

PENNANTPARK INVESTMENT CORP  
Form 10-Q  
May 04, 2011  
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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 QUARTER ENDED MARCH 31, 2011

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: 814-00736

**PENNANTPARK INVESTMENT**  
**CORPORATION**

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(Exact name of registrant as specified in its charter)

|   |  |
|---|--|
| <b>MARYLAND</b><br>(State or other jurisdiction of<br>incorporation or organization)                                      | <b>20-8250744</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>590 Madison Avenue, 15<sup>th</sup> Floor</b><br><br><b>New York, N.Y.</b><br>(Address of principal executive offices) | <b>10022</b><br>(Zip Code)                                   |
| <b>(212)-905-1000</b><br>(Registrant's Telephone Number, Including Area Code)   |  |

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 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 files). Yes  No .

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

|  |   |
|--|---|
| Large accelerated filer <input type="checkbox"/>   | Accelerated filer <input checked="" type="checkbox"/> |
| Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company) | Smaller reporting company <input type="checkbox"/>    |

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

The number of shares of the issuer's common stock, \$0.001 par value, outstanding as of May 4, 2011 was 45,581,084.

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**PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES**

**FORM 10-Q**

**FOR THE QUARTER ENDED MARCH 31, 2011**

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**PART I CONSOLIDATED FINANCIAL INFORMATION**

We are filing this form 10-Q (the Report ) in compliance with Rule 13a-13 promulgated by the Securities and Exchange Commission ( SEC ). In this Report, we , our or us refer to PennantPark Investment Corporation and its consolidated subsidiaries unless the context suggests otherwise. References to PennantPark Investment refer to only PennantPark Investment Corporation. References to subsidiaries or our SBIC refer to PennantPark SBIC LP ( SBIC LP ) and its general partner PennantPark SBIC GP, LLC ( SBIC GP ), which are wholly owned and consolidated. References to our portfolio and investments include investments we make through subsidiaries.

**Table of Contents****Item 1. Consolidated Financial Statements****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES**

|   | March 31, 2011<br>(unaudited) | September 30, 2010    |
|---|-------------------------------|-----------------------|
| <b>Assets</b>   |                               |                       |
| Investments at fair value   |                               |                       |
| Non-controlled, non-affiliated investments, at fair value (cost \$698,256,084 and \$631,280,755, respectively)                                  | \$ 731,730,316                | \$ 641,290,626        |
| Non-controlled, affiliated investments, at fair value (cost \$17,875,050 and \$17,427,648, respectively)  | 15,919,916                    | 15,433,680            |
| Controlled, affiliated investments, at fair value (cost \$11,000,100 and 8,000,100, respectively)   | 11,000,000                    | 8,000,100             |
| Total of Investments, at fair value (cost \$727,131,234 and \$656,708,503, respectively)  | 758,650,232                   | 664,724,406           |
| Cash equivalents (See Note 8)   | 1,546,429                     | 1,814,451             |
| Interest receivable   | 11,576,869                    | 12,814,096            |
| Receivable for investments sold   |                               | 30,254,774            |
| Prepaid expenses and other assets   | 3,139,923                     | 1,886,119             |
| <b>Total assets</b>   | <b>774,913,453</b>            | <b>711,493,846</b>    |
| <b>Liabilities</b>  |                               |                       |
| Distributions payable   | 12,286,331                    | 9,401,281             |
| Payable for investments purchased   | 12,375,000                    | 52,785,000            |
| Unfunded investments  | 18,633,872                    | 22,203,434            |
| Credit facility payable (cost: \$152,838,800 and \$233,100,000, respectively)<br>(See Notes 5 and 10)   | 150,183,371                   | 219,141,125           |
| SBA debentures payable (See Note 10)  | 59,500,000                    | 14,500,000            |
| Interest payable on credit facility and SBA debentures  | 292,514                       | 215,135               |
| Management fee payable (See Note 3)   | 3,589,342                     | 3,286,816             |
| Performance-based incentive fee payable (See Note 3)  | 3,338,434                     | 2,239,011             |
| Accrued other expenses  | 694,751                       | 1,146,821             |
| <b>Total liabilities</b>  | <b>260,893,615</b>            | <b>324,918,623</b>    |
| <b>Net Assets</b>   |                               |                       |
| Common stock, par value \$0.001 per share, 100,000,000 shares authorized, 45,504,932 and 36,158,772 shares issued and outstanding, respectively | 45,505                        | 36,159                |
| Paid-in capital in excess of par value  | 538,546,978                   | 428,675,184           |
| Undistributed net investment income   | 4,584,659                     | 1,800,646             |
| Accumulated net realized loss on investments  | (63,331,731)                  | (65,911,544)          |
| Net unrealized appreciation on investments  | 31,518,998                    | 8,015,903             |
| Net unrealized depreciation on credit facility  | 2,655,429                     | 13,958,875            |
| <b>Total net assets</b>   | <b>\$ 514,019,838</b>         | <b>\$ 386,575,223</b> |
| <b>Total liabilities and net assets</b>   | <b>\$ 774,913,453</b>         | <b>\$ 711,493,846</b> |
| <b>Net asset value per share</b>  | <b>\$ 11.30</b>               | <b>\$ 10.69</b>       |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS



**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

|   | Three Months Ended March 31, |                       | Six Months Ended March 31, |                     |
|---|------------------------------|-----------------------|----------------------------|---------------------|
|   | 2011                         | 2010                  | 2011                       | 2010                |
| <b>Investment income:</b>   |                              |                       |                            |                     |
| From non-controlled, non-affiliated investments:  |                              |                       |                            |                     |
| Interest  | \$ 20,836,197                | \$ 12,783,931         | \$ 39,395,362              | \$ 25,735,164       |
| Other   | 1,233,863                    | 412,482               | 2,080,447                  | 732,085             |
| From non-controlled, affiliated investments:  |                              |                       |                            |                     |
| Interest  | 381,222                      | 328,580               | 744,654                    | 656,229             |
| From controlled, affiliated investments:  |                              |                       |                            |                     |
| Interest  | 260,167                      |                       | 470,167                    |                     |
| <b>Total investment income</b>  | <b>22,711,449</b>            | <b>13,524,993</b>     | <b>42,690,630</b>          | <b>27,123,478</b>   |
| <b>Expenses:</b>  |                              |                       |                            |                     |
| Base management fee (See Note 3)  | 3,589,342                    | 2,772,132             | 7,087,936                  | 5,296,785           |
| Performance-based incentive fee (See Note 3)  | 3,338,434                    | 1,764,607             | 6,131,428                  | 3,573,987           |
| Interest and expenses on the credit facility and SBA debentures (See Note 10)                 | 1,086,523                    | 838,275               | 2,221,950                  | 1,656,958           |
| Administrative services expenses (See Note 3)   | 650,662                      | 539,619               | 1,229,717                  | 1,097,123           |
| Other general and administrative expenses   | 847,668                      | 560,974               | 1,531,027                  | 1,104,389           |
| <b>Expenses before taxes</b>  | <b>9,512,629</b>             | <b>6,475,607</b>      | <b>18,202,058</b>          | <b>12,729,242</b>   |
| Excise tax (See Note 2)   | 39,857                       | (9,072)               | 158,824                    | 97,890              |
| <b>Total expenses</b>   | <b>9,552,486</b>             | <b>6,466,535</b>      | <b>18,360,882</b>          | <b>12,827,132</b>   |
| <b>Net investment income</b>  | <b>13,158,963</b>            | <b>7,058,458</b>      | <b>24,329,748</b>          | <b>14,296,346</b>   |
| <b>Realized and unrealized gain (loss) on investments and credit facility:</b>                |                              |                       |                            |                     |
| Net realized gain (loss) on non-controlled, non-affiliated investments                        | 286,452                      | (140,986)             | 2,579,813                  | (16,744,851)        |
| Net change in unrealized appreciation (depreciation) on:                                      |                              |                       |                            |                     |
| Non-controlled, non-affiliated investments  | 4,711,487                    | 9,895,674             | 23,464,360                 | 33,989,336          |
| Non-controlled, affiliated investments  | 129,006                      | 8,425                 | 38,835                     | (204,099)           |
| Controlled, affiliated investments  | (100)                        |                       | (100)                      |                     |
| Credit facility unrealized (appreciation) (See Note 5)  | (4,698,821)                  | (19,852,714)          | (11,303,446)               | (25,691,628)        |
| <b>Net change in unrealized appreciation (depreciation)</b>                                   | <b>141,572</b>               | <b>(9,948,615)</b>    | <b>12,199,649</b>          | <b>8,093,609</b>    |
| Net realized and unrealized gain (loss) from investments and credit facility                  | 428,024                      | (10,089,601)          | 14,779,462                 | (8,651,242)         |
| <b>Net increase (decrease) in net assets resulting from operations</b>                        | <b>\$ 13,586,987</b>         | <b>\$ (3,031,143)</b> | <b>\$ 39,109,210</b>       | <b>\$ 5,645,104</b> |
| Net increase (decrease) in net assets resulting from operations per common share (See Note 7) | \$ 0.33                      | \$ (0.11)             | \$ 1.01                    | \$ 0.21             |

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|  |    |      |    |      |    |      |    |      |
|--|----|------|----|------|----|------|----|------|
| Net investment income per common share | \$ | 0.32 | \$ | 0.26 | \$ | 0.63 | \$ | 0.54 |
|--|----|------|----|------|----|------|----|------|

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS



**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS****(Unaudited)**

|   | <b>Six Months Ended March 31,</b> |                   |
|---|-----------------------------------|-------------------|
|   | <b>2011</b>                       | <b>2010</b>       |
| <b>Increase in net assets from operations:</b>              |                                   |                   |
| Net investment income                                       | \$ 24,329,748                     | \$ 14,296,346     |
| Net realized gain (loss) on investments                     | 2,579,813                         | (16,744,851)      |
| Net change in unrealized appreciation on investments        | 23,503,095                        | 33,785,237        |
| Net change in unrealized (appreciation) on credit facility  | (11,303,446)                      | (25,691,628)      |
| <b>Net increase in net assets resulting from operations</b> | <b>39,109,210</b>                 | <b>5,645,104</b>  |
| <b>Distributions to Stockholders:</b>                       |                                   |                   |
| Distributions from net investment income                    | (21,704,559)                      | (14,657,474)      |
| <b>Capital Share Transactions:</b>                          |                                   |                   |
| Public offering   | 114,080,000                       | 61,020,000        |
| Offering costs relating to public offering                  | (5,743,800)                       | (3,376,000)       |
| Reinvestment of dividends                                   | 1,703,764                         |                   |
| <b>Total increase in net assets</b>                         | <b>127,444,615</b>                | <b>48,631,630</b> |
| <b>Net Assets:</b>  |                                   |                   |
| Beginning of period   | 386,575,223                       | 300,580,268       |
| End of period   | \$ 514,019,838                    | \$ 349,211,898    |
| Undistributed net investment income, end of period          | 4,584,659                         | 1,626,997         |
| <b>Capital Share Activity:</b>                              |                                   |                   |
| Public offering   | 9,200,000                         | 6,190,000         |
| Reinvestment of dividends                                   | 146,160                           |                   |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

|  | <b>Six Months Ended March 31,</b> |                       |
|--|-----------------------------------|-----------------------|
|  | <b>2011</b>                       | <b>2010</b>           |
| <b>Cash flows from operating activities:</b>   |                                   |                       |
| Net increase in net assets resulting from operations   | \$ 39,109,210                     | \$ 5,645,104          |
| Adjustments to reconcile net increase in net assets resulting from operations to net cash used for operating activities: |                                   |                       |
| Net change in unrealized appreciation on investments   | (23,503,095)                      | (33,785,237)          |
| Net change in unrealized appreciation on credit facility   | 11,303,446                        | 25,691,628            |
| Net realized (gain) loss on investments  | (2,579,813)                       | 16,744,851            |
| Net accretion of discount and amortization of premium  | (3,219,842)                       | (2,000,365)           |
| Purchase of investments  | (196,549,024)                     | (119,033,410)         |
| Payment-in-kind interest   | (5,181,586)                       | (3,354,193)           |
| Proceeds from dispositions of investments  | 137,107,533                       | 23,491,075            |
| Decrease (Increase) in interest receivable   | 1,237,227                         | (2,564,187)           |
| Decrease (Increase) in receivable for investments sold   | 30,254,774                        | (2,136,493)           |
| Decrease in prepaid expenses and other assets  | 502,446                           | 320,321               |
| (Decrease) Increase in payable for investments purchased   | (40,410,000)                      | 5,010,475             |
| (Decrease) Increase in unfunded investments  | (3,569,562)                       | 7,010,744             |
| Increase (Decrease) in interest payable on credit facility and SBA debentures  | 77,379                            | (21,337)              |
| Increase in management fee payable   | 302,526                           | 552,096               |
| Increase in performance-based incentive fee payable  | 1,099,423                         | 256,428               |
| (Decrease) in accrued expenses   | (452,070)                         | (675,898)             |
| <br>Net cash used for operating activities   | <br>(54,471,028)                  | <br>(78,848,398)      |
| <b>Cash flows from financing activities:</b>   |                                   |                       |
| Public offering  | 114,080,000                       | 61,020,000            |
| Offering costs related to public offering  | (5,743,800)                       | (3,376,000)           |
| Distributions paid to stockholders, net of dividends reinvested  | (17,115,744)                      | (11,508,698)          |
| Borrowings under SBA debentures (See Note 10)  | 45,000,000                        |                       |
| Capitalized borrowing costs  | (1,756,250)                       |                       |
| Borrowings under credit facility (See Note 10)   | 200,300,000                       | 116,000,000           |
| Repayments under credit facility (See Note 10)   | (280,561,200)                     | (115,600,000)         |
| <br>Net cash provided by financing activities  | <br>54,203,006                    | <br>46,535,302        |
| <br><b>Net decrease in cash equivalents</b>  | <br>(268,022)                     | <br>(32,313,096)      |
| <b>Cash equivalents, beginning of period</b>   | <b>1,814,451</b>                  | <b>33,247,666</b>     |
| <br><b>Cash equivalents, end of period</b>   | <br><b>\$ 1,546,429</b>           | <br><b>\$ 934,570</b> |
| <b>Supplemental disclosure of cash flow information and non-cash financing activity (See Note 5):</b>                    |                                   |                       |
| Interest paid  | \$ 1,826,073                      | \$ 1,545,142          |
| Income taxes paid  | \$ 123,824                        | \$ 97,890             |
| Dividends reinvested   | \$ 1,703,764                      | \$                    |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS



**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS****MARCH 31, 2011****(Unaudited)**

| <b>Issuer Name</b>   | <b>Maturity</b> | <b>Industry</b>   | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>        | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|-----------------------|---|---------------------|--------------------|---------------------------------|
| <b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies</b> |                 |   | <b>142.4</b>          | <b>0<sup>(1)</sup>,<sup>(2)</sup></b>         |                     |                    |                                 |
| <b>First Lien Secured Debt 57.5%</b>                                     |                 |   |                       |   |                     |                    |                                 |
| Affinity Group Holdings, Inc. <sup>(5)</sup>                             | 12/01/2016      | Consumer Products   | 11.50%                |   | \$ 12,000,000       | \$ 11,758,305      | \$ 12,600,000                   |
| American Surgical Holdings, Inc.   | 03/23/2015      | Healthcare, Education and Childcare                                   | 14.00%                | L+1,000 <sup>(8)</sup>                        | 21,000,000          | 20,371,820         | 20,370,000                      |
| Birch Communications, Inc.   | 06/21/2015      | Telecommunications  | 15.00%                | L+1,300 <sup>(8)</sup>                        | 20,000,000          | 19,465,255         | 20,200,000                      |
| CEVA Group PLC <sup>(5),(10)</sup>                                       | 10/01/2016      | Logistics   | 11.63%                |   | 7,500,000           | 7,316,405          | 8,250,000                       |
| CEVA Group PLC <sup>(5),(10)</sup>                                       | 04/01/2018      | Logistics   | 11.50%                |   | 1,000,000           | 988,304            | 1,086,250                       |
| Chester Downs and Marina, LLC  | 07/31/2016      | Hotels, Motels, Inns and Gaming                                       | 12.38%                | L+988 <sup>(8)</sup>                          | 8,875,000           | 8,440,033          | 9,141,250                       |
| Columbus International, Inc. <sup>(5),(10)</sup>                         | 11/20/2014      | Communications  | 11.50%                |   | 10,000,000          | 10,000,000         | 11,525,000                      |
| Covad Communications Group, Inc. <sup>(5)</sup>                          | 11/03/2015      | Telecommunications  | 12.00%                | L+1,000 <sup>(8)</sup>                        | 6,825,000           | 6,696,339          | 6,876,188                       |
| EnviroSolutions, Inc. <sup>(9)</sup>                                     | 07/29/2013      | Environmental Services  |                       |   | 6,666,666           | 6,666,666          | 6,666,666                       |
| Hanley-Wood, L.L.C.  | 03/08/2014      | Other Media   | 2.63%                 | L+225   | 8,707,500           | 8,707,500          | 4,702,050                       |
| Instant Web, Inc.  | 08/07/2014      | Printing and Publishing   | 14.50%                | L+950 <sup>(8)</sup>                          | 24,750,000          | 24,310,573         | 25,987,500                      |
| Jacuzzi Brands Corp.   | 02/07/2014      | Home and Office Furnishings, Housewares and Durable Consumer Products | 2.56%                 | L+225   | 9,708,108           | 9,708,108          | 8,227,622                       |
| K2 Pure Solutions NoCal, L.P.  | 09/10/2015      | Chemicals, Plastics and Rubber  | 10.00%                | P+675 <sup>(8)</sup>                          | 18,952,500          | 17,914,550         | 18,952,500                      |
| Learning Care Group, Inc.  | 04/27/2016      | Education   | 12.00%                |   | 26,052,632          | 25,520,274         | 26,052,631                      |
| Penton Media, Inc.   | 08/01/2014      | Other Media   | 5.00% <sup>(6)</sup>  | L+400 <sup>(8)</sup>                          | 33,331,117          | 27,879,932         | 26,720,456                      |
| Questex Media Group LLC <sup>(9)</sup>                                   | 12/16/2012      | Other Media   |                       |   | 267,205             | 267,205            | 261,060                         |
| Sugarhouse HSP Gaming Prop.  | 09/23/2014      | Hotels, Motels, Inns and Gaming                                       | 11.25%                | L+825 <sup>(8)</sup>                          | 29,352,500          | 28,672,202         | 29,756,097                      |
| Survey Sampling International, L.L.C.                                    | 12/31/2012      | Business Services   | 10.65% <sup>(6)</sup> | L+650 <sup>(8)</sup>                          | 4,489,615           | 3,518,960          | 3,501,900                       |
| Three Rivers Pharmaceutical, L.L.C.                                      | 10/22/2012      | Healthcare, Education and Childcare                                   | 15.00%                | L+1,300 <sup>(8)</sup>                        | 30,000,000          | 28,309,372         | 31,800,000                      |
| VPSI, Inc.   | 12/22/2015      | Personal Transportation   | 12.00%                | L+1,000 <sup>(8)</sup>                        | 17,989,583          | 17,701,158         | 17,989,583                      |
| Yonkers Racing Corp. <sup>(5)</sup>                                      | 07/15/2016      | Hotels, Motels, Inns and Gaming                                       | 11.38%                |   | 4,500,000           | 4,386,421          | 5,006,250                       |
| <b>Total First Lien Secured Debt</b>                                     |                 |   |                       |   |                     | <b>288,599,382</b> | <b>295,673,003</b>              |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

