 2014	123,800	\$ 31.40
<b>1999 Plan</b>		
Balance at March 31, 2012	380,000	28.41
Granted	—	—
Exercised	(76,420)	23.83
Canceled/Forfeited	(57,580)	27.79
Balance at March 31, 2013	246,000	33.00
Granted	—	—
Exercised	(108,000)	30.37
Canceled/Forfeited	(100,000)	38.25
Balance at March 31, 2014	38,000	\$ 26.68
Granted	—	—
Exercised	—	—
Canceled/Forfeited	—	—
Balance at June 30, 2014	38,000	26.68
Combined Balance at June 30, 2014	161,800	\$ 30.29

June 30, 2014	Weighted Average Aggregate Intrinsic	
	Remaining Contractual Term	Value
Outstanding	2.7 years	\$ 1,307,329
Exercisable	0.5 years	\$ 379,047

At June 30, 2014, the range of exercise prices was \$19.19 to \$37.02 and the weighted-average remaining contractual life of outstanding options was 2.7 years. The total number of shares of options exercisable under both the 2009 Plan and the 1999 Plan at June 30, 2014, was 52,800 shares with a weighted-average exercise price of \$25.69. During the quarter ended June 30, 2014, no options were exercised. During the quarter ended June 30, 2013, 4,900 options were exercised.

**Stock Awards**

Pursuant to the Capital Southwest Corporation 2010 Restricted Stock Award Plan, our Board of Directors reserved for issuance 188,000 shares of restricted stock to certain key employees. A restricted stock award is an award of shares of our common stock (which have full voting and dividend rights but are restricted with regard to sale or transfer), the restrictions on which lapse ratably over a specified period of time (generally five years). Restricted stock awards are independent of stock grants and are subject to forfeiture if employment terminates prior to these restrictions lapsing. These shares vest in equal annual installments over a five-year period from the grant date and are expensed over the five-year service period starting on the grant date. On January 16, 2012, the Board of Directors granted 38,600 shares of restricted stock to key employees of the Company. On January 22, 2013, the Board of Directors granted 8,000 shares of restricted stock to officers of the Company. On July 15, 2013, The Board of Directors granted 5,000 shares of restricted stock to a key officer of the Company. On January 20, 2014, the Board of Directors granted 4,800 shares of restricted stock to key employees of the Company. On March 17, 2014, the Board of Directors granted 5,000 shares of restricted stock to a key employee of the Company. The following table summarizes the restricted stock available for issuance as of June 30, 2014:

Restricted stock available for issuance as of March 31, 2014	154,240
Restricted stock granted during the three months ended June 30, 2014	-
Restricted stock forfeited during the three months ended June 30, 2014	-
Restricted stock available for issuance as of June 30, 2014	<u>154,240</u>

We expense the cost of the restricted stock awards, which is determined to equal the fair value of the restricted stock award at the date of grant on a straight-line basis over the vesting period. For these purposes, the fair value of the restricted stock award is determined based upon the closing price of our common stock on the date of the grant. For the quarters ended June 30, 2014 and 2013, we recognized total share based compensation expense of \$42,790 and \$30,406, respectively, related to the restricted stock issued to our employees and officers.

As of June 30, 2014, the total remaining unrecognized compensation expense related to non-vested restricted stock awards was \$649,503, which will be amortized over the weighted-average service period of approximately 3.8 years.

No restricted stock was granted during the three months ended June 30, 2014.

Restricted Stock Awards	Number of Shares	Weighted Average Fair Value Per Share	Weighted Average Remaining Vesting Term (in Years)
Unvested at March 31, 2014	24,680	\$ 30.30	4.1
Granted	-	-	-
Vested	-	-	-
Forfeited	-	-	-
Unvested at June 30, 2014	<u>24,680</u>	<u>\$ 30.30</u>	<u>3.8</u>