| <b>Issuer Name</b>                             | <b>Maturity</b> | <b>Industry</b>   | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>   | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|-----------------------|---|---------------------|---------------|---------------------------------|
| <b>Second Lien Secured Debt 26.0%</b>          |                 |   |                       |   |                     |               |                                 |
| Brand Energy and Infrastructure Services, Inc. | 02/07/2015      | Energy/Utilities  | 6.31%                 | L+600   | \$ 13,600,000       | \$ 13,247,258 | \$ 12,648,000                   |
| Brand Energy and Infrastructure Services, Inc. | 02/07/2015      | Energy/Utilities  | 7.31%                 | L+700   | 12,000,000          | 11,793,689    | 11,497,500                      |
| DirectBuy Holdings, Inc. <sup>(5)</sup>        | 02/01/2017      | Consumer Products   | 12.00%                |   | 34,000,000          | 31,824,243    | 25,840,000                      |
| EnviroSolutions, Inc.                          | 07/29/2014      | Environmental Services  | 8.00%                 | L+600 <sup>(8)</sup>                          | 6,237,317           | 6,237,317     | 6,237,317                       |
| Greatwide Logistics Services, L.L.C.           | 03/01/2014      | Cargo Transport   | 11.00% <sup>(6)</sup> | L+700 <sup>(8)</sup>                          | 2,711,726           | 2,711,727     | 2,738,843                       |
| Questex Media Group LLC, Term Loan A           | 12/15/2014      | Other Media   | 9.50%                 | L+650 <sup>(8)</sup>                          | 3,094,979           | 3,094,979     | 2,698,822                       |
| Questex Media Group LLC, Term Loan B           | 12/15/2015      | Other Media   | 11.50% <sup>(6)</sup> | L+750 <sup>(8)</sup>                          | 1,879,375           | 1,879,375     | 1,578,675                       |
| RAM Energy Resources, Inc.                     | 09/13/2016      | Oil and Gas   | 11.00%                | L+900 <sup>(8)</sup>                          | 17,000,000          | 16,662,330    | 16,660,000                      |
| Realogy Corp.                                  | 10/15/2017      | Buildings and Real Estate   | 13.50%                |   | 10,000,000          | 10,000,000    | 10,825,000                      |
| Sheridan Holdings, Inc.                        | 06/15/2015      | Healthcare, Education and Childcare                                   | 6.06% <sup>(6)</sup>  | L+575   | 13,500,000          | 11,686,995    | 13,162,500                      |
| Specialized Technology Resources, Inc.         | 12/15/2014      | Chemicals, Plastics and Rubber  | 7.25% <sup>(6)</sup>  | L+700   | 22,500,000          | 22,491,157    | 22,500,000                      |
| TransFirst Holdings, Inc.                      | 06/15/2015      | Financial Services  | 6.31% <sup>(6)</sup>  | L+600   | 7,811,488           | 7,383,586     | 7,342,799                       |
| <b>Total Second Lien Secured Debt</b>          |                 |   |                       |   |                     | 139,012,656   | 133,729,456                     |
| <b>Subordinated Debt/Corporate Notes 47.1%</b> |                 |   |                       |   |                     |               |                                 |
| Affinion Group Holdings, Inc. <sup>(5)</sup>   | 11/15/2015      | Consumer Products   | 11.63%                |   | 10,000,000          | 9,868,722     | 10,175,000                      |
| Aquilex Holdings, LLC <sup>(5)</sup>           | 12/15/2016      | Diversified / Conglomerate Services                                   | 11.13%                |   | 18,885,000          | 18,409,596    | 19,947,281                      |
| Consolidated Foundries, Inc.                   | 04/17/2015      | Aerospace and Defense   | 14.25% <sup>(6)</sup> |   | 8,109,468           | 7,982,866     | 8,231,110                       |
| Da-Lite Screen Company, Inc. <sup>(5)</sup>    | 04/01/2015      | Home and Office Furnishings, Housewares and Durable Consumer Products | 12.50%                |   | 25,000,000          | 24,432,431    | 27,093,750                      |
| Escort Inc.                                    | 06/01/2016      | Electronics   | 14.75% <sup>(6)</sup> |   | 24,220,378          | 23,583,273    | 24,220,378                      |
| i2 Holdings Ltd. <sup>(10)</sup>               | 06/06/2014      | Aerospace and Defense   | 14.75% <sup>(6)</sup> |   | 23,607,187          | 23,337,934    | 23,607,187                      |
| Learning Care Group (US) Inc.                  | 06/30/2016      | Education   | 15.00% <sup>(6)</sup> |   | 4,248,355           | 3,532,698     | 3,919,108                       |
| MailSouth, Inc.                                | 05/15/2018      | Printing and Publishing   | 14.50%                |   | 15,000,000          | 14,558,633    | 15,000,000                      |
| MedQuist, Inc.                                 | 10/15/2016      | Business Services   | 13.00% <sup>(6)</sup> |   | 19,000,000          | 18,458,388    | 19,190,000                      |
| PAS Technologies, Inc.                         | 05/12/2017      | Aerospace and Defense   | 14.02% <sup>(6)</sup> |   | 16,785,000          | 16,378,606    | 16,785,000                      |
| Realogy Corp.                                  | 04/15/2018      | Buildings and Real Estate   | 11.00%                |   | 10,000,000          | 9,117,736     | 10,900,000                      |
| TRAK Acquisition Corp.                         | 12/29/2015      | Business Services   | 15.00% <sup>(6)</sup> |   | 11,869,628          | 11,524,231    | 11,822,149                      |
| UP Support Services, Inc.                      | 02/08/2015      | Oil and Gas   | 17.00% <sup>(6)</sup> |   | 24,061,922          | 23,708,609    | 24,061,922                      |
| Veritext Corp.                                 | 12/31/2015      | Business Services   | 14.00% <sup>(6)</sup> |   | 15,000,000          | 14,660,342    | 15,000,000                      |
| Veritext Corp. <sup>(9)</sup>                  | 12/31/2012      | Business Services   |                       |   | 12,000,000          | 11,700,000    | 12,000,000                      |
| <b>Total Subordinated Debt/Corporate Notes</b> |                 |   |                       |   |                     | 231,254,065   | 241,952,885                     |



**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

| <b>Issuer Name</b>  | <b>Maturity</b> | <b>Industry</b>                        | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>       | <b>Fair Value<sup>(3)</sup></b> |
|---|-----------------|--|-----------------------|---|---------------------|-------------------|---------------------------------|
| <b>Preferred Equity Partnership Interests 2.8%</b>                                |                 |  |                       |   |                     |                   |                                 |
| AH Holdings, Inc.<br>(American Surgical Holdings, Inc.)                           |                 | Healthcare, Education and<br>Childcare | 6.00%                 |   | 211                 | \$ 500,000        | \$ 500,750                      |
| AHC Mezzanine, LLC<br>(Advanstar Inc.)  |                 | Other Media                            |                       |   | 319                 | 318,896           |                                 |
| CFHC Holdings, Inc., Class A<br>(Consolidated Foundries, Inc.)                    |                 | Aerospace and Defense                  | 12.00%                |   | 909                 | 909,248           | 1,245,661                       |
| i2 Holdings Ltd. <sup>(10)</sup>  |                 | Aerospace and Defense                  | 12.00%                |   | 4,137,240           | 4,137,240         | 5,681,642                       |
| PAS Tech Holdings, Inc. Series<br>A-1   |                 | Aerospace and Defense                  | 8.00%                 |   | 20,000              | 1,980,000         | 2,040,709                       |
| TZ Holdings, L.P., Series A<br>(Trizetto Group, Inc.)                             |                 | Insurance                              |                       |   | 686                 | 685,820           | 685,820                         |
| TZ Holdings, L.P., Series B<br>(Trizetto Group, Inc.)                             |                 | Insurance                              | 6.50%                 |   | 1,312               | 1,312,006         | 1,538,408                       |
| Universal Pegasus International,<br>Inc.<br>(UP Support Services, Inc.)           |                 | Oil and Gas                            | 8.00%                 |   | 101,175             | 2,738,050         | 961,017                         |
| Verde Parent Holdings, Inc.<br>(VPSI, Inc.)                                       |                 | Personal Transportation                | 8.00%                 |   | 1,824,167           | 1,824,167         | 1,804,391                       |
| <b>Total Preferred Equity/Partnership Interests</b>                               |                 |  |                       |   |                     | <b>14,405,427</b> | <b>14,458,398</b>               |
| <b>Common Equity/ Warrants/Partnership Interests 9.0%</b>                         |                 |  |                       |   |                     |                   |                                 |
| AH Holdings, Inc.<br>(American Surgical Holdings, Inc.)<br>(Warrants)             | 03/23/2021      | Healthcare, Education and<br>Childcare |                       |   | 753                 |                   |                                 |
| CEA Autumn Management, L.L.C.   |                 | Broadcasting and<br>Entertainment      |                       |   | 1,333               | 3,000,000         | 3,000,000                       |
| CFHC Holdings, Inc.<br>(Consolidated Foundries, Inc.)                             |                 | Aerospace and Defense                  |                       |   | 1,856               | 18,556            | 531,427                         |
| CT Technologies Holdings, LLC<br>(CT Technologies Intermediate<br>Holdings, Inc.) |                 | Business Services                      |                       |   | 5,556               | 2,580,158         | 7,446,464                       |
| DirectBuy Investors L.P.<br>(DirectBuy Holdings, Inc.)                            |                 | Consumer Products                      |                       |   | 30,000              | 1,350,000         | 1,350,000                       |
| EnviroSolutions, Inc.   |                 | Environmental Services                 |                       |   | 24,375              | 1,506,075         | 2,170,935                       |
| EnviroSolutions, Inc.<br>(Warrants)   |                 | Environmental Services                 |                       |   | 49,005              | 3,027,906         | 4,364,091                       |
| i2 Holdings Ltd. <sup>(10)</sup>  |                 | Aerospace and Defense                  |                       |   | 457,322             | 454,030           | 148,032                         |
| Kadmon Holdings, L. L.C., Class<br>A<br>(Three Rivers Pharmaceutical,<br>L.L.C.)  |                 | Healthcare, Education and<br>Childcare |                       |   | 10,799              | 1,236,832         | 1,805,212                       |
| Kadmon Holdings, L.L.C., Class D<br>(Three Rivers Pharmaceutical,<br>L.L.C.)      |                 | Healthcare, Education and<br>Childcare |                       |   | 10,799              | 1,028,807         | 1,028,807                       |
|   | 04/27/2020      | Education                              |                       |   | 1,267               | 779,920           | 407,499                         |

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|  |            |                         |           |                |                |
|--|------------|-------------------------|-----------|----------------|----------------|
| Learning Care Group (US) Inc. (Warrants )                                |            |                         |           |                |                |
| Magnum Hunter Resources Corporation                                      |            | Oil and Gas             | 1,055,932 | 2,464,999      | 9,049,337      |
| PAS Tech Holdings, Inc.  |            | Aerospace and Defense   | 20,000    | 20,000         | 261,064        |
| QMG HoldCo, LLC, Class A (Questex Media Group, Inc.)                     |            | Other Media             | 4,325     | 1,306,167      | 1,370,149      |
| QMG HoldCo, LLC, Class B (Questex Media Group, Inc.)                     |            | Other Media             | 531       |                | 168,219        |
| TRAK Acquisition Corp. (Warrants)  | 12/29/2019 | Business Services       | 3,500     | 29,400         | 427,922        |
| Transportation 100 Holdco, L.L.C. (Greatwide Logistics Services, L.L.C.) |            | Cargo Transport         | 137,923   | 2,111,588      | 4,842,886      |
| TZ Holdings, L.P. (Trizetto Group, Inc.)                                 |            | Insurance               | 2         | 9,843          | 1,397,025      |
| Universal Pegasus International, Inc. (UP Support Services, Inc.)        |            | Oil and Gas             | 110,742   | 1,107          |                |
| Verde Parent Holdings, Inc. (VPSI, Inc.)                                 |            | Personal Transportation | 9,166     | 9,166          |                |
| VText Holdings, Inc. (Veritext Corp.)                                    |            | Business Services       | 35,526    | 4,050,000      | 6,147,505      |
| <b>Total Common Equity/Warrants/Partnership Interests</b>                |            |                         |           | 24,984,554     | 45,916,574     |
| <b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies</b> |            |                         |           | \$ 698,256,084 | \$ 731,730,316 |

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**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

| <b>Issuer Name</b>   | <b>Maturity</b> | <b>Industry</b>   | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>    | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|-----------------------|---|---------------------|----------------|---------------------------------|
| <b>Investments in Non-Controlled, Affiliated Portfolio Companies 3.1%</b> <sup>(1),(2)</sup> |                 |   |                       |   |                     |                |                                 |
| <b>Second Lien Secured Debt 1.5%</b>   |                 |   |                       |   |                     |                |                                 |
| Performance, Inc.<br>(Performance Holdings, Inc.)  | 01/16/2015      | Leisure, Amusement,<br>Motion Pictures and<br>Entertainment | 7.25%                 | L+625 <sup>(8)</sup>                          | \$ 8,000,000        | \$ 8,000,000   | \$ 7,748,000                    |
| <b>Subordinated Debt/Corporate Notes 1.2%</b>  |                 |   |                       |   |                     |                |                                 |
| Performance Holdings, Inc.   | 07/16/2015      | Leisure, Amusement,<br>Motion Pictures and<br>Entertainment | 15.00% <sup>(6)</sup> |   | 6,295,013           | 6,125,050      | 6,200,588                       |
| <b>Common Equity/Partnership Interest 0.4%</b>   |                 |   |                       |   |                     |                |                                 |
| NCP-Performance<br>(Performance Holdings, Inc.)  |                 | Leisure, Amusement,<br>Motion Pictures and<br>Entertainment |                       |   | 37,500              | 3,750,000      | 1,971,328                       |
| <b>Investments in Non-Controlled, Affiliated Portfolio Companies</b>                         |                 |   |                       |   |                     | 17,875,050     | 15,919,916                      |
| <b>Investments in Controlled, Affiliated Portfolio Companies 2.1%</b> <sup>(1),(2)</sup>     |                 |   |                       |   |                     |                |                                 |
| <b>First Lien Secured Debt 1.6%</b>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  | 06/30/2020      | Business Services   | 14.00% <sup>(6)</sup> |   | 7,200,000           | 7,200,000      | 7,998,020                       |
| <b>Subordinated Debt/Corporate Notes 0.3%</b>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  | 06/30/2020      | Business Services   | 14.00% <sup>(6)</sup> |   | 1,800,000           | 1,800,000      | 1,710,734                       |
| <b>Preferred Equity 0.2%</b>   |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  |                 | Business Services   | 14.00%                |   | 2,000               | 2,000,000      | 1,291,246                       |
| <b>Common Equity 0.0%</b>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  |                 | Business Services   |                       |   | 100                 | 100            |                                 |
| <b>Investments in Controlled, Affiliated Portfolio Companies</b>                             |                 |   |                       |   |                     | 11,000,100     | 11,000,000                      |
| <b>Total Investments 147.6%</b>  |                 |   |                       |   |                     | 727,131,234    | 758,650,232                     |
| <b>Cash Equivalents 0.3%</b>   |                 |   |                       |   |                     | 1,546,429      | 1,546,429                       |
| <b>Total Investments and Cash Equivalents 147.9%</b>   |                 |   |                       |   |                     | \$ 728,677,663 | \$ 760,196,661                  |

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|  |                |
|--|----------------|
| <b>Liabilities in Excess of Other Assets</b> (47.9%) | (246,176,823)  |
| <b>Net Assets</b> 100.0%                             | \$ 514,019,838 |

- (1) The provisions of the 1940 Act classify investments based on the level of control that we maintain in a particular portfolio company. As defined in the 1940 Act, a company is deemed as non-controlled when we own less than 25% of a portfolio company's voting securities and controlled when we own 25% or more of a portfolio company's voting securities.
- (2) The provisions of the 1940 Act classify investments further based on the level of ownership that we maintain in a particular portfolio company. As defined in the 1940 Act, a company is deemed as non-affiliated when we own less than 5% of a portfolio company's voting securities and affiliated when we own 5% or more of a portfolio company's voting securities.
- (3) Valued based on our accounting policy (see Note 2 to our consolidated financial statements).
- (4) Represents floating rate instruments that accrue interest at a predetermined spread relative to an index, typically the applicable London Interbank Offer Rate (LIBOR or L ) or Prime Rate (Prime or P ).
- (5) Security is exempt from registration under Rule 144A promulgated under the Securities Act of 1933. The security may be resold in transactions that are exempt from registration, usually to qualified institutional buyers.
- (6) Coupon is payable in cash and/or payable in-kind ( PIK ).
- (7) Non-income producing securities.
- (8) Coupon is subject to a LIBOR or a Prime rate floor or cap, as applicable.
- (9) Represents the purchase of a security with delayed settlement (unfunded investment). This security does not have a basis point spread above an index.
- (10) Non-U.S. company or principal place of business outside the United States.