**Phantom Stock Plan**

On January 16, 2012, our Board of Directors approved the issuance of 104,000 phantom stock options at an exercise price of \$36.74 (Net Asset Value at December 31, 2011) pursuant to the Capital Southwest Corporation Phantom Stock Option Plan to provide deferred compensation to certain key employees. On January 22, 2013, the Board of Directors granted 16,200 shares of phantom stock options at an exercise price of \$41.34 per share (Net Asset Value at December 31, 2012) to officers of the Company. On July 15, 2013, the Board of Directors granted 24,000 shares of phantom stock options at an exercise price of \$43.80 per share (Net Asset Value at June 30, 2013) to a key officer of the Company. Additionally, the Board of Directors granted 38,000 shares of phantom stock options at an exercise price of \$50.25 per share (Net Asset Value at December 31, 2013) to several key employees of the Company in January 2014 and March 2014. Under the plan, awards vest on the fifth anniversary of the award date. Upon exercise of the phantom option, a cash payment in an amount for each phantom share equal to estimated fair market value minus the phantom option exercise price, adjusted for capital gain dividends declared, will be distributed to plan participants. The estimated liability for phantom stock awards was \$758,768 as of June 30, 2014.

There were no phantom stock options granted during the three months ended June 30, 2014.

Phantom Stock Awards	Number of Shares	Weighted Average Grant Price Per Share	Weighted Average Remaining Vesting Term (in Years)
Unvested at March 31, 2014	95,000	\$ 43.59	4.1
Granted	-	-	-
Vested	-	-	-
Forfeited or expired	-	-	-
Unvested at June 30, 2014	95,000	\$ 43.59	3.8

7. COMMITMENTS

From time to time the Company may be liable for claims against its portfolio companies. We do not believe the effects of such claims would have a material impact on our results of operations and financial condition.

CSWC has agreed, subject to certain conditions, to invest up to \$1,357,576 in three portfolio companies as of June 30, 2014.

## 8. SUMMARY OF PER SHARE INFORMATION

The following presents a summary of per share data for the three months ended June 30, 2014 and 2013.

Per Share Data	Three Months Ended June 30,	
	2014	2013
Investment income	\$ .05	\$ .07
Operating expenses	(.15)	(.15)
Income taxes	-	-
Net investment loss	(.10)	(.08)
Distributions from undistributed net investment income	(.10)	(.10)
Net realized loss	(1.02)	-
Net increase in unrealized appreciation of investment	2.40	.68
<i>Capital Share transactions:</i>		
Exercise of employee stock options	-	(.02)
Forfeiture of restricted stock*	-	.01
Stock option expense	.01	.01
Increase in net asset value	1.19	.50
Net asset value		
Beginning of period	49.98	43.30
End of period	\$ 51.17	\$ 43.80

\*Reflects impact of the different share amounts as a result of issuance or forfeiture of restricted stock during the period.

## Item 2. – Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with our financial statements and the notes thereto included elsewhere in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014 (the "Form 10-K").

The information contained herein may contain "forward-looking statements" based on our current expectations, assumptions and estimates about us and our industry. These forward-looking statements involve risks and uncertainties. Words such as "believe," "anticipate," "estimate," "expect," "intend," "plan," "will," "may," "might," "could," "continue" and other similar expressions identify forward-looking statements. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of several factors more fully described in "Risk Factors" and elsewhere in this Form 10-Q, and in our Form 10-K for the year ended March 31, 2014. The forward-looking statements made in this Form 10-Q related only to events as of the date on which the statements are made. You should read the following discussion in conjunction with the consolidated financial statements and related footnotes and other financial information included in our Form 10-K for the year ended March 31, 2014. We undertake no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

**Results of Operations**

The composite measure of our financial performance in the Consolidated Statements of Operations is captioned “Increase in net assets from operations” and consists of three elements. The first is “Net investment income/loss,” which is the difference between income from interest, dividends and fees and our combined operating and interest expenses, net of applicable income taxes. The second element is “Net realized gain/loss on investments,” which is the difference between the proceeds received from the disposition of portfolio securities and their stated cost, net of applicable income tax expense based on our tax year. The third element is the “Net increase in unrealized appreciation of investments,” which is the net change in the market or fair value of our investment portfolio, compared with stated cost. It should be noted that the “Net realized gain on investments” and “Net increase in unrealized appreciation of investments” are directly related in that when an appreciated portfolio security is sold to realize a gain, a corresponding decrease in net unrealized appreciation occurs by transferring the gain associated with the transaction from being “unrealized” to being “realized.” Conversely, when a loss is realized on a depreciated portfolio security, an increase in net unrealized appreciation occurs.