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| <b>Issuer Name</b>   | <b>Maturity</b> | <b>Industry</b>   | <b>Current Coupon</b>        | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>   | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|------------------------------|---|---------------------|---------------|---------------------------------|
| <b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies</b> |                 |   | <b>165.9%</b> <sup>(2)</sup> |   |                     |               |                                 |
| <b>First Lien Secured Debt</b>   |                 |   |                              |   |                     |               |                                 |
| <b>59.3%</b>   |                 |   |                              |   |                     |               |                                 |
| Airvana Networks Solution, Inc.  | 08/27/2014      | Communications  | 11.00%                       | L+900 <sup>(8)</sup>                          | \$ 13,583,333       | \$ 13,316,337 | \$ 13,447,500                   |
| Birch Communications, Inc.   | 06/21/2015      | Telecommunications  | 15.00%                       | L+1,300 <sup>(8)</sup>                        | 16,363,636          | 15,786,257    | 16,363,636                      |
| Birch Communications, Inc.   | 01/31/2011      | Telecommunications  |                              |   | 3,636,364           | 3,636,364     | 3,636,364                       |
| CEVA Group PLC <sup>(5),(10)</sup>                                       | 10/01/2016      | Logistics   | 11.63%                       |   | 7,500,000           | 7,305,603     | 7,912,500                       |
| CEVA Group PLC <sup>(5),(10)</sup>                                       | 04/01/2018      | Logistics   | 11.50%                       |   | 1,000,000           | 987,774       | 1,045,000                       |
| Chester Downs and Marina, LLC  | 07/31/2016      | Hotels, Motels, Inns and Gaming                                       | 12.38%                       | L+988 <sup>(8)</sup>                          | 9,250,000           | 8,765,468     | 9,296,250                       |
| Columbus International, Inc. <sup>(5),(10)</sup>                         | 11/20/2014      | Communications  | 11.50%                       |   | 10,000,000          | 10,000,000    | 11,048,000                      |
| EnviroSolutions, Inc. <sup>(9)</sup>                                     | 07/29/2013      | Environmental Services  |                              |   | 6,666,666           | 6,666,666     | 6,666,666                       |
| Fairway Group Acquisition Company  | 10/01/2014      | Grocery   | 12.00%                       | L+950 <sup>(8)</sup>                          | 11,905,025          | 11,650,744    | 11,845,500                      |
| Hanley-Wood, L.L.C.  | 03/08/2014      | Other Media   | 2.62%                        | L+225   | 8,752,500           | 8,752,500     | 3,894,863                       |
| Instant Web, Inc.  | 08/07/2014      | Printing and Publishing   | 14.50%                       | L+950 <sup>(8)</sup>                          | 24,875,000          | 24,402,321    | 24,875,000                      |
| Jacuzzi Brands Corp.   | 02/07/2014      | Home and Office Furnishings, Housewares and Durable Consumer Products | 2.71%                        | L+225   | 9,744,595           | 9,744,595     | 7,874,850                       |
| K2 Pure Solutions NoCal, L.P.  | 09/10/2015      | Chemicals, Plastics and Rubber  | 10.00%                       | L+675 <sup>(8)</sup>                          | 19,000,000          | 17,866,826    | 18,240,000                      |
| Learning Care Group, Inc.  | 04/27/2016      | Education   | 12.00%                       |   | 26,052,631          | 25,481,512    | 26,052,631                      |
| Mattress Holding, Corp.  | 01/18/2014      | Home and Office Furnishings, Housewares and Durable Consumer Products | 2.54%                        |   | 3,844,931           | 3,844,931     | 3,345,090                       |
| Penton Media, Inc.   | 08/01/2014      | Other Media   | 5.00% <sup>(6)</sup>         | L+400 <sup>(8)</sup>                          | 9,829,738           | 8,432,037     | 6,995,500                       |
| Questex Media Group LLC  | 12/16/2012      | Other Media   | 10.50%                       | L+650 <sup>(8)</sup>                          | 66,801              | 66,801        | 64,263                          |
| Questex Media Group LLC <sup>(9)</sup>                                   | 12/16/2012      | Other Media   |                              |   | 200,404             | 200,404       | 192,789                         |
| Sugarhouse HSP Gaming Prop.  | 09/23/2014      | Hotels, Motels, Inns and Gaming                                       | 11.25%                       | L+825 <sup>(8)</sup>                          | 29,500,000          | 28,756,343    | 29,702,813                      |
| Three Rivers Pharmaceutical, L.L.C.                                      | 10/22/2011      | Healthcare, Education and Childcare                                   | 15.25%                       | L+1,300 <sup>(8)</sup>                        | 25,000,000          | 21,861,968    | 21,861,968                      |
|  |                 |   |                              | P+1,200                                       |                     |               |                                 |
| Yonkers Racing Corp. <sup>(5)</sup>                                      | 07/15/2016      | Hotels, Motels, Inns and Gaming                                       | 11.38%                       |   | 4,500,000           | 4,381,967     | 4,882,500                       |
| <b>Total First Lien Secured Debt</b>                                     |                 |   |                              |   |                     | 231,907,418   | 229,243,683                     |

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**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****SEPTEMBER 30, 2010**

| <b>Issuer Name</b>                             | <b>Maturity</b> | <b>Industry</b>   | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>        | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|-----------------------|---|---------------------|--------------------|---------------------------------|
| <b>Second Lien Secured Debt</b>                |                 |   |                       |   |                     |                    |                                 |
| <b>38.6 %</b>                                  |                 |   |                       |   |                     |                    |                                 |
| Brand Energy and Infrastructure Services, Inc. | 02/07/2015      | Energy/Utilities  | 6.43%                 | L+600   | \$ 13,600,000       | \$ 13,216,845      | \$ 11,696,000                   |
| Brand Energy and Infrastructure Services, Inc. | 02/07/2015      | Energy/Utilities  | 7.39%                 | L+700   | 12,000,000          | 11,776,589         | 10,410,000                      |
| EnviroSolutions, Inc.                          | 07/29/2014      | Environmental Services  | 8.00%                 | L+600 <sup>(8)</sup>                          | 6,237,317           | 6,237,317          | 5,950,400                       |
| Generics International (U.S.), Inc.            | 04/30/2015      | Healthcare, Education and Childcare                                   | 7.79%                 | L+750   | 12,000,000          | 11,958,469         | 11,940,000                      |
| Greatwide Logistics Services, L.L.C.           | 03/01/2014      | Cargo Transport   | 11.00% <sup>(6)</sup> | L+700 <sup>(8)</sup>                          | 2,570,357           | 2,570,357          | 2,594,775                       |
| Mohegan Tribal Gaming Authority                | 11/01/2017      | Hotels, Motels, Inns and Gaming                                       | 11.50%                |   | 5,000,000           | 4,825,762          | 4,475,000                       |
| Questex Media Group LLC, Term Loan A           | 12/15/2014      | Other Media   | 9.50%                 | L+650 <sup>(8)</sup>                          | 3,219,319           | 3,219,319          | 2,675,254                       |
| Questex Media Group LLC, Term Loan B           | 12/15/2015      | Other Media   | 11.50% <sup>(6)</sup> | L+850 <sup>(8)</sup>                          | 1,773,703           | 1,773,703          | 1,349,788                       |
| Realogy Corp.                                  | 10/15/2017      | Buildings and Real Estate   | 13.50%                |   | 10,000,000          | 10,000,000         | 10,600,000                      |
| Saint Acquisition Corp. <sup>(5)</sup>         | 05/15/2015      | Transportation  | 8.13%                 | L+775   | 10,000,000          | 9,950,907          | 9,325,000                       |
| Saint Acquisition Corp. <sup>(5)</sup>         | 05/15/2017      | Transportation  | 12.50%                |   | 19,000,000          | 17,039,991         | 19,118,750                      |
| Sheridan Holdings, Inc.                        | 06/15/2015      | Healthcare, Education and Childcare                                   | 6.05% <sup>(6)</sup>  | L+575   | 21,500,000          | 19,211,412         | 19,887,500                      |
| Specialized Technology Resources, Inc.         | 12/15/2014      | Chemical, Plastics and Rubber   | 7.26% <sup>(6)</sup>  | L+700   | 22,500,000          | 22,490,129         | 22,500,000                      |
| TransFirst Holdings, Inc.                      | 06/15/2015      | Financial Services  | 6.29% <sup>(6)</sup>  | L+600   | 17,811,488          | 17,341,134         | 16,564,684                      |
| <b>Total Second Lien Secured Debt</b>          |                 |   |                       |   |                     | <b>151,611,934</b> | <b>149,087,151</b>              |
| <b>Subordinated Debt/Corporate Notes 56.1%</b> |                 |   |                       |   |                     |                    |                                 |
| Affinion Group Holdings, Inc. <sup>(5)</sup>   | 11/15/2015      | Consumer Products   | 11.63%                |   | 10,000,000          | 9,855,000          | 9,855,000                       |
| Aquilex Holdings, LLC <sup>(5)</sup>           | 12/15/2016      | Diversified / Conglomerate Services                                   | 11.13%                |   | 18,885,000          | 18,380,337         | 18,696,150                      |
| Consolidated Foundries, Inc.                   | 04/17/2015      | Aerospace and Defense   | 14.25% <sup>(6)</sup> |   | 8,109,468           | 7,973,429          | 8,170,289                       |
| CT Technologies Intermediate Holdings, Inc.    | 03/22/2014      | Business Services   | 14.00% <sup>(6)</sup> |   | 20,720,892          | 20,359,932         | 21,425,401                      |
| Da-Lite Screen Company, Inc. <sup>(5)</sup>    | 04/01/2015      | Home and Office Furnishings, Housewares and Durable Consumer Products | 12.50%                |   | 25,000,000          | 24,379,843         | 25,625,000                      |
| i2 Holdings Ltd. <sup>(10)</sup>               | 06/06/2014      | Aerospace and Defense   | 14.75% <sup>(6)</sup> |   | 23,283,292          | 22,970,124         | 23,283,292                      |
| Learning Care Group (U.S.) Inc.                | 06/30/2016      | Education   | 15.00% <sup>(6)</sup> |   | 3,947,368           | 3,194,611          | 3,592,105                       |
| MedQuist, Inc.                                 | 10/15/2016      | Business Services   | 13.00% <sup>(6)</sup> |   | 19,000,000          | 18,430,000         | 18,430,000                      |
| Realogy Corp.                                  | 04/15/2015      | Buildings and Real Estate   | 12.38%                |   | 10,000,000          | 9,055,731          | 7,900,000                       |
| TRAK Acquisition Corp.                         | 12/29/2015      | Business Services   | 15.00% <sup>(6)</sup> |   | 11,721,019          | 11,361,858         | 11,838,229                      |
| Trizetto Group, Inc.                           | 10/01/2016      | Insurance   | 13.50% <sup>(6)</sup> |   | 20,501,960          | 20,331,704         | 21,117,018                      |
| UP Acquisition Sub., Inc.                      | 02/08/2015      | Oil and Gas   | 15.50% <sup>(6)</sup> |   | 21,098,000          | 20,642,507         | 20,148,590                      |
| Veritext Corp.                                 | 12/31/2015      | Business Services   | 14.00% <sup>(6)</sup> |   | 15,000,000          | 14,636,487         | 15,000,000                      |
| Veritext Corp. <sup>(9)</sup>                  | 12/31/2012      | Business Services   |                       |   | 12,000,000          | 11,700,000         | 12,000,000                      |

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**Total Subordinated Debt/Corporate Notes**

213,271,563

217,081,074

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**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****SEPTEMBER 30, 2010**

| <b>Issuer Name</b>  | <b>Maturity</b> | <b>Industry</b>                     | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>      | <b>Fair Value<sup>(3)</sup></b> |
|---|-----------------|-------------------------------------|-----------------------|---|---------------------|------------------|---------------------------------|
| <b>Preferred Equity/Partnership Interests 2.0%</b>                                |                 |                                     |                       |   |                     |                  |                                 |
| AHC Mezzanine, LLC<br>(Advanstar Inc.)  |                 | Other Media                         |                       |   | 319                 | \$ 318,896       | \$                              |
| CFHC Holdings, Inc., Class A<br>(Consolidated Foundries, Inc.)                    |                 | Aerospace and Defense               | 12.00%                |   | 797                 | 797,288          | 1,070,352                       |
| CT Technologies Holdings, L.L.C.<br>(CT Technologies Intermediate Holdings, Inc.) |                 | Business Services                   | 9.00%                 |   | 144,375             | 144,376          | 148,909                         |
| i2 Holdings Ltd. <sup>(10)</sup>  |                 | Aerospace and Defense               | 12.00%                |   | 4,137,240           | 4,137,240        | 3,869,263                       |
| TZ Holdings, L.P., Series A<br>(Trizetto Group, Inc.)                             |                 | Insurance                           |                       |   | 686                 | 685,820          | 685,820                         |
| TZ Holdings, L.P., Series B<br>(Trizetto Group, Inc.)                             |                 | Insurance                           | 6.50%                 |   | 1,312               | 1,312,006        | 1,495,885                       |
| UP Holdings, Inc., Class A-1<br>(UP Acquisitions Sub, Inc.)                       |                 | Oil and Gas                         | 8.00%                 |   | 91,608              | 2,499,066        | 495,851                         |
| <b>Total Preferred Equity/Partnership Interests</b>                               |                 |                                     |                       |   |                     | <b>9,894,692</b> | <b>7,766,080</b>                |
| <b>Common Equity/Warrants/Partnership Interests 9.9%</b>                          |                 |                                     |                       |   |                     |                  |                                 |
| CEA Autumn Management, L.L.C.   |                 | Broadcasting and Entertainment      |                       |   | 1,333               | 3,000,000        | 3,000,000                       |
| CFHC Holdings, Inc.<br>(Consolidated Foundries, Inc.)                             |                 | Aerospace and Defense               |                       |   | 1,627               | 16,271           | 387,012                         |
| CT Technologies Holdings, L.L.C.<br>(CT Technologies Intermediate Holdings, Inc.) |                 | Business Services                   |                       |   | 5,556               | 3,200,000        | 7,987,755                       |
| EnviroSolutions, Inc.   |                 | Environmental Services              |                       |   | 24,375              | 1,506,076        | 1,998,008                       |
| EnviroSolutions, Inc. (Warrants)  |                 | Environmental Services              |                       |   | 49,005              | 3,027,906        | 4,016,429                       |
| i2 Holdings Ltd. <sup>(10)</sup>  |                 | Aerospace and Defense               |                       |   | 457,322             | 454,030          |                                 |
| Kadmon Holdings, L.L.C., Class A<br>(Three Rivers Pharmaceutical, L.L.C.)         |                 | Healthcare, Education and Childcare |                       |   | 8,999               | 1,780,693        | 1,780,693                       |
| Kadmon Holdings, L.L.C., Class D<br>(Three Rivers Pharmaceutical, L.L.C.)         |                 | Healthcare, Education and Childcare |                       |   | 8,999               | 857,339          | 857,339                         |
| Learning Care Group (U.S.), Inc.<br>(Warrants)                                    | 04/27/2020      | Education                           |                       |   | 1,267               | 779,920          | 633,308                         |
| Magnum Hunter Resources Corporation   |                 | Oil and Gas                         |                       |   | 1,055,932           | 2,464,999        | 4,350,440                       |
| QMG HoldCo, LLC, Class A<br>(Questex Media Group, Inc.)                           |                 | Other Media                         |                       |   | 4,325               | 1,306,167        | 1,081,683                       |
| QMG HoldCo, LLC, Class B<br>(Questex Media Group, Inc.)                           |                 | Other Media                         |                       |   | 531                 |                  | 132,803                         |
| TRAK Acquisition Corp. (Warrants)   | 12/29/2019      | Business Services                   |                       |   | 3,500               | 29,400           | 973,875                         |
| Transportation 100 Holdco, L.L.C.<br>(Greatwide Logistics Services, L.L.C.)       |                 | Cargo Transport                     |                       |   | 137,923             | 2,111,588        | 4,589,906                       |
| TZ Holdings, L.P.<br>(Trizetto Group, Inc.)                                       |                 | Insurance                           |                       |   | 2                   | 9,843            | 1,688,629                       |
| UP Holdings, Inc.<br>(UP Acquisitions Sub, Inc.)                                  |                 | Oil and Gas                         |                       |   | 91,608              | 916              |                                 |

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|  |                   |        |                |                |
|--|-------------------|--------|----------------|----------------|
| VText Holdings, Inc.   | Business Services | 35,526 | 4,050,000      | 4,634,758      |
| <b>Total Common Equity/Warrants/Partnership Interests</b>                |                   |        | 24,595,148     | 38,112,638     |
| <b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies</b> |                   |        | \$ 631,280,755 | \$ 641,290,626 |

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)****SEPTEMBER 30, 2010**

| <b>Issuer Name</b>   | <b>Maturity</b> | <b>Industry</b>                                       | <b>Current Coupon</b> | <b>Basis Points Above Index<sup>(4)</sup></b> | <b>Par / Shares</b> | <b>Cost</b>    | <b>Fair Value<sup>(3)</sup></b> |
|--|-----------------|---|-----------------------|---|---------------------|----------------|---------------------------------|
| <b>Investments in Non-Controlled, Affiliated Portfolio Companies 4.0%</b> <sup>(1),(2)</sup> |                 |   |                       |   |                     |                |                                 |
| <b>Second Lien Secured Debt 2.0%</b>   |                 |   |                       |   |                     |                |                                 |
| Performance, Inc.  | 01/16/2015      | Leisure, Amusement, Motion Pictures and Entertainment | 7.50%                 | L+650 <sup>(8)</sup>                          | \$ 8,000,000        | \$ 8,000,000   | \$ 7,584,000                    |
| <b>Subordinated Debt/Corporate Notes 1.5%</b>  |                 |   |                       |   |                     |                |                                 |
| Performance Holdings, Inc.   | 07/16/2015      | Leisure, Amusement, Motion Pictures and Entertainment | 15.00% <sup>(6)</sup> |   | 5,848,176           | 5,677,648      | 5,745,832                       |
| <b>Common Equity/Partnership Interest 0.5%</b> <sup>(7)</sup>                                |                 |   |                       |   |                     |                |                                 |
| NCP-Performance (Performance Holdings, Inc.)   |                 | Leisure, Amusement, Motion Pictures and Entertainment |                       |   | 37,500              | 3,750,000      | 2,103,848                       |
| <b>Investments in Non-Controlled, Affiliated Portfolio Companies</b>                         |                 |   |                       |   |                     | 17,427,648     | 15,433,680                      |
| <b>Investments in Controlled, Affiliated Portfolio Companies 2.1%</b> <sup>(1),(2)</sup>     |                 |   |                       |   |                     |                |                                 |
| <b>First Lien Secured Debt 1.4%</b>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  | 06/30/2020      | Business Services                                     | 14.00% <sup>(6)</sup> |   | 4,800,000           | 4,800,000      | 5,352,000                       |
| <b>Subordinated Debt/Corporate Notes 0.3%</b>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  | 06/30/2020      | Business Services                                     | 14.00% <sup>(6)</sup> |   | 1,200,000           | 1,200,000      | 1,142,398                       |
| <b>Preferred Equity 0.4%</b> <sup>(7)</sup>  |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  |                 | Business Services                                     | 14.00%                |   | 2,000               | 2,000,000      | 1,505,602                       |
| <b>Common Equity 0.0%</b> <sup>(7)</sup>   |                 |   |                       |   |                     |                |                                 |
| SuttonPark Holdings, Inc.  |                 | Business Services                                     |                       |   | 100                 | 100            | 100                             |
| <b>Investments in Controlled, Affiliated Portfolio Companies</b>                             |                 |   |                       |   |                     | 8,000,100      | 8,000,100                       |
| <b>Total Investments 172.0%</b>  |                 |   |                       |   |                     | 656,708,503    | 664,724,406                     |
| <b>Cash and Cash Equivalents 0.5%</b>  |                 |   |                       |   | 1,814,451           | 1,814,451      | 1,814,451                       |
| <b>Total Investments and Cash and Cash Equivalents 172.5%</b>                                |                 |   |                       |   |                     | \$ 658,522,954 | \$ 666,538,857                  |
| <b>Liabilities in Excess of Other Assets (72.5%)</b>   |                 |   |                       |   |                     |                | (279,963,634)                   |
| <b>Net Assets 100.0%</b>   |                 |   |                       |   |                     |                | \$ 386,575,223                  |



- (1) The provisions of the 1940 Act classify investments based on the level of control that we maintain in a particular portfolio company. As defined in the 1940 Act, a company is deemed as non-controlled when we own less than 25% of a portfolio company's voting securities and controlled when we own 25% or more of a portfolio company's voting securities.
- (2) The provisions of the 1940 Act classify investments further based on the level of ownership that we maintain in a particular portfolio company. As defined in the 1940 Act, a company is deemed as non-affiliated when we own less than 5% of a portfolio company's voting securities and affiliated when we own 5% or more of a portfolio company's voting securities.
- (3) Valued based on our accounting policy (see Note 2 to our consolidated financial statements).
- (4) Represents floating rate instruments that accrue interest at a predetermined spread relative to an index, typically the applicable LIBOR or Prime Rate.
- (5) Security is exempt from registration under Rule 144A promulgated under the Securities Act of 1933. The security may be resold in transactions that are exempt from registration, usually to qualified institutional buyers.
- (6) Coupon is payable in cash and/or PIK.
- (7) Non-income producing securities.
- (8) Coupon is subject to a LIBOR or Prime rate floor.
- (9) Represents the purchase of a security with delayed settlement (unfunded investment). This security does not have a basis point spread above an index.
- (10) Non-U.S. company or principal place of business outside the United States.

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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**PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**MARCH 31, 2011**

**(Unaudited)**

**1. ORGANIZATION**

PennantPark Investment Corporation was organized as a Maryland corporation on January 11, 2007. PennantPark Investment is a closed-end, externally managed, non-diversified investment company that has elected to be treated as a business development company under the Investment Company Act of 1940 (the 1940 Act ). PennantPark Investment's objective is to generate both current income and capital appreciation through debt and equity investments. PennantPark Investment invests primarily in U.S. middle-market companies in the form of senior secured loans, mezzanine debt and equity investments.

On April 24, 2007, PennantPark Investment closed its initial public offering and its common stock trades on the NASDAQ Global Select Market under the symbol PNNT . PennantPark Investment entered into an investment management agreement (the Investment Management Agreement ) with PennantPark Investment Advisers, LLC (the Investment Adviser or PennantPark Investment Advisers ), an external adviser that manages our day-to-day operations. PennantPark Investment also entered into an administration agreement (the Administration Agreement ) with PennantPark Investment Administration, LLC (the Administrator or PennantPark Investment Administration ) that provides the administrative services necessary for us to operate.

PennantPark Investment, through the Investment Adviser, manages day-to-day operations of and provides investment advisory services to SBIC LP under a separate investment management agreement. PennantPark Investment, through the Administrator, also provides similar services to SBIC LP and our controlled affiliate SuttonPark Holdings, Inc. and its subsidiaries ( SPH ) under separate administration agreements. See Note 3.

SBIC LP and its general partner, SBIC GP, were organized in Delaware as a limited partnership and a limited liability company, respectively, on May 7, 2010 and began operations on June 11, 2010. SBIC LP received a license from the Small Business Administration ( SBA ) to operate as a Small Business Investment Company ( SBIC ) effective July 30, 2010 under Section 301(c) of the Small Business Investment Act of 1958 (the 1958 Act ). Our subsidiaries are consolidated and wholly owned by PennantPark Investment. The SBIC LP's investment objective is substantially similar to PennantPark Investment, generally co-investing in SBA eligible businesses that meet the investment criteria of PennantPark Investment.

PennantPark Investment completed its initial public offering of common stock in 2007 and issued 21.0 million shares raising \$294.1 million in net proceeds. Since PennantPark Investment's initial public offering, it has sold 24.3 million shares of common stock through follow-on public offerings, resulting in net proceeds of \$242.5 million. On February 11, 2011, PennantPark Investment sold 9.2 million shares in a follow-on public offering including the overallotment, resulting in net proceeds of \$108.3 million.

**2. SIGNIFICANT ACCOUNTING POLICIES**

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles ( GAAP ) requires management to make estimates and assumptions that affect the reported amount of our consolidated assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expenses during the reported period. Actual results could differ from these estimates. We have reclassified certain prior period amounts to conform to the current period presentation. We have eliminated all intercompany balances and transactions. References to the Accounting Standards Codification ( ASC ) serve as a single source of accounting literature and are not intended to change accounting literature. Subsequent events are evaluated and disclosed as appropriate for events occurring through the date the consolidated financial statements are issued.

Our consolidated financial statements are prepared in accordance with GAAP and pursuant to the requirements for reporting on Form 10-K and Article 6 or 10 of Regulation S-X, as appropriate. In accordance with Article 6-09 of Regulation S-X under the Exchange Act, we have provided a Consolidated Statement of Changes in Net Assets in lieu of a Consolidated Statement of Changes in Stockholders' Equity.

Our significant accounting policies consistently applied are as follows:

(a) ***Investment Valuations***

Our board of directors generally uses market quotations to assess the value of our investments for which market quotations are readily available. We obtain these market values from independent pricing services or at the bid prices obtained from at least two broker/dealers if available, otherwise by a principal market maker or a primary market dealer. If the board of directors has a bona fide reason to believe any such market quote does not reflect the fair value of an investment, it may independently value such investments by using the valuation procedure that it uses with respect to assets for which market quotations are not readily available. Investments, of sufficient credit quality, purchased within 60 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates fair value.

We expect that there will not be readily available market values for many of our investments which are or will be in our portfolio, and we value such investments at fair value as determined in good faith by or under the direction of our board of directors using a documented valuation policy, described herein, and a consistently applied valuation process. With respect to investments for which there is no readily available market value, the factors that the board of directors may take into account in pricing our investments at fair value include, as relevant, the nature and realizable value of any collateral, the portfolio company's ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business, comparison to publicly traded securities and other relevant factors. When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, we consider the pricing indicated by the external event to corroborate or revise our valuation. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material. See Note 5.

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**PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**MARCH 31, 2011**

**(Unaudited)**

With respect to investments for which market quotations are not readily available, or for which market quotations are deemed not reflective of the fair value, our board of directors undertakes a multi-step valuation process each quarter, as described below:

- (1) Our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals of our Investment Adviser responsible for the portfolio investment;
- (2) Preliminary valuation conclusions are then documented and discussed with the management of our Investment Adviser;
- (3) Our board of directors also engages independent valuation firms to conduct independent appraisals of our investments for which market quotations are not readily available or are readily available but deemed not reflective of the fair value of the investment. The independent valuation firms review management's preliminary valuations in light of their own independent assessment and also in light of any market quotations obtained from an independent pricing service, broker, dealer or market maker.
- (4) The audit committee of our board of directors reviews the preliminary valuations of the Investment Adviser and that of the independent valuation firms and responds and supplements the valuation recommendations of the independent valuation firms to reflect any comments; and
- (5) The board of directors discusses these valuations and determines the fair value of each investment in our portfolio in good faith based on the input of our Investment Adviser, the respective independent valuation firms and the audit committee.

***(b) Security Transactions, Revenue Recognition, and Realized/Unrealized Gains or Losses***

Security transactions are recorded on a trade-date basis. We measure realized gains or losses by the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment, using the specific identification method, without regard to unrealized appreciation or depreciation previously recognized, but considering unamortized upfront fees and prepayment penalties. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment and credit facility values during the reporting period, including any reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

We record interest income on an accrual basis to the extent that we expect to collect such amounts. For loans and debt investments with contractual PIK interest, which represents interest accrued and added to the loan balance that generally becomes due at maturity, we will generally not accrue PIK interest when the portfolio company valuation indicates that such PIK interest is not collectable. We do not accrue as a receivable interest on loans and debt investments if we have reason to doubt our ability to collect such interest. Loan origination fees, original issue discount, market discount or premium and deferred financing costs are capitalized and we then accreted or amortized such amounts using the effective interest method as interest income or interest expense as it relates to our deferred financing costs. We record prepayment premiums on loans and debt investments as income. Dividend income, if any, is recognized on an accrual basis on the ex-dividend date to the extent that we expect to collect such amounts.

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Loans are placed on non-accrual status when principal or interest payments are past due 30 days or more and/or when there is reasonable doubt that principal or interest will be collected. Accrued interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management's judgment. Non-accrual loans are restored to accrual status when past due principal and interest is paid and, in management's judgment, are likely to remain current.

### *(c) Income Taxes*

Since May 1, 2007, PennantPark Investment has complied with the requirements of Subchapter M of the Internal Revenue Code of 1986, as amended, (the Code), and expects to be subject to tax as a regulated investment company (RIC). As a RIC, PennantPark Investment accounts for income taxes using the asset liability method prescribed by ASC 740, Income Taxes. Under this method, income taxes were provided for amounts currently payable and for amounts deferred as tax assets and liabilities based on differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. Based upon PennantPark Investment's qualification and election to be subject to tax as a RIC, we do not anticipate paying any material level of federal income taxes in the future. Although we are subject to tax as a RIC, we elected to retain a portion of our calendar year income and incurred an excise tax of \$0.2 million and \$0.1 million for the six months ended March 31, 2011 and 2010, respectively. PennantPark Investment recognizes in its consolidated financial statements the effect of a tax position when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. We did not have any uncertain tax positions that met the recognition or measurement criteria of ASC 740-10-25 nor did we have any unrecognized tax benefits as of the periods presented herein. Although we file federal and state tax returns, our major tax jurisdiction is federal. Our tax returns for each of our inception-to-date federal tax years remain subject to examination by the Internal Revenue Service.

Book and tax basis differences relating to permanent book and tax differences are reclassified among PennantPark Investment's capital accounts, as appropriate. Additionally, the tax characteristics of distributions are determined in accordance with income tax regulations that may differ from GAAP.

### *(d) Dividends, Distributions and Capital Transactions*

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be paid as a dividend is determined by the board of directors each quarter and is generally based upon the earnings estimated by management. Net realized capital gains, if any, are distributed at least annually.

Capital transactions, in connection with our dividend reinvestment plan or through offerings of our common stock, are recorded when issued and offering costs are charged as a reduction of capital upon issuance of our common stock.

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**PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**MARCH 31, 2011**

**(Unaudited)**

**(e) Consolidation**

As permitted under Regulation S-X and the AICPA Audit and Accounting Guide for Investment Companies, PennantPark Investment will generally not consolidate its investment in a company other than an investment company subsidiary or a controlled operating company whose business consists of providing services to us. Accordingly, we have consolidated the results of our subsidiaries in our consolidated financial statements.

**(f) New Accounting Pronouncements and Accounting Standards Updates ( ASU )**

In January 2010, the FASB issued ASU 2010-06, *Fair Value Measurements and Disclosures* ( ASU 2010-06 ), to clarify and amend ASC 820-10. In particular, it requires that entities disclose on a gross basis purchases, sales, issuances, and settlements within the Level 3 fair value roll-forward. ASU 2010-06 clarifies existing fair value disclosures about the level of disaggregation as well as inputs and valuation techniques for both recurring and nonrecurring fair value measurements that fall into Level 2 or 3. The new disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. We have adopted the disclosures regarding the disaggregation of purchases, sales and settlements in the roll-forward of activity in Level 3 fair value measurements and it did not have a material impact on our consolidated financial statements.

**3. AGREEMENTS**

PennantPark Investment's Investment Management Agreement with the Investment Adviser was re-approved by our board of directors, including a majority of our independent directors of PennantPark Investment, in February 2011. Under this agreement the Investment Adviser, subject to the overall supervision of PennantPark Investment's board of directors, manages the day-to-day operations of and provides investment advisory services to PennantPark Investment. SBIC LP's investment management agreement does not affect the management or incentive fees that we pay to the Investment Adviser on a consolidated basis. For providing these services, the Investment Adviser receives a fee from PennantPark Investment, consisting of two components—a base management fee and an incentive fee (collectively, Management Fees).

The base management fee is calculated at an annual rate of 2.00% on PennantPark Investment's average adjusted gross assets (net of U.S. Treasury Bills and/or temporary draws on the credit facility, if any, see Note 10). The base management fee is 2.00% and is payable quarterly in arrears. The base management fee is calculated based on the average adjusted gross assets at the end of the two most recently completed calendar quarters, and appropriately adjusted for any share issuances or repurchases during the current calendar quarter. For the three and six months ended March 31, 2011, the Investment Adviser earned a base management fee of \$3.6 million and \$7.1 million, respectively, from us. For the three and six months ended March 31, 2010, the Investment Adviser earned a base management fee of \$2.8 million and \$5.3 million, respectively, from us.