*Net Investment Income*

For the three months ended June 30, 2014, total investment income was \$780,279, a \$274,666, or 26.04%, decrease from total investment income of \$1,054,945 for the three months ended June 30, 2013. This decrease was primarily attributable to a decrease in interest income from PalletOne and i-Memories. PalletOne was sold in FY 2014 and we ceased accruing interest from i-Memories in current quarter.

Our principal objective is to achieve capital appreciation. Therefore, a significant portion of our investment portfolio is structured to maximize the potential return from equity participation which typically provides minimal current yield in the form of interest or dividends. We also earn interest income from the short-term investment of cash funds, and the annual amount of such income varies based upon the average level of funds invested during the year and fluctuations in short-term interest rates. During the three months ended June 30, 2014 and 2013, the Company had interest income from temporary cash investments of \$17,264 and \$17,926, respectively.

The Company’s management fees, received primarily from its controlled affiliates, totaled \$139,950 for both the three months ended June 30, 2014 and 2013.

During the three months ended June 30, 2014 and 2013, the Company recorded dividend income from the following sources:

	Three Months Ended June 30,	
	2014	2013
Alamo Group, Inc.	\$ 198,310	\$ 198,261
Encore Wire Corporation	-	26,250
North American Energy Partners	1,190	-
The RectorSeal Corporation	240,000	240,000
TCI Holdings, Inc.	-	20,318
The Whitmore Manufacturing Company	60,000	60,000
	<u>\$ 499,500</u>	<u>\$ 544,829</u>

Due to the nature of our business, the majority of our operating expenses are related to employees’ and directors’ compensation, office expenses, legal, professional and accounting fees and pension expense. Total operating expenses increased by \$24,434, or 1.1%, for the quarter ended June 30, 2014 as compared to the quarter ended June 30, 2013. This increase is primarily due to an increase of \$165,349 in professional fees, \$52,527 in pension expense, \$44,361 in insurance expense offset by a decrease of \$166,288 in compensation and \$57,673 in stock option expense.

*Net Realized Gain (Loss) on Investments*

During the quarter ended June 30, 2014, we received proceeds of \$588,577 and realized a gain of \$351,591 from the sale of North American Energy Partners, Inc. We also received proceeds of \$2,398,706 and realized a loss of \$14,889,677 from the liquidation of Cinatra Clean Technologies, Inc. In addition, we received proceeds of \$139,713 and realized a loss of \$1,175,287 from the sale of our limited partnership interest in Discovery Alliance, LLC.

During the quarter ended June 30, 2013, we received a capital gain dividend of \$55,000 from Diamond State Venture, L.P.

Management does not attempt to maintain a consistent level of realized gains from year to year, but instead attempts to maximize total investment portfolio appreciation. This strategy often dictates the long-term holding of portfolio securities in pursuit of increased values and increased unrealized appreciation, but may at opportune times dictate realizing gains or losses through the disposition of certain portfolio investments.

*Net Increase/(Decrease) in Unrealized Appreciation of Investments*

For the quarter ended June 30, 2014, we recognized a \$36,917,417 increase in net change in unrealized appreciation of investments. This increase in unrealized appreciation is attributable to The Rectorseal Corporation, The Whitmore Manufacturing Company, Media Recovery and Balco, Inc., which increased by \$13,600,000, \$7,100,000, \$600,000 and \$600,000, respectively, due to increases in each entity's earnings; Deepwater Corrosion Services, Inc. increased by \$1,055,000 as it was the first quarter we utilized a market valuation approach since we made our investment; Encore Wire Corporation increased by \$669,375 due to an increase in its stock price. Offsetting these increases were iMemories, Inc. and Instawares Holding Company, LLC, which decreased by \$1,591,002 and \$2,302,000 respectively, due to a reduction in its enterprise value and a decrease in valuation multiple, respectively; Alamo Group, Inc. decreased by \$642,947 due to a decrease in its stock price.

For the quarter ended June 30, 2013, we recognized a \$10,391,960 increase in net change in unrealized appreciation of investments. The largest increases in unrealized appreciation are attributable to Alamo Group, Inc., which increased by \$7,295,566 due to an increase in its stock price at June 30, 2013, while The Rectorseal Corporation increased by \$6,000,000; The Whitmore Manufacturing Company increased by \$2,100,000; and Media Recovery, Inc. increased by \$1,500,000 all due to increases in the entities' respective earnings. Offsetting these increases were Hologic, Inc., which decreased by \$1,923,306, and Encore Wire Corporation, which decreased by \$1,194,375 each due to a decrease in the respective entity's stock price at June 30, 2013. Additionally, Cinatra Clean Technologies, Inc. decreased by \$1,170,995 due to under performance in their market.

Set forth in the following table are the significant increases and decreases in unrealized appreciation by our current portfolio company:

	Three Months Ended	
	June 30,	
	2014	2013
Alamo Group, Inc.	\$ (642,947)	\$ 7,295,566
Balco, Inc	600,000	-
Deepwater Corrosion Services, Inc.	1,055,000	-
Encore Wire Corporation	669,375	(1,194,375)
iMemories, Inc.	(1,591,002)	-
Instawares Holding Company, LLC	(2,302,000)	151,000
Media Recovery, Inc.	600,000	1,500,000
The RectorSeal Corporation	13,600,000	6,000,000
Trax Holdings, Inc.	(500,000)	-
The Whitmore Manufacturing Company	7,100,000	2,100,000

A description of the investments listed above and other material components of the investment portfolio are included elsewhere in this report under the caption “Consolidated Schedule of Investments – June 30, 2014 and March 31, 2014.”

### **Financial Liquidity and Capital Resources**

At June 30, 2014, the Company had cash and cash equivalents of approximately \$88.2 million. Funds may be transferred to the Company in the form of dividends from our controlled affiliates to the extent available. Additionally, approximately \$219.5 million of our June 30, 2014 investment portfolio is represented by unrestricted publicly traded securities and represents a potential source of liquidity.

Management believes that the Company’s cash and cash equivalents and cash available from other sources described above are adequate to meet its expected requirements. Consistent with the long-term strategy of the Company, the disposition of investments from time to time may also be an important source of funds for future investment activities.

### **Application of Critical Accounting Policies and Accounting Estimates**

There have been no changes during the quarter ended June 30, 2014 to the critical accounting policies or the area that involves the use of significant judgments or estimates we described in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

We are subject to financial market risks, including changes in marketable equity security prices. We do not use derivative financial instruments to mitigate any of these risks.

Our investment performance is a function of our portfolio companies’ profitability, which may be affected by economic cycles, competitive forces, foreign currency fluctuations and production costs including labor rates, raw material prices and certain basic commodity prices. Most of the companies in our investment portfolio do not hedge their exposure to raw material and commodity price fluctuations. However, the portfolio company with the greatest exposure to foreign currency fluctuations generally hedges its exposure. All of these factors may have an adverse effect on the value of our investments and on our net asset value.

Our investment in portfolio securities includes fixed-rate debt securities which totaled \$2,605,000 at June 30, 2014, equivalent to 0.37% of the value of our total investments. Generally, these debt securities are below investment grade and have relatively high fixed rates of interest; therefore, minor changes in market yields of publicly traded debt securities have little or no effect on the values of debt securities in our portfolio and no effect on interest income. Our investments in debt securities are generally held to maturity and their fair values are determined on the basis of the terms of the debt security and the financial condition of the issuer.

A portion of our investment portfolio consists of debt and equity securities of private companies. We anticipate little or no effect on the values of these investments from modest changes in public market equity valuations. Should significant changes in market valuations of comparable publicly traded companies occur, there may be a corresponding effect on valuations of private companies, which would affect the value and the amount and timing of proceeds eventually realized from these investments. A portion of our investment portfolio also consists of unrestricted, freely marketable common stock of publicly traded companies. These freely marketable investments, which are valued at the public market price, are directly exposed to equity price risks because a change in an issuer’s public market equity price would result in an identical change in the value of our investment in such security.