The incentive fee has two parts, as follows:

One part is calculated and payable quarterly in arrears based on PennantPark Investment's Pre-Incentive Fee Net Investment Income for the immediately preceding calendar quarter. For this purpose, Pre-Incentive Fee Net Investment Income means interest income, distribution income and any other income, including any other fees other than fees for providing managerial assistance, such as commitment, origination, structuring, diligence and consulting fees or other fees received from portfolio companies accrued during the calendar quarter, minus PennantPark Investment's operating expenses for the quarter (including the base management fee, any expenses payable under the Administration Agreement, and any interest expense and distribution paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-Incentive Fee Net Investment Income includes, in the case of investments with a deferred interest feature (such as original issue discount, debt instruments with PIK interest and zero coupon securities), accrued income not yet received in cash. Pre-Incentive Fee Net Investment Income does not include any realized capital gains, realized capital losses or unrealized capital appreciation or depreciation. Pre-Incentive Fee Net Investment Income, expressed as a rate of return on the value of PennantPark Investment's net assets at the end of the immediately preceding calendar

quarter, is compared to the hurdle rate of 1.75% per quarter (7.00% annualized). PennantPark Investment pays the Investment Adviser an incentive fee with respect to PennantPark Investment's Pre-Incentive Fee Net Investment Income in each calendar quarter as follows: (1) no incentive fee in any calendar quarter in which PennantPark Investment's Pre-Incentive Fee Net Investment Income does not exceed the hurdle rate of 1.75%, (2) 100% of PennantPark Investment's Pre-Incentive Fee Net Investment Income with respect to that portion of such Pre-Incentive Fee Net Investment Income, if any, that exceeds the hurdle rate but is less than 2.1875% in any calendar quarter (8.75% annualized), and (3) 20% of the amount of PennantPark Investment's Pre-Incentive Fee Net Investment Income, if any, that exceeds 2.1875% in any calendar quarter. These calculations are pro rated for any period of less than three months and adjusted for any share issuances or repurchases during the current quarter.

The second part of the incentive fee is determined and payable in arrears as of the end of each calendar year (or upon termination of the Investment Management Agreement, as of the termination date) and equals 20.0% of PennantPark Investment's realized capital gains, if any, on a cumulative basis from inception through the end of each calendar year, computed net of all realized capital losses and unrealized capital depreciation on a cumulative basis, less the aggregate amount of any previously paid capital gain incentive fees. For the three and six months ended March 31, 2011, the Investment Adviser earned an incentive fee of \$3.3 million and \$6.1 million, respectively from us on net investment income. For the three and six months ended March 31, 2010, the Investment Adviser earned an incentive fee of \$1.8 million and \$3.6 million, respectively from us on net investment income. As of March 31, 2011, our unrealized capital gains did not exceed our cumulative realized and unrealized capital losses.

PennantPark Investment's Administration Agreement with the Administrator was reapproved by our board of directors, including a majority of our directors who are not interested persons of PennantPark Investment, in February 2011. Under this agreement PennantPark Investment Administration provides administrative services for PennantPark Investment. The Administrator provides similar services to SBIC LP under its administration agreement with PennantPark Investment. For providing these services, facilities and personnel, PennantPark Investment reimburses the Administrator for its allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under the Administration Agreement, including rent, technology systems, insurance and PennantPark Investment's allocable portion of the costs of the compensation and related expenses for its chief compliance officer, chief financial officer and their respective staffs. The Administrator also offers, on PennantPark Investment's behalf, managerial assistance to portfolio companies to which PennantPark Investment is required to offer such assistance. Reimbursement for certain of these costs is included in administrative services expenses in the Consolidated Statement of Operations. For the three and six months ended March 31, 2011, the Investment Adviser was reimbursed \$1.3 million and \$1.9 million, respectively, from us, including expenses it incurred on behalf of the Administrator, for services described above. For the three and six months ended March 31, 2010, the Investment Adviser was reimbursed \$1.1 million and \$1.5 million, respectively, from us, including expenses it incurred on behalf of the Administrator.

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

PennantPark Investment entered into an administration agreement with its controlled affiliate SuttonPark Holdings, Inc. and its subsidiaries ( SPH ). Under the administration agreement with SPH, or the SPH Administration Agreement, PennantPark Investment, through the Administrator, furnishes SPH with office facilities, equipment and clerical, bookkeeping and record keeping services at such facilities. Additionally, the Administrator performs or oversees the performance of SPH s required administrative services, which include, among other things, maintaining financial records, preparing financial reports and filing of tax returns. Payments under the SPH Administration Agreement are equal to an amount based upon SPH s allocable portion of the Administrator s overhead in performing its obligations under the SPH Administration Agreement, including rent and allocable portion of the cost of compensation and related expenses of our chief financial officer and his respective staff. For the three and six months ended March 31, 2011, the PennantPark Investment was reimbursed \$0.3 million and \$0.4 million for the services described above.

**4. INVESTMENTS**

Purchases of long-term investments including PIK for the three and six months ended March 31, 2011 totaled \$98.8 million and \$201.7 million, respectively. For the same period in the prior year, purchases of long-term investments including PIK totaled \$70.8 million and \$122.4 million, respectively. Sales and repayments of long-term investments for the three and six months ended March 31, 2011 totaled \$51.6 million and \$137.1 million, respectively. For the same period in the prior year, sales and repayments of long-term investments totaled \$6.7 million and \$23.5 million, respectively.

Investments and cash equivalents consisted of the following:

|  | March 31, 2011 |                | September 30, 2010 |                |
|--|----------------|----------------|--------------------|----------------|
|  | Cost           | Fair Value     | Cost               | Fair Value     |
| First lien                             | \$ 295,799,382 | \$ 303,671,023 | \$ 236,707,418     | \$ 234,595,683 |
| Second lien                            | 147,012,656    | 141,477,456    | 159,611,934        | 156,671,151    |
| Subordinated debt / corporate notes    | 239,179,115    | 249,864,207    | 220,149,211        | 223,969,304    |
| Preferred equity                       | 16,405,427     | 15,749,644     | 11,894,692         | 9,271,682      |
| Common equity                          | 28,734,654     | 47,887,902     | 28,345,248         | 40,216,586     |
| Total Investments                      | 727,131,234    | 758,650,232    | 656,708,503        | 664,724,406    |
| Cash equivalents                       | 1,546,429      | 1,546,429      | 1,814,451          | 1,814,451      |
| Total Investments and cash equivalents | \$ 728,677,663 | \$ 760,196,661 | \$ 658,522,954     | \$ 666,538,857 |

The table below describes investments by industry classification and enumerates the percentage, by fair value, of the total portfolio assets (excluding cash equivalents) in such industries as of March 31, 2011 and September 30, 2010.

| Industry Classification           | March 31, 2011 | September 30, 2010 |
|-----------------------------------|----------------|--------------------|
| Business Services                 | 11%            | 15%                |
| Healthcare, Education & Childcare | 9              | 8                  |
| Aerospace and Defense             | 8              | 6                  |



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|  |             |             |
|--|-------------|-------------|
| Consumer Products  | 7           | 1           |
| Oil & Gas  | 7           | 4           |
| Hotels, Motels, Inns and Gaming  | 6           | 7           |
| Chemicals, Plastic and Rubber  | 5           | 6           |
| Home and Office Furnishings, Housewares, and Durable Consumer Products | 5           | 6           |
| Other Media  | 5           | 2           |
| Printing and Publishing  | 5           | 4           |
| Education  | 4           | 5           |
| Telecommunications   | 4           | 3           |
| Buildings and Real Estate  | 3           | 3           |
| Diversified/Conglomerate Services                                      | 3           | 3           |
| Electronics  | 3           |             |
| Energy / Utilities   | 3           | 3           |
| Environmental Services   | 3           | 3           |
| Personal Transportation  | 3           |             |
| Communications   | 2           | 4           |
| Leisure, Amusement, Motion Picture, Entertainment                      | 2           | 2           |
| Grocery  |             | 2           |
| Insurance  |             | 4           |
| Transportation   |             | 4           |
| Other  | 2           | 5           |
| <b>Total</b>   | <b>100%</b> | <b>100%</b> |

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**PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**MARCH 31, 2011**

**(Unaudited)**

**5. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Fair Value Measurements, as defined under ASC 820, is the price that we would receive upon selling an investment or pay to transfer a liability in an orderly transaction to a market participant in the principal or most advantageous market for the investment or liability. ASC 820 emphasizes that valuation techniques maximize the use of observable market inputs and minimize the use of unobservable inputs. Inputs refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of PennantPark Investment. Unobservable inputs reflect the assumptions market participants would use in pricing an asset or liability developed based on the best information available at the time.

ASC 820 classifies the inputs used to measure these fair values into the following hierarchies:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities, accessible by us at the measurement date.

Level 2: Inputs that are quoted prices for similar assets or liabilities in active markets, or that are quoted prices for identical or similar assets or liabilities in markets that are not active and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term, if applicable, of the financial instrument.

Level 3: Inputs that are unobservable for an asset or liability because they are based on our own assumptions about how market participants would price the asset or liability.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Generally, most of our investments and long-term credit facility are classified as Level 3. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, which may include assets using both levels 2 and 3 inputs, the fair value of our investments may fluctuate from period to period.

The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes from brokers/dealers accompanied by disclaimer would result in classification as Level 3 information, assuming no additional corroborating evidence was available. Corroborating evidence that would result in classifying these non-binding broker/dealer bids as a level 2 asset includes, but is not limited to, observable market based transactions for the same or similar assets or other relevant observable market based inputs that may be used in pricing an asset.

Our investments are generally structured as debt and equity investments in the form of senior secured loans, mezzanine debt and equity co-investments. The transaction price, excluding transaction costs, is typically the best estimate of fair value at inception. When evidence supports a subsequent change to the carrying value from the original transaction price, adjustments are made to reflect the expected exit values. Ongoing reviews by our Investment Adviser and independent valuation firms are based on an assessment of each underlying investment, incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows and market-based information including comparable transactions, performance multiples and yields, among other factors. These non-public investments using unobservable inputs are included in Level 3 of the fair value hierarchy.

A review of fair value hierarchy classifications is conducted on a quarterly basis. Changes in our ability to observable valuation inputs may result in a reclassification for certain financial assets or liabilities. Reclassifications impacting Level 3 of the fair value hierarchy are reported as transfers in or out of the Level 3 category as of the end of the quarter in which the reclassifications occur. During the six months ended

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March 31, 2011, our ability to observe valuation inputs has resulted in a reclassification of assets from Level 3 to Level 2.

In addition to using the above inputs in cash equivalents, investments and long-term credit facility valuations, PennantPark Investment employs the valuation policy approved by its board of directors that is consistent with ASC 820 (See Note 2). Consistent with our valuation policy, PennantPark Investment evaluates the source of inputs, including any markets in which its investments are trading, in determining fair value.

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

At March 31, 2011 and September 30, 2010, our cash equivalents, investments and our long-term credit facility were categorized as follows in the fair value hierarchy for ASC 820 purposes.

**March 31, 2011**

| <b>Description</b>                            | <b>Fair Value</b>  | <b>Level 1</b>    | <b>Level 2</b>    | <b>Level 3</b>     |
|---|--------------------|-------------------|-------------------|--------------------|
| Loan and debt investments                     | \$ 695,012,686     | \$                | \$ 31,472,281     | \$ 663,540,405     |
| Equity investments                            | 63,637,546         | 9,049,337         |                   | 54,588,209         |
| <b>Total Investments</b>                      | <b>758,650,232</b> | <b>9,049,337</b>  | <b>31,472,281</b> | <b>718,128,614</b> |
| Cash Equivalents                              | 1,546,429          | 1,546,429         |                   |                    |
| <b>Total Investments and cash equivalents</b> | <b>760,196,661</b> | <b>10,595,766</b> | <b>31,472,281</b> | <b>718,128,614</b> |
| Long-Term Credit Facility                     | \$ (149,083,371)   | \$                | \$                | \$ (149,083,371)   |

**September 30, 2010**

| <b>Description</b>                            | <b>Fair Value</b>  | <b>Level 1</b>   | <b>Level 2</b> | <b>Level 3</b>     |
|---|--------------------|------------------|----------------|--------------------|
| Loan and debt investments                     | \$ 615,236,138     | \$               | \$             | \$ 615,236,138     |
| Equity investments                            | 49,488,268         | 4,350,440        |                | 45,137,828         |
| <b>Total Investments</b>                      | <b>664,724,406</b> | <b>4,350,440</b> |                | <b>660,373,966</b> |
| Cash Equivalents                              | 1,814,451          | 1,814,451        |                |                    |
| <b>Total Investments and cash equivalents</b> | <b>666,538,857</b> | <b>6,164,891</b> |                | <b>660,373,966</b> |
| Long-Term Credit Facility                     | \$ (213,941,125)   | \$               | \$             | \$ (213,941,125)   |

The following tables show a reconciliation of the beginning and ending balances for fair valued investments measured using significant unobservable inputs (Level 3) for the six months ended March 31, 2011 and 2010:

**Period Ended March 31, 2011**

| <b>Description</b>                    | <b>Loan and debt investments</b> | <b>Equity investments</b> | <b>Totals</b>  |
|---------------------------------------|----------------------------------|---------------------------|----------------|
| Beginning Balance, September 30, 2010 | \$ 615,236,138                   | \$ 45,137,828             | \$ 660,373,966 |
| Realized gains                        | 2,579,813                        |                           | 2,579,813      |

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|   |                |               |                |
|---|----------------|---------------|----------------|
| Unrealized appreciation                   | 11,465,652     | 4,550,239     | 16,015,891     |
| Purchases, PIK and net discount accretion | 199,248,180    | 5,664,360     | 204,912,540    |
| Sales / repayments                        | (136,343,315)  | (764,218)     | (137,107,533)  |
| Non-cash exchanges                        |                |               |                |
| Transfers out of Level 3                  | (28,646,063)   |               | (28,646,063)   |
| Ending Balance, March 31, 2011            | \$ 663,540,405 | \$ 54,588,209 | \$ 718,128,614 |

|   |               |              |               |
|---|---------------|--------------|---------------|
| Net change in unrealized appreciation for the six months ended March 31, 2011 reported within the net change in unrealized appreciation on investments in our Consolidated Statement of Operations attributable to our Level 3 assets still held at the reporting date. | \$ 12,379,569 | \$ 4,550,239 | \$ 16,929,808 |
|---|---------------|--------------|---------------|

**Period Ended March 31, 2010**

| Description                               | Loan and debt investments | Equity investments | Totals         |
|---|---------------------------|--------------------|----------------|
| Beginning Balance, September 30, 2009     | \$ 442,128,049            | \$ 27,632,024      | \$ 469,760,073 |
| Realized losses                           | (13,739,688)              | (3,005,163)        | (16,744,851)   |
| Unrealized appreciation                   | 32,692,977                | 400,023            | 33,093,000     |
| Purchases, PIK and net discount accretion | 121,095,534               | 827,434            | 121,922,968    |
| Sales / repayments                        | (23,491,075)              |                    | (23,491,075)   |
| Non-cash exchanges                        | (1,306,167)               | 1,306,167          |                |
| Transfers in and /or out of Level 3       |                           |                    |                |
| Ending Balance, March 31, 2010            | \$ 557,379,630            | 27,160,485         | 584,540,115    |

|  |               |                |               |
|--|---------------|----------------|---------------|
| Net change in unrealized appreciation (depreciation) for the six months ended March 31, 2010 reported within the net change in unrealized depreciation on investments in our Consolidated Statement of Operations attributable to our Level 3 assets still held at the reporting date. | \$ 16,550,354 | \$ (2,605,139) | \$ 13,945,215 |
|--|---------------|----------------|---------------|

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****MARCH 31, 2011****(Unaudited)**

The following tables show a reconciliation of the beginning and ending balances for fair valued liabilities measured using significant unobservable inputs (Level 3) for the six months ended March 31, 2011 and 2010, respectively. There were no temporary draws outstanding at March 31, 2010.

**Period Ended March 31, 2011**

|   | <b>Carrying /<br/>Fair Value</b> |
|---|----------------------------------|
| <b>Long-Term Credit Facility</b>  |                                  |
| Beginning balance, September 30, 2010 (Cost \$227,900,000)                      | \$ 213,941,125                   |
| Total unrealized appreciation included in earnings                              | 11,303,446                       |
| Borrowings  | 128,900,000                      |
| Repayments  | (205,061,200)                    |
| Transfers in and/or out of Level 3  |                                  |
| Ending balance of long-term credit facility at fair value, (Cost \$151,738,800) | 149,083,371                      |
| Temporary draw outstanding, at cost   | 1,100,000                        |
| Total credit facility, March 31, 2011 (Cost \$152,838,800)                      | \$ 150,183,371                   |

**Period Ended March 31, 2010**

|  | <b>Carrying /<br/>Fair Value</b> |
|--|----------------------------------|
| <b>Long-Term Credit Facility</b>                           |                                  |
| Beginning balance, September 30, 2009 (Cost \$218,100,000) | \$ 168,475,380                   |
| Total unrealized appreciation included in earnings         | 25,691,628                       |
| Borrowings   | 86,700,000                       |
| Repayments   | (79,300,000)                     |
| Transfers in and/or out of Level 3                         |                                  |
| Ending Balance, March 31, 2010 (Cost \$225,500,000)        | \$ 201,567,008                   |

The carrying value of PennantPark Investment's financial liabilities approximates fair value. We adopted ASC 825-10, which provides companies with an option to report selected financial assets and liabilities at fair value, and made an irrevocable election to apply ASC 825-10 to its long-term credit facility. PennantPark Investment elected to use the fair value option for its credit facility to align the measurement attributes of both our assets and liabilities while mitigating volatility in earnings from using different measurement attributes. ASC 825-10 establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities and to more easily understand the effect of a company's choice to use fair value on its earnings. ASC 825-10 also requires entities to display the fair value of the selected assets and liabilities on the face of the balance sheet and changes in fair value of the credit facility are recorded in the Consolidated Statement of Operations. For the three and six months ended March 31, 2011, our credit facility had a net change in unrealized appreciation of \$4.7 million and \$11.3 million, respectively. For the three and six months ended March 31, 2010, our credit facility had a net change in unrealized appreciation of \$19.9 million and \$25.7 million, respectively. On March 31, 2011 and

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September 30, 2010, net unrealized depreciation on our long-term credit facility totaled \$2.7 million and \$14.0 million, respectively. PennantPark Investment uses a nationally recognized independent valuation services to measure the fair value of its credit facility in a manner consistent with the valuation process that the board of directors uses to value investments.

### 6. TRANSACTIONS WITH AFFILIATED COMPANIES

An affiliated company is a company in which we own 5% or more of the portfolio company's voting securities. A controlled affiliate is a company in which we own 25% or more of a portfolio company's voting securities. Advances to and distributions from affiliates are included in the Consolidated Statements of Cash Flow under purchases. Transactions related to our investments with both controlled and non-controlled affiliates for the six months ended March 31, 2011 were as follows:

| Name of Investment                                    | Fair Value at<br>September 30, 2010 | Advances to<br>affiliates | Distributions<br>from<br>affiliates | Income<br>Received  | Fair Value at<br>March 31, 2011 |
|---|-------------------------------------|---------------------------|-------------------------------------|---------------------|---------------------------------|
| <b>Controlled Affiliates</b>                          |                                     |                           |                                     |                     |                                 |
| SuttonPark Holdings, Inc.                             | \$ 8,000,100                        | \$ 3,000,000              | \$                                  | \$ 470,167          | \$ 11,000,000                   |
| <b>Non-Controlled Affiliates</b>                      |                                     |                           |                                     |                     |                                 |
| Performance Holdings, Inc.                            | 15,433,680                          |                           |                                     | 744,654             | 15,919,916                      |
| <b>Total Controlled and Non-Controlled Affiliates</b> | <b>\$ 23,433,780</b>                | <b>\$ 3,000,000</b>       | <b>\$</b>                           | <b>\$ 1,214,821</b> | <b>\$ 26,919,916</b>            |

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****MARCH 31, 2011****(Unaudited)****7. CHANGE IN NET ASSETS FROM OPERATIONS PER COMMON SHARE**

The following information sets forth the computation of basic and diluted net increase in net assets resulting from operations per share.

| Class and Year  | Three Months Ended<br>March 31, |                | Six Months Ended<br>March 31, |              |
|---|---------------------------------|----------------|-------------------------------|--------------|
|   | 2011                            | 2010           | 2011                          | 2010         |
| Numerator for net increase (decrease) in net assets resulting from operations               | \$ 13,586,987                   | \$ (3,031,143) | \$ 39,109,210                 | \$ 5,645,104 |
| Denominator for basic and diluted weighted average shares                                   | 41,312,021                      | 27,342,105     | 38,737,522                    | 26,538,003   |
| Basic and diluted net increase (decrease) in net assets resulting from operations per share | \$ 0.33                         | \$ (0.11)      | \$ 1.01                       | \$ 0.21      |

**8. CASH EQUIVALENTS**

Cash equivalents represent cash pending investment in longer-term portfolio holdings. Our portfolio may consist of temporary investments in U.S. Treasury Bills (of varying maturities), repurchase agreements, money market funds or repo-like treasury securities. These temporary investments with maturities of 90 days or less are deemed cash equivalents and are included in the Consolidated Schedule of Investments. At the end of each fiscal quarter, we may take proactive steps to preserve investment flexibility for the next quarter by investing in cash equivalents, which is dependent upon the composition of its total assets at quarter end. We may accomplish this in several ways, including purchasing U.S. Treasury Bills and closing out its positions on a net cash basis after quarter-end, temporarily drawing down on the credit facility or utilizing repurchase agreements or other balance sheet transactions as are deemed appropriate for this purpose. These amounts are excluded from average adjusted gross assets for purposes of computing management fee. U.S. Treasury Bills with maturities greater than 60 days from the time of purchase are marked-to-market consistent with our valuation policy. As of March 31, 2011 and September 30, 2010, cash equivalents consisted of \$1.5 million and \$1.8 million in money market products, respectively.

**9. FINANCIAL HIGHLIGHTS**

Our net assets and net asset value per share on March 31, 2011 and 2010 were \$514.0 million and \$349.2 million, respectively, and \$11.30 and \$11.07, respectively. Below are the financial highlights for the six months ended March 31, 2011 and 2010.

|   | Six Months Ended<br>March 31, |          |
|---|-------------------------------|----------|
|   | 2011                          | 2010     |
| <b>Per Share Data:</b>  |                               |          |
| Net asset value, beginning of period                                | \$ 10.69                      | \$ 11.85 |
| Net investment income <sup>(1)</sup>                                | 0.63                          | 0.54     |
| Net change in realized and unrealized gain (loss) <sup>(1)</sup>    | 0.38                          | (0.33)   |
| Net increase in net assets resulting from operations <sup>(1)</sup> | 1.01                          | 0.21     |
| Dividends to stockholders <sup>(1),(2)</sup>                        | (0.56)                        | (0.55)   |



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|   |                |                |
|---|----------------|----------------|
| Accretive (Dilutive) effect of common stock issuance            | 0.31           | (0.31)         |
| (Dilutive) effect of offering costs                             | (0.15)         | (0.13)         |
| Net asset value, end of period                                  | \$ 11.30       | \$ 11.07       |
| Per share market value, end of period                           | \$ 11.92       | \$ 10.37       |
| Total return <sup>*(3)</sup>                                    | 17.33%         | 34.54%         |
| Shares outstanding at end of period                             | 45,504,932     | 31,558,772     |
| <b>Ratios ** / Supplemental Data:</b>                           |                |                |
| Ratio of operating expenses to average net assets               | 7.46%          | 7.11%          |
| Ratio of credit facility related expenses to average net assets | 1.03%          | 1.05%          |
| Ratio of total expenses to average net assets                   | 8.49%          | 8.16%          |
| Ratio of net investment income to average net assets            | 11.25%         | 9.10%          |
| Net assets at end of period                                     | \$ 514,019,838 | \$ 349,211,898 |
| Average debt outstanding  | \$ 275,352,204 | \$ 231,791,209 |
| Average debt per share  | \$ 7.11        | \$ 8.73        |
| Portfolio turnover ratio  | 38.63%         | 9.23%          |

\* Not annualized for periods less than one year.

\*\* Annualized for periods less than one year.

(1) Per share data are calculated based on the weighted average shares outstanding for the respective periods.

(2) Distributions are determined based on taxable income calculated in accordance with income tax regulations, which may differ from amounts determined under accounting principles generally accepted in the United States of America.

(3) Total return is based on the change in market price per share during the period and takes into account distributions, if any, reinvested in accordance with our dividend reinvestment plan.

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****MARCH 31, 2011****(Unaudited)****10. CREDIT FACILITY AND SBA DEBENTURES***Credit Facility*

On June 25, 2007, PennantPark Investment entered into a senior secured revolving credit agreement, (the credit facility or our credit facility), with various lenders and SunTrust Bank, as administrative agent for the lenders. As of March 31, 2011 and September 30, 2010, there was \$152.8 million (including a \$1.1 million temporary draw) and \$233.1 million (including a \$5.2 million temporary draw) in outstanding borrowings under the credit facility, with a weighted average interest rate at the time of 1.31% and 1.34% exclusive of the fee on undrawn commitment of 0.20%, and \$162.2 million and \$66.9 million of unused borrowing capacity, respectively.

Our credit facility lenders agreed to extend credit to PennantPark Investment in an aggregate principal or face amount not exceeding \$315.0 million at any one time outstanding. The credit facility is a five-year revolving facility (with a stated maturity date of June 25, 2012) and pricing is set at 100 basis points over LIBOR. The credit facility contains customary affirmative and negative covenants, including the maintenance of a minimum stockholders' equity, the maintenance of a ratio not less than 200% of total assets (less total liabilities other than indebtedness) to total indebtedness, and restrictions on certain payments and issuance of debt. For a complete list of such covenants, see our report on Form 8-K, filed June 28, 2007 and on Form 10-Q, filed May 5, 2010. As of March 31, 2011, we were in compliance with our covenants relating to our credit facility.

*SBA Debentures*

SBIC LP is able to borrow funds from the SBA against regulatory capital (which approximates equity capital) that is paid-in and is subject to customary regulatory requirements including, but not limited to, an examination by the SBA. As of March 31, 2011, PennantPark Investment had committed to SBIC LP \$50.0 million and fully funded it. As of September 30, 2010, we had committed to SBIC LP \$50.0 million and funded it with equity capital of \$14.5 million. SBA debentures are non-recourse to us, have a 10-year maturity, and may be prepaid at any time without penalty. The interest rate of SBA debentures is fixed at the time of issuance, often referred to as pooling, at a market-driven spread over 10-year U.S. Treasury Notes.

Below is a summary of our borrowings outstanding with the SBA:

| Issuance Dates                | Maturity          | As of March 31, 2011   |                   | As of September 30, 2010 |                   |
|-------------------------------|-------------------|------------------------|-------------------|--------------------------|-------------------|
|                               |                   | All-in Coupon Rate (1) | Principal Balance | All-in Coupon Rate (1)   | Principal Balance |
| <b>Fixed SBA Debentures</b>   |                   |                        |                   |                          |                   |
| September 22, 2010            | September 1, 2020 | 3.50%                  | \$ 500,000        | 3.50%                    | \$ 500,000        |
| March 29, 2011                | March 1, 2021     | 4.46                   | 44,500,000        |                          |                   |
|                               |                   | 4.45%                  | \$ 45,000,000     | 3.50%                    | \$ 500,000        |
| <b>Interim SBA Debentures</b> |                   |                        |                   |                          |                   |
|                               |                   | 1.18%                  | \$ 14,500,000     | 0.84%                    | \$ 14,000,000     |
| <b>Total SBA Debentures</b>   |                   |                        |                   |                          |                   |
|                               |                   | 3.65%                  | \$ 59,500,000     | 0.93%                    | \$ 14,500,000     |

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|                                  |             |            |
|----------------------------------|-------------|------------|
| SBA Commitment                   | 100,000,000 | 33,500,000 |
| Available Undrawn SBA Commitment | 40,500,000  | 19,000,000 |

(1) Coupon rate excludes 3.43% of upfront fees.

Current SBA regulations limit the amount that SBIC LP may borrow to a maximum of \$150 million, which is up to twice its potential regulatory capital. This means that SBIC LP may access the maximum borrowing if it has \$75 million in regulatory capital. Under SBA regulations, SBIC LP is subject to regulatory requirements including making investments in SBA eligible businesses, investing at least 25% of regulatory capital in eligible smaller businesses, as defined under the 1958 Act, placing certain limitations on the financing terms of investments, prohibiting investing in certain industries, requiring capitalization thresholds and being subject to periodic audits and examinations. If our SBIC subsidiary fails to comply with applicable SBA regulations the SBA could, depending on the severity of the violation, limit or prohibit its use of debentures, declare outstanding debentures immediately due and payable and/or limit it from making new investments. These actions by the SBA would, in turn, negatively affect us because SBIC LP is wholly owned by us. As of March 31, 2011, SBIC LP was in compliance with all terms relating to our SBA debentures.

In connection with the filing of its SBA license application, PennantPark Investment applied for exemptive relief from the SEC to permit us to exclude the debt of SBIC LP from our consolidated asset coverage ratio. There can be no assurance that we will be able to capitalize SBIC LP with sufficient regulatory capital to access the maximum borrowing amount available or that we will receive an exemptive relief from the SEC with respect to the SBA-guaranteed debentures. If we are granted exemptive relief, our ratio of total assets on a consolidated basis to outstanding indebtedness may be greater than 200% which, while providing increased investment flexibility, would also increase our exposure to risks associated with leverage.

Our net asset value may decline as a result of economic conditions in the United States. Our continued compliance with the covenants under our credit facility and SBA debentures depend on many factors, some of which are beyond our control. Material net asset devaluation could have a material adverse effect on our operations and could require us to reduce our borrowings under our credit facility and SBA debentures in order to comply with certain covenants, including the ratio of total assets to total indebtedness.

### 11. COMMITMENTS AND CONTINGENCIES

From time to time, we, the Investment Adviser or the Administrator may be a party to legal proceedings in the ordinary course of business, including proceedings relating to the enforcement of our rights under contracts with our portfolio companies. While the outcome of these legal proceedings cannot be predicted with certainty, we do not expect that these proceedings will have a material effect upon our financial condition or results of operations. Unfunded debt investments described in the Consolidated Statement of Assets and Liabilities represent unfunded delayed draws on investments in first lien secured debt and subordinated debt investments.

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**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders

PennantPark Investment Corporation and subsidiaries

We have reviewed the accompanying consolidated statement of assets and liabilities of PennantPark Investment Corporation and subsidiaries (the Company), including the consolidated schedules of investments, as of March 31, 2011, and the consolidated statements of operations for the three and six months ended March 31, 2011 and 2010, changes in net assets, and cash flows for the six months ended March 31, 2011 and 2010. These interim consolidated financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the consolidated financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated statement of assets and liabilities of PennantPark Investment Corporation and subsidiaries, including the consolidated schedule of investments, as of September 30, 2010; and in our report dated November 17, 2010, we expressed an unqualified opinion on that financial statement and schedule.

New York, New York

May 4, 2011

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**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS  
FORWARD-LOOKING STATEMENTS**

This Report contains statements that constitute forward-looking statements, which relate to both us and our consolidated SBIC subsidiary regarding future events or our future performance or financial condition. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs and our assumptions. The forward-looking statements contained in this Report involve risks and uncertainties, including statements as to:

our future operating results;

our business prospects and the prospects of our prospective portfolio companies;

the dependence of our future success on the general economy and its impact on the industries in which we invest;

the impact of a protracted decline in the liquidity of credit markets on our business;

the impact of investments that we expect to make;

the impact of fluctuations in interest rates on our business;

our contractual arrangements and relationships with third parties;

the valuation of our investments in portfolio companies, particularly those having no liquid trading market;

the ability of our prospective portfolio companies to achieve their objectives;

our expected financings and investments;

the adequacy of our cash resources and working capital;

the timing of cash flows, if any, from the operations of our prospective portfolio companies; and

the ability of the Investment Adviser to locate suitable investments for us and to monitor and administer our investments.

We use words such as anticipates, believes, expects, intends, seeks and similar expressions to identify forward-looking statements. You should not place undue influence on the forward looking statements as our actual results could differ materially from those projected in the forward-looking statements for any reason, including the factors in Risk Factors and elsewhere in this Report.

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We have based the forward-looking statements included in this report on information available to us on the date of this Report, and we assume no obligation to update any such forward-looking statements. Although we undertake no obligation to revise or update any forward-looking statements in this Report, whether as a result of new information, future events or otherwise, you are advised to consult any additional disclosures that we may make directly to you or through reports that we in the future may file with the SEC, including, reports on Form 10-Q and current reports on Form 8-K.

The following analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes thereto contained elsewhere in this Report.

### Overview

PennantPark Investment Corporation is a business development company whose objectives are to generate both current income and capital appreciation through debt and equity investments primarily in U.S. middle-market companies in the form of senior secured loans, mezzanine debt and equity investments.

We believe the middle-market offers attractive risk-reward to investors due to the limited amount of capital available for such companies. We seek to create a diversified portfolio that includes senior secured loans, mezzanine debt and equity investments by investing approximately \$10 to \$50 million of capital, on average, in the securities of middle-market companies. We use the term *middle-market* to refer to companies with annual revenues between \$50 million and \$1 billion. We expect this investment size to vary proportionately with the size of our capital base. The companies in which we invest are typically highly leveraged, and, in most cases, are not rated by national rating agencies. If such companies were rated, we believe that they would typically receive a rating below investment grade (between BB and CCC under the Standard & Poor's system) from the national rating agencies. In addition, we expect our debt investments to generally range in maturity from three to ten years.

Our investment activity depends on many factors, including the amount of debt and equity capital available to middle-market companies, the level of merger and acquisition activity for such companies, the general economic environment and the competitive environment for the types of investments we make. Turmoil in the credit markets has adversely affected each of these factors and has resulted in a broad-based reduction in the demand for, and valuation of, middle-market debt instruments. These conditions have presented us with and may continue to offer attractive investment opportunities, as we believe that there are many middle-market companies that need senior secured and mezzanine debt financing. We have used, and expect to continue to use, our credit facility, the SBA debentures, proceeds from the rotation of our portfolio and proceeds from public and private offerings of securities to finance our investment objectives. In the future, we may also securitize a portion of our investments to raise investment capital.

### Organization and Structure of PennantPark Investment Corporation

PennantPark Investment Corporation was organized under the Maryland General Corporation Law in January 2007. We are a closed-end, externally managed, non-diversified investment company that has elected to be treated as a business development company under the 1940 Act. As such, we are required to comply with certain regulatory requirements. For instance, we generally have to invest at least 70% of our total assets in *qualifying assets*, including securities of U.S. private companies or thinly traded public companies, public companies with a market capitalization of less than \$250 million, cash, cash equivalents, U.S. government securities and high quality debt investments that mature in one year or less.

Our wholly owned subsidiary, PennantPark SBIC LP, was organized as a Delaware limited partnership on May 7, 2010 and received a license from the SBA to operate as an SBIC under Section 301(c) of the 1958 Act on July 30, 2010. The SBIC LP's investment objective is substantially similar to PennantPark Investment, generally co-investing in SBA eligible businesses that meet the investment criteria of PennantPark Investment.

Our investment activities are managed by PennantPark Investment Advisers. Under our Investment Management Agreement, we have agreed to pay our Investment Adviser an annual base management fee based on our average adjusted gross assets as well as an incentive fee based on our investment performance. PennantPark Investment, through the Investment Adviser, provides similar services to SBIC LP under a separate investment management agreement. The SBIC LP investment management agreement does not affect the management and incentive fees that we pay to the Investment Adviser on a consolidated basis. We have also entered into an Administration Agreement with PennantPark Investment Administration. Under our Administration Agreement, we have agreed to reimburse the Administrator for our allocable portion of overhead and other expenses incurred by the Administrator in performing its

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obligations under our Administration Agreement, including rent and our allocable portion of the costs of compensation and related expenses of our chief compliance officer, chief financial officer and their respective staffs. PennantPark Investment, through the Administrator, provides similar services to SBIC LP under separate administration agreement. Our board of directors, a majority of whom are independent of us and PennantPark Investment Advisers, supervises our activities.

### **Revenues**

We generate revenue in the form of interest income on the debt securities we hold and capital gains and distributions, if any, on investment securities that we may acquire in portfolio companies. Our debt investments, whether in the form of senior secured loans or mezzanine debt, typically have a term of three to ten years and bear interest at a fixed or floating rate. Interest on debt securities is generally payable quarterly or semiannually. In some cases, some of our investments provide for deferred interest payments or PIK. The principal amount of the debt securities and any accrued but unpaid interest generally becomes due at the maturity date. In addition, we may generate revenue in the form of commitment, origination, structuring or diligence fees, fees for providing managerial assistance and possibly consulting fees. Loan origination fees, original issue discount and market discount or premium are capitalized, and we accrete or amortize such amounts into income. We record contractual prepayment premiums on loans and debt securities as income. Dividend income, if any, is recognized on an accrual basis on the ex-dividend date to the extent that we expect to collect such amounts.

### **Expenses**

Our primary operating expenses include the payment of management fees to our Investment Adviser, our allocable portion of overhead under our Administration Agreement and other operating costs as detailed below. Our management fee compensates our Investment Adviser for its work in identifying, evaluating, negotiating, consummating and monitoring our investments. Additionally, we pay interest expense on the outstanding debt we accrue under our credit facility and SBA debentures. We bear all other direct or indirect costs and expenses of our operations and transactions, including:

the cost of calculating our net asset value, including the cost of any third-party valuation services;

the cost of effecting sales and repurchases of shares of our common stock and other securities;

fees payable to third parties relating to, or associated with, making investments, including fees and expenses associated with performing due diligence and reviews of prospective investments or complimentary businesses;

expenses incurred by the Investment Adviser in performing due diligence and reviews of investments;

transfer agent and custodial fees;

fees and expenses associated with marketing efforts;

federal and state registration fees and any stock exchange listing fees;

federal, state and local taxes;

independent directors' fees and expenses;

brokerage commissions;

fidelity bond, directors and officers/errors and omissions liability insurance and other insurance premiums;

direct costs such as printing, mailing, long distance telephone and staff;

fees and expenses associated with independent audits and outside legal costs;

costs associated with our reporting and compliance obligations under the 1940 Act, the 1958 Act and applicable federal and state securities laws; and

all other expenses incurred by either the Administrator or us in connection with administering our business, including payments under our Administration Agreement that will be based upon our allocable portion of overhead, and other expenses incurred by the Administrator in performing its obligations under our Administration Agreement, including rent and our allocable portion of the costs of compensation and related expenses of our chief compliance officer, chief financial officer and their respective staffs.

#### **PORTFOLIO AND INVESTMENT ACTIVITY**

As of March 31, 2011, our portfolio totaled \$758.7 million and consisted of \$303.7 million of senior secured loans, \$141.5 million of second lien secured debt, \$249.9 million of subordinated debt and \$63.6 million of preferred and common equity investments. Our portfolio consisted of 51% fixed rate investments, 37% variable rate investments with a LIBOR or prime floor and 12% variable rate investments. Overall, the portfolio had an unrealized appreciation of \$31.5 million. Our overall portfolio consisted of 47 companies with an average investment size of \$16.1 million, a weighted average yield on debt investments of 13.5%, and was invested 40% in senior secured loans, 19% in second lien secured debt, 33% in subordinated debt and 8% in preferred and common equity investments.

As of September 30, 2010, our portfolio totaled \$664.7 million and consisted of \$234.6 million of senior secured loans, \$156.7 million of second lien secured debt, \$223.9 million of subordinated debt and \$49.5 million of preferred and common equity investments. Our portfolio consisted of 49% fixed-rate investments, 26% variable rate investments with a LIBOR or prime floor and 25% variable rate investments. Overall, the portfolio had an unrealized appreciation of \$8.0 million. Our overall portfolio consisted of 43 companies with an average investment size of \$15.5 million, a weighted average yield on debt investments of 12.7%, and was invested 35% in senior secured loans, 24% in second lien secured debt, 34% in subordinated debt and 7% in preferred and common equity investments.

For the three months ended March 31, 2011, we invested \$96.6 million in four new and two existing portfolio companies with a weighted average yield on debt investments of 13.6%. Sales and repayments of long-term investments for the three months ended March 31, 2011 totaled \$51.6 million. For the six months ended March 31, 2011, we invested approximately \$196.5 million in ten new and three existing portfolio companies with a weighted average yield of 14.3% on debt investments. Sales and repayments of long-term investments totaled \$137.1 million for the same period.

For the three months ended March 31, 2010, we invested \$68.5 million in three new and four existing portfolio companies with a weighted average yield on debt investments of 13.7%. Sales and repayments of long term investments for the three months ended March 31, 2010 totaled \$6.7 million. For the six months ended March 31, 2010, we invested approximately \$119.0 million in nine new and six existing portfolio companies with a weighted average yield of 13.3% on debt investments. Sales and repayments of long-term investments totaled \$23.5 million for the same period.



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### **CRITICAL ACCOUNTING POLICIES**

The discussion of our financial condition and results of operation is based upon our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Changes in the economic environment, financial markets and any other parameters used in determining such estimates could cause actual results to differ. In addition to the discussion below, we describe our critical accounting policies in the notes to our consolidated financial statements.

#### **Valuation of Portfolio Investments**

Our board of directors generally uses market quotations to assess the value of our investments for which market quotations are readily available. We obtain these market values from independent pricing services or at the bid prices obtained from at least two broker/dealers if available, otherwise by a principal market maker or a primary market dealer. If the board of directors has a bona fide reason to believe any such market quote does not reflect the fair value of an investment, it may independently value such investments by using the valuation procedure that it uses with respect to assets for which market quotations are not readily available. Investments, of sufficient credit quality, purchased within 60 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates fair value.

We expect that there will not be readily available market values for most, if not all, of the investments which are or will be in our portfolio, and we value such investments at fair value as determined in good faith by or under the direction of our board of directors using a documented valuation policy, described herein, and a consistently applied valuation process. With respect to investments for which there is no readily available market value, the factors that the board of directors may take into account in pricing our investments at fair value include, as relevant, the nature and realizable value of any collateral, the portfolio company's ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business, comparison to publicly traded securities and other relevant factors. When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, we consider the pricing indicated by the external event to corroborate or revise our valuation. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material. See Note 5 to the consolidated financial statements.

With respect to investments for which market quotations are not readily available, or for which market quotations are deemed not reflective of the fair value, our board of directors undertakes a multi-step valuation process each quarter, as described below:

- (1) Our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals of the Investment Adviser responsible for the portfolio investment;
- (2) Preliminary valuation conclusions are then documented and discussed with the management of our Investment Adviser;
- (3) Our board of directors also engages independent valuation firms to conduct independent appraisals of our investments for which market quotations are not readily available or are readily available but deemed not reflective of the fair value of an investment. The independent valuation firms review management's preliminary valuations in light of their own independent assessment and also in light of any market quotations obtained from an independent pricing service, broker, dealer or market maker;
- (4) The audit committee of our board of directors reviews the preliminary valuations of the Investment Adviser and that of the independent valuation firms and responds and supplements the valuation recommendations of the independent valuation firms to reflect any comments; and
- (5) The board of directors discusses the valuations and determines the fair value of each investment in our portfolio in good faith, based on the input of our Investment Adviser, the independent valuation firms and the audit committee.

Fair Value Measurements, as defined under ASC 820, is the price that we would receive upon selling an investment or pay to transfer a liability in an orderly transaction to a market participant in the principal or most advantageous market for the investment or liability. ASC 820

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emphasizes that valuation techniques maximize the use of observable market inputs and minimize the use of unobservable inputs. Inputs refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of PennantPark Investment. Unobservable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on the best information available at the time.

ASC 820 classifies the inputs used to measure these fair values into the following hierarchies:

Level 1: Inputs that are quoted prices (unadjusted) in active markets for identical assets or liabilities, accessible by us at the measurement date.

Level 2: Inputs that are quoted prices for similar assets or liabilities in active markets, or that are quoted prices for identical or similar assets or liabilities in markets that are not active and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term, if applicable, of the financial instrument.

Level 3: Inputs that are unobservable for an asset or liability because they are based on our own assumptions about how market participants would price the asset or liability.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Generally, most of our investments and long-term credit facility are classified as Level 3.

The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes from brokers/dealers accompanied by disclaimer would result in classification as Level 3 information, assuming no additional corroborating evidence was available. Corroborating evidence that would result in classifying these non-binding broker/dealer bids as a level 2 asset includes, but is not limited to, observable market based transactions for the same or similar assets or other relevant observable market based inputs that may be used in pricing an asset.

Our investments are generally structured as debt and equity investments in the form of senior secured loans, mezzanine debt and equity co-investments. The transaction price, excluding transaction costs, is typically the best estimate of fair value at inception. When evidence supports a subsequent change to the carrying value from the original transaction price, adjustments are made to reflect the expected exit values. Ongoing reviews by our Investment Adviser and independent valuation firms are based on an assessment of each underlying investment, incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows and market-based information including comparable transactions, performance multiples and yields, among other factors. These non-public investments using unobservable inputs are included in Level 3 of the fair value hierarchy.

A review of fair value hierarchy classifications is conducted on a quarterly basis. Changes in the observability of valuation inputs may result in a reclassification for certain financial assets or liabilities. Reclassifications impacting Level 3 of the fair value hierarchy are reported as transfers in or out of the Level 3 category as of the end of the quarter in which the reclassifications occur.

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In addition to using the above inputs in cash equivalents, investments and long-term credit facility valuations, PennantPark Investment employs the valuation policy approved by its board of directors that is consistent with ASC 820 (See Note 2). Consistent with our valuation policy, PennantPark Investment evaluates the source of inputs, including any markets in which its investments are trading, in determining fair value.

### **Revenue Recognition**

We record interest income on an accrual basis to the extent that we expect to collect such amounts. For loans and debt investments with contractual PIK interest which represents contractual interest accrued and added to the loan balance that generally becomes due at maturity, we will generally not accrue PIK interest if the portfolio company valuation indicates that such PIK interest is not collectible. We do not accrue as a receivable interest on loans and debt investments if we determine that it is probable that we will not be able to collect such interest. Loan origination fees, original issue discount, market discount or premium and deferred financing costs on our debt are capitalized, and we then amortize such amounts as interest income or expense as applicable. We record contractual prepayment premiums on loans and debt investments as income. Dividend income, if any, is recognized on an accrual basis on the ex-dividend date to the extent that we expect to collect such amounts.

### **Net Realized Gains or Losses and Net Change in Unrealized Appreciation or Depreciation**

We measure realized gains or losses by the difference between the net proceeds from the repayment or sale and the amortized cost basis of the investment, using the specific identification method, without regard to unrealized appreciation or depreciation previously recognized, but considering unamortized upfront fees and prepayment penalties. Net change in unrealized appreciation or depreciation reflects the change in portfolio investment values during the reporting period, including any reversal of previously recorded unrealized appreciation or depreciation, when gains or losses are realized.

### **Payment-in-Kind Interest, or PIK**

We have investments in our portfolio which contain a PIK interest provision. PIK interest is added to the principal balance of the investment and is recorded as income. For us to maintain our status as a RIC, substantially all of this income must be paid out to stockholders in the form of dividends, even though we have not collected any cash with respect to PIK securities.

### **Federal Income Taxes**

We operate so as to qualify to maintain our election to be taxed as a RIC under Subchapter M of the Code and intend to continue to do so. In order to qualify as a RIC and to not be subject to corporate-level tax on income, we are required, under Subchapter M of the Code, to distribute at least 90% of the sum of our ordinary income and realized net short-term capital gains, if any to our stockholders on an annual basis. Although not required for us to maintain our RIC tax status, we must also distribute an amount at least equal to the sum of 98% of our ordinary income (during each calendar year) plus 98.2% of our net capital gains (during each 12 month period ending on October 31) to avoid a 4% excise tax.

Because federal income tax regulations differ from GAAP, distributions in accordance with tax regulations may differ from net investment income and realized gains recognized for financial reporting purposes. Differences may be permanent or temporary. Permanent differences are reclassified among capital accounts in the financial statements to reflect their tax character. Temporary differences arise when certain items of income, expense, gain or loss are recognized at some time in the future. Differences in classification may also result from the treatment of short-term gains as ordinary income for tax purposes.

## **RESULTS OF OPERATIONS**

Set forth below are the results of operations for the three and six months ended March 31, 2011 and 2010.

### **Investment Income**

Investment income for the three and six months ended March 31, 2011 was \$22.7 million and \$42.7 million, respectively, and was primarily attributable to \$8.0 million and \$15.1 million from senior secured loans, \$2.8 million and \$6.0 million from second lien secured debt investments, and \$8.6 million and \$16.3 million from subordinated debt investments, respectively. This compares to investment income for the three and six months ended March 31, 2010, which was \$13.5 million and \$27.1 million, respectively, and was primarily attributable to \$3.2 million and \$6.7 million from senior secured loans, \$3.3 million and \$6.5 million from second lien secured debt investments and \$5.9 million and \$11.3 million from subordinated debt investments, respectively. The increase in investment income compared with the same period in the prior year is due to the growth of our portfolio and rotation out of our lower yielding investments.

## Expenses

Expenses for the three and six months ended March 31, 2011, totaled \$9.6 million and \$18.4 million, respectively. Base management fee for the same respective periods totaled \$3.6 million and \$7.1 million, performance-based incentive fees totaled \$3.3 million and \$6.1 million, credit facility and SBA debentures expenses totaled \$1.1 million and \$2.2 million, general and administrative expenses totaled \$1.5 million and \$2.8 million, respectively, and excise tax for the six months ended March 31, 2011 totaled \$0.2 million. This compares to expenses for the three and six months ended March 31, 2010, which totaled \$6.5 million and \$12.8 million, respectively. Base management fee for the same respective periods totaled \$2.8 million and \$5.3 million, performance-based incentive fees totaled \$1.8 million and \$3.6 million, credit facility expenses totaled \$0.8 million and \$1.6 million, general and administrative expenses totaled \$1.1 million and \$2.2 million, respectively, and excise tax for the six months ended March 31, 2010 totaled \$0.1 million. The increase in expenses is due to the growth of both the portfolio and net investment income.

## Net Investment Income

Net investment income totaled \$13.2 million and \$24.3 million, or \$0.32 and \$0.63 per share, for the three and six months ended March 31, 2011, respectively. For the same respective periods in the prior year, net investment income totaled \$7.1 million and \$14.3 million, or \$0.26 and \$0.54 per share.

## Net Realized Gains or Losses

Sales and repayments of long-term investments for the three and six months ended March 31, 2011 totaled \$51.6 million and \$137.1 million, and realized gains totaled \$0.3 million and \$2.6 million, respectively, due to sales of lower yielding investments and refinancing of our debt investments. Sales and repayments of long-term investments for the three and six months ended March 31, 2010 totaled \$6.7 million and \$23.5 million, and realized losses totaled \$0.1 million and \$16.7 million, respectively, due to sales and repayments of our debt investments.

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### **Net Change in Unrealized Appreciation or Depreciation on Investments and Credit Facility**

For the three and six months ended March 31, 2011, our investments had a net change in unrealized appreciation of \$4.8 million and \$23.5 million, respectively. For the three and six months ended March 31, 2010, our investments had a net change in unrealized appreciation of \$9.9 million and \$33.8 million, respectively. The decrease in the net change in unrealized appreciation compared to the prior year is the result of changes in the leveraged credit markets over the comparable periods. On March 31, 2011 and September 30, 2010, net unrealized appreciation on investments totaled \$31.5 million and \$8.0 million, respectively.

For the three and six months ended March 31, 2011, our long-term credit facility had a net change in unrealized appreciation of \$4.7 million and \$11.3 million, respectively. For the three and six months ended March 31, 2010, our long-term credit facility had a net change in unrealized appreciation of \$19.9 million and \$25.7 million, respectively. The net change in unrealized appreciation over the prior year is the result of the credit facility approaching maturity and the reduced borrowings outstanding. On March 31, 2011 and September 30, 2010, net unrealized depreciation on our long-term credit facility totaled \$2.7 million and \$14.0 million, respectively.

### **Net Increase in Net Assets Resulting from Operations**

Net increase in net assets resulting from operations totaled \$13.6 million and \$39.1 million, respectively, or \$0.33 per share and \$1.01 per share, respectively, for the three and six months ended March 31, 2011. This compares to a net (decrease) increase in net assets resulting from operations which totaled \$(3.0) million and \$5.6 million, respectively, or \$(0.11) per share or \$0.21 per share, for the three and six months ended March 31, 2010. This increase in net assets from operations is due to the continued growth in net investment income which is a result of growing our portfolio offset by the appreciation in the value of our long-term credit facility as it approaches maturity.

## **LIQUIDITY AND CAPITAL RESOURCES**

Our liquidity and capital resources are derived from our credit facility, SBA debentures and cash flows from operations, including investment sales and repayments, and income earned. Our primary use of funds from operations includes investments in portfolio companies and other operating expenses we incur. We used, and expect to continue to use, these capital resources as well as proceeds from rotation within our portfolio and from public and private offerings of securities to finance our investment objectives.

As of March 31, 2011 and September 30, 2010, we had \$162.2 million and \$66.9 million, respectively, of unused borrowing capacity under our credit facility, subject to maintenance of the applicable total assets to debt ratio of 200%, maintenance of a blended percentage of the values of our portfolio companies and restrictions on certain payments and issuance of debt.

On June 25, 2007, PennantPark Investment entered into its credit facility, among us, various lenders and SunTrust Bank, as administrative agent for the lenders. SunTrust Robinson Humphrey Capital Markets acted as the joint lead arranger and JPMorgan Chase (Chase Lincoln First Commercial as successor in interest of Bear Stearns Corporate Lending Inc.) acted as joint lead arranger and syndication agent. As of March 31, 2011 and September 30, 2010, there were \$152.8 million (including a \$1.1 million temporary draw) and \$233.1 million (including a \$5.2 million temporary draw) in outstanding borrowings under the credit facility, with a weighted average interest rate at the time of 1.31% and 1.34%, exclusive of the fee on undrawn commitment of 0.20%, respectively.

Under the credit facility, the lenders agreed to extend us credit in an initial aggregate principal or face amount not exceeding \$315.0 million outstanding at any one time. The credit facility is a five-year revolving facility (with a stated maturity date of June 25, 2012) and is secured by substantially all of our investment portfolio assets, except for those assets of SBIC LP. Pricing of borrowings under our credit facility is set at 100 basis points over LIBOR.

The credit facility contains affirmative and restrictive covenants, including but not limited to maintenance of a minimum shareholders' equity of the greater of (i) 40% of the total assets of PennantPark Investment and its subsidiaries as of the last day of any fiscal quarter and (ii) the sum of (A) \$120,000,000 plus (B) 25% of the net proceeds from the sale of equity interests in PennantPark Investment and its subsidiaries after the closing date of the credit facility and maintenance of a ratio of total assets (less total liabilities other than indebtedness) to total indebtedness, in each case of PennantPark Investment, of not less than 2.0:1.0 (excluding any exemptive relief granted by the SEC with respect to the indebtedness of any SBIC subsidiary). In addition to the asset coverage ratio described in the preceding sentence, borrowings under our credit facility (and the incurrence of certain other permitted debt) are subject to compliance with a borrowing base that applies different advance rates to different types of assets in PennantPark Investment's portfolio. As of March 31, 2011, PennantPark Investment was in compliance with the terms of its credit facility.

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We may raise additional equity or debt capital through both registered offerings off a shelf registration and private offerings of securities, by securitizing a portion of our investments or borrowing from the SBA through our SBIC subsidiary, among other considerations. Any future additional debt capital we incur, to the extent it is available under current credit market conditions, may be issued at a higher cost and on less favorable terms and conditions than our current credit facility. We continuously monitor conditions in the credit markets and seek opportunities to enhance our debt structure as our credit facility matures in June 2012. Furthermore, our availability under the credit facility depends on various covenants and restrictions discussed in the preceding paragraph. The primary uses of existing funds and any funds raised in the future is expected to be for repayment of indebtedness, investments in portfolio companies, cash distributions to our shareholders and other general corporate purposes.

On February 11, 2011, we sold 9.2 million shares of our common stock at a price of \$12.40 per share resulting in net proceeds of \$108.3 million. This compares to selling 5.75 million shares at a price of \$10.00 per share resulting in net proceeds of \$54.3 million for the same period in the prior year.

As of March 31, 2011, we had committed to SBIC LP \$50.0 million, funded it with equity capital of \$50.0 million, had SBA debentures outstanding of \$59.5 million with a weighted average interest rate of 3.65%, exclusive of 3.43% of upfront fees, and had \$40.5 million remaining unused borrowing capacity subject to customary regulatory requirements. As of September 30, 2010, we had committed to SBIC LP \$50.0 million, funded it with equity capital of \$14.5 million, had SBA debentures outstanding of \$14.5 million with a weighted average interest rate at the time of 0.93%, exclusive of 3.43% of upfront fees, and had \$19 million remaining unused borrowing capacity. SBA debentures are non-recourse to us, have a 10-year maturity, and may be prepaid at any time without penalty. The interest rate of SBA debentures is fixed at the time of issuance, often referred to as pooling, at a market-driven spread over 10-year U.S. Treasury Notes. SBA current regulations limit the amount that SBIC LP may borrow to a maximum of \$150 million, which is up to twice its potential regulatory capital. This means that SBIC LP may access the maximum borrowing if it has \$75 million in regulatory capital.

As of March 31, 2011, SBIC LP had a debenture commitment from the SBA in the amount of \$100.0 million with \$59.5 million outstanding. Of the \$59.5 million of SBA debentures outstanding, \$45.0 million is fixed for 10-years with a rate of 4.45%, inclusive of the SBA annual fee, and \$14.5 million is temporary financing currently bearing a weighted average rate of 1.18% that will reset to a market-driven rate in September 2011 and will remain fixed thereafter for 10 years.

The SBIC program is designed to stimulate the flow of capital into eligible businesses. Under SBA regulations, SBIC LP is subject to regulatory requirements including making investments in SBA eligible businesses, investing at least 25% of regulatory capital in eligible smaller businesses, as defined under the 1958 Act, placing certain limitations on the financing terms of investments, prohibiting investment in certain industries, requiring capitalization thresholds that limit distributions to us, and is subject to periodic audits and examinations. As of March 31, 2011, SBIC LP was in compliance with its regulatory requirements.

In connection with the filing of its SBA license application, PennantPark Investment has applied for exemptive relief from the SEC to permit us to exclude the debt of SBIC LP from our consolidated asset coverage ratio. There can be no assurance that we will be able to capitalize SBIC LP with sufficient regulatory capital to borrow the maximum amount available or that we will receive an exemptive relief from the SEC with respect to the SBA-guaranteed debentures.

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If we are granted exemptive relief, our ratio of total assets on a consolidated basis outstanding to indebtedness may be greater than 200% which, while providing increased investment flexibility, would also increase our exposure to risks associated with leverage.

As of March 31, 2011, we had approximately \$57.6 million of assets bearing a coupon of 9% or lower. We will seek to rotate out of these assets into new, higher yielding investments over time.

Our operating activities used cash of \$54.5 million for the six months ended March 31, 2011, and our financing activities provided cash of \$54.2 million for the same period, primarily from net repayments under our credit facility, SBA debentures issued, and our common stock offering.

Our operating activities used cash of \$78.8 million for the six months ended March 31, 2010, and our financing activities provided cash of \$46.5 million for the same period, primarily from our common stock offering.

**Contractual Obligations**

A summary of our significant contractual payment obligations as of March 31, 2011 including, but not limited to, borrowings under our multi-currency \$315.0 million, five-year, revolving credit facility maturing in June 2012 are as follows:

|   | Payments due by period (in millions) |                     |              |              |                      |
|---|--------------------------------------|---------------------|--------------|--------------|----------------------|
|   | Total                                | Less than<br>1 year | 1-3<br>years | 3-5<br>years | More than<br>5 years |
| Senior secured revolving credit facility <sup>(1)</sup> | \$ 152.8                             | \$                  | \$ 152.8     | \$           | \$                   |
| SBA debentures <sup>(2)</sup>                           | 59.5                                 |                     |              |              | 59.5                 |
| Subtotal debt outstanding <sup>(3)</sup>                | 212.3                                |                     | 152.8        |              | 59.5                 |
| Unfunded investments <sup>(4)</sup>                     | 18.6                                 |                     | 18.6         |              |                      |
| Total contractual obligations                           | \$ 230.9                             | \$                  | \$ 171.4     | \$           | \$ 59.5              |

- (1) As of March 31, 2011, we had \$162.2 million of unused borrowing capacity under our credit facility, subject to maintenance of the applicable total assets to debt ratio of 200%, maintenance of a blended percentage of the values of our portfolio companies and restrictions on certain payments and issuance of debt.
- (2) As of March 31, 2011, SBIC LP had \$40.5 million of unused borrowing capacity under SBIC LP's commitment from the SBA.
- (3) The weighted average interest rate on the total debt outstanding as of March 31, 2011 is 1.97% exclusive of the fee on the undrawn commitment of 0.20% on the credit facility and 3.43% of upfront fees on SBIC LP's SBA debentures.
- (4) Unfunded debt investments described in the Consolidated Statement of Assets and Liabilities represent unfunded delayed draws on investments in first lien secured debt and subordinated debt investments.

We have entered into certain contracts under which we have material future commitments. Under our Investment Management Agreement, which was renewed in February 2011, PennantPark Investment Advisers serves as our investment adviser in accordance with the terms of that Investment Management Agreement. PennantPark Investment, through the Investment Adviser, provides similar services to SBIC LP under its investment management agreement with SBIC LP. The SBIC LP investment management agreement does not affect the management or incentive fees that we pay to the Investment Adviser on a consolidated basis. Payments under our Investment Management Agreement in each reporting period is equal to (1) a management fee equal to a percentage of the value of our gross assets and (2) an incentive fee based on our performance. See Note 3 to the consolidated financial statements.

Under our Administration Agreement, which was renewed in February 2011, PennantPark Investment Administration furnishes us with office facilities and administrative services necessary to conduct our day-to-day operations. PennantPark Investment, through the Administrator, provides similar services to SBIC LP under an administration agreement with SBIC LP, which is intended to have no effect on the consolidated administration fee. We, through the Administrator, provide administrative and managerial assistance to our controlled affiliate, SuttonPark Holdings, Inc. If requested to provide managerial assistance to our portfolio companies, we or PennantPark Investment Administration will be paid an additional amount based on the services provided. Payment under our Administration Agreement is based upon our allocable portion of the Administrator's overhead in performing its obligations under our Administration Agreement, including rent, technology systems, insurance

and our allocable portion of the costs of our chief compliance officer, chief financial officer and their respective staffs. See Note 3 to the consolidated financial statements.

If any of our contractual obligations discussed above are terminated, our costs under new agreements that we enter into may increase. In addition, we will likely incur significant time and expense in locating alternative parties to provide the services we expect to receive under our Investment Management Agreement and our Administration Agreement. Any new Investment Management Agreement would also be subject to approval by our stockholders.

#### **Off-Balance Sheet Arrangements**

We currently engage in no off-balance sheet arrangements, including any risk management of commodity pricing or other hedging practices.

#### **Distributions**

In order to qualify as a RIC and to not be subject to corporate-level tax on income, we are required, under Subchapter M of the Code, to distribute at least 90% of the sum of our ordinary income and realized net short-term capital gains, if any, to our stockholders on an annual basis. Although not required for us to maintain our RIC tax status, we must also distribute an amount at least equal to the sum of 98% of our ordinary income (during each calendar year) plus 98.2% of our net capital gains (during each 12 month period ending on October 31) to avoid a 4% excise tax. For the six months ended March 31, 2011 and 2010, we have elected to retain a portion of our calendar year income and record an excise tax of \$0.2 million and \$0.1 million, respectively.

During the three and six months ended March 31, 2011, we declared distributions of \$0.27 and \$0.53 per share, respectively, for total distributions of \$12.3 million and \$21.7 million, respectively. For the same periods in the prior year, we declared distributions of \$0.26 and \$0.51 per share, respectively, for total distributions of \$8.2 million and \$14.7 million, respectively. We monitor available net investment income to determine if a tax return of capital may occur for the fiscal year. To the extent our taxable earnings fall below the total amount of our distributions for any given fiscal year, a portion of those distributions may be deemed to be a tax return of capital to our common stockholders. Tax characteristics of all distributions will be reported to stockholders on Form 1099-DIV after the end of the calendar year.

We intend to continue to distribute quarterly dividends to our stockholders. Our quarterly dividends, if any, are determined by our board of directors.



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We can offer no assurance that we will achieve results that will permit the payment of any cash distributions and, if we issue senior securities, we will be prohibited from making distributions if doing so causes us to fail to maintain the asset coverage ratios stipulated by the 1940 Act or if distributions are limited by the terms of any of our borrowings.

We maintain an opt out dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend, then stockholders' cash dividends will be automatically reinvested in additional shares of our common stock, unless they specifically opt out of the dividend reinvestment plan so as to receive cash dividends.

In January 2010, the Internal Revenue Service issued a revenue procedure that temporarily allows a RIC to distribute its own stock as a dividend for the purpose of fulfilling its distribution requirements. Pursuant to this revenue procedure, a RIC may treat a distribution of its own stock as a dividend if (1) the stock is publicly traded on an established securities market, (2) the distribution is declared with respect to a taxable year ending on or before December 31, 2011 and (3) each shareholder may elect to receive his or her entire distribution in either cash or stock of the RIC subject to a limitation on the aggregate amount of cash to be distributed to all shareholders, which must be at least 10% of the aggregate declared distribution. If too many shareholders elect to receive cash, each shareholder electing to receive cash will receive a pro rata amount of cash (with the balance of the distribution paid in stock). In no event will any shareholder electing to receive cash receive less than 10% of his or her entire distribution in cash. We have not elected to distribute stock as a dividend but reserve the right to do so.

We may not be able to achieve operating results that will allow us to make dividends and distributions at a specific level or to increase the amount of these dividends and distributions from time to time. In addition, we may be limited in our ability to make dividends and distributions due to the asset coverage test for borrowings applicable to us as a business development company under the 1940 Act and/or due to provisions in future credit facilities. If we do not distribute a certain percentage of our income annually, we will suffer adverse tax consequences, including possible loss of RIC status. We cannot assure stockholders that they will receive any dividends and distributions at a particular level.

### **Item 3. Quantitative And Qualitative Disclosures About Market Risk**

We are subject to financial market risks, including changes in interest rates. During the period covered by this report, many of the loans in our portfolio had floating interest rates. These loans are usually based on a floating LIBOR rate and typically have durations of three months, after which they reset to current market interest rates.

Assuming that the balance sheet as of March 31, 2011 was to remain constant, and no actions were taken to alter the existing interest rate sensitivity, a hypothetical immediate 1% change in interest rates may affect net income by more than 1% over a one-year horizon. Although management believes that this measure is indicative of our sensitivity to interest rate changes, it does not adjust for potential changes in the credit market, credit quality, size and composition of the assets on the balance sheet and other business developments that could affect the net change in net assets resulting from operations, or net income. Accordingly, no assurances can be given that actual results would not differ materially from the statement above.

Because we borrow money to make investments, our net investment income is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest these funds. In periods of declining interest rates, our cost of funds would decrease, which may reduce our net investment income. As a result, there can be no assurance that a significant change in market interest rates will not have a material adverse effect on our net investment income.

We may hedge against interest rate fluctuations by using standard hedging instruments such as futures, options and forward contracts subject to the requirements of the 1940 Act. While hedging activities may insulate us against adverse changes in interest rates, they may also limit our ability to participate in benefits of lower interest rates with respect to our portfolio of investments with fixed interest rates. During the periods covered by this Report, we did not engage in interest rate hedging activities.

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

As of the period covered by this Report, we, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the 1934 Act). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective and provided reasonable assurance that information required to be disclosed in our periodic SEC filings is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions

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regarding required disclosure. However, in evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of such possible controls and procedures.

**Table of Contents****PART II OTHER INFORMATION****Item 1. Legal Proceedings**

Neither we nor our Investment Adviser nor our Administrator is currently subject to any material legal proceedings, nor, to our knowledge, is any material legal proceeding threatened against us, our Investment Adviser or Administrator. From time to time, we, our Investment Adviser or Administrator, may be a party to certain legal proceedings in the ordinary course of business, including proceedings relating to the enforcement of our rights under contracts with our portfolio companies. While the outcome of these legal proceedings cannot be predicted with certainty, we do not expect that these proceedings will have a material effect upon our financial condition or results of operations.

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should consider carefully the factors discussed in Part I Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended September 30, 2010, which could materially affect our business, financial condition and/or operating results. The risks described in our Annual Report on Form 10-K are not the only risks facing us. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition and/or operating results.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Submission of Matters to a Vote of Security Holders**

On February 1, 2011, PennantPark Investment Corporation (the Company) held its annual meeting of stockholders (the Annual Meeting). On February 3, 2011 the Company reported that at the Annual Meeting, the Company's stockholders approved two of three proposals. The proposals are described in detail in the Company's definitive proxy statement for the Annual Meeting as filed with the Securities and Exchange Commission on December 7, 2010. Votes were cast as follows:

**Proposal 1.** The two directors were re-elected pursuant to the voting results set forth below:

| Name             | For        | Withheld | Broker<br>Non-Vote |
|------------------|------------|----------|--------------------|
| Marshall Brozost | 18,152,090 | 888,035  | 12,816,497         |
| Samuel L. Katz   | 18,705,888 | 334,237  | 12,816,497         |

**Proposal 2.** The Company's stockholders ratified the selection of KPMG LLP to serve as the Company's independent registered public accounting firm for the year ending September 30, 2011, as set forth below:

| For        | Against | Abstain |
|------------|---------|---------|
| 31,725,951 | 89,119  | 41,552  |

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**Proposal 3.** The Company's stockholders did not approve a proposal to authorize flexibility for the Company, with the approval of its Board of Directors, to sell shares of its common stock