#### **Item 4. Controls and Procedures**

As of the end of the period covered by this report, an evaluation was performed under the supervision and with the participation of our management, including the President and Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15 of the Securities Exchange Act of 1934). Based upon this evaluation, management, including our President and Chief Executive Officer and our Chief Financial Officer, have concluded that our current disclosure controls and procedures are effective as of June 30, 2014.

During the fiscal quarter ended June 30, 2014, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect our internal control over financial reporting.

### **PART II. – OTHER INFORMATION**

#### **Item 1. Legal Proceedings**

We may, from time to time, be involved in litigation arising out of our operations in the normal course of business or otherwise. Furthermore, third parties may try to seek to impose liability on us in connection with the activities of our portfolio companies. We have no current pending legal proceedings to which we are party or to which any of our assets is subject.

#### **Item 1A. Risk Factors**

There have been no material changes to our risk factors disclosed in Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014.

#### **Item 6. Exhibits**

<u>Exhibit No.</u>	<u>Description</u>
<a href="#">31.1</a>	Certification of President and Chief Executive Officer required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), filed herewith.
<a href="#">31.2</a>	Certification of Chief Financial Officer required by Rule 13a-14(a) of the Exchange Act, filed herewith.
<a href="#">32.1</a>	Certification of President and Chief Executive Officer required by Rule 13a-14(b) of the Exchange Act and Section 1350 of Chapter 63 of Title 18 of the United States Code, furnished herewith.
<a href="#">32.2</a>	Certification of Chief Financial Officer required by Rule 13a-14(b) of the Exchange Act and Section 1350 of Chapter 63 of Title 18 of the United States Code, furnished herewith.

**SIGNATURES**

Pursuant to the requirements the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**CAPITAL SOUTHWEST CORPORATION**

August 7, 2014

\_\_\_\_\_  
Date

By: /s/ Joseph B. Armes

\_\_\_\_\_  
Joseph B. Armes  
Chairman of the Board  
President and Chief Executive Officer

August 7, 2014

\_\_\_\_\_  
Date

By: /s/ Kelly Tacke

\_\_\_\_\_  
Kelly Tacke  
Chief Financial Officer

**CERTIFICATIONS**

I, Joseph B. Armes, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capital Southwest Corporation (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: August 7, 2014

By: /s/ Joseph B. Armes

Joseph B. Armes  
Chairman of the Board  
President and Chief Executive Officer

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## CERTIFICATIONS

I, Kelly Tacke, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Capital Southwest Corporation (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: August 7, 2014

By: /s/ Kelly Tacke  
Kelly Tacke  
Chief Financial Officer

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**Certification of the President and Chief Executive Officer  
Pursuant to 18 U.S.C. Section, as adopted pursuant to Section 906 of the  
Sarbanes-Oxley Act of 2002**

I, Joseph B. Armes, President and Chief Executive Officer of Capital Southwest Corporation, certify that, to my knowledge:

1. The Form 10-Q for the quarter ended June 30, 2014, filed with the Securities and Exchange Commission on August 7, 2014 (“accompanied report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the accompanied report fairly presents, in all material respects, the consolidated financial condition and results of operations of Capital Southwest Corporation.

Date: August 7, 2014

By: /s/ Joseph B. Armes  
Joseph B. Armes  
Chairman of the Board  
President and Chief Executive Officer

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**Certification of the Chief Financial Officer  
Pursuant to 18 U.S.C. Section, as adopted pursuant to Section 906 of the  
Sarbanes-Oxley Act of 2002**

I, Kelly Tacke, Chief Financial Officer of Capital Southwest Corporation, certify that, to my knowledge:

1. The Form 10-Q for the quarter ended June 30, 2014, filed with the Securities and Exchange Commission on August 7, 2014 (“accompanied report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the accompanied report fairly presents, in all material respects, the consolidated financial condition and results of operations of Capital Southwest Corporation.

Date: August 7, 2014

By: /s/ Kelly Tacke

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Kelly Tacke  
Chief Financial Officer

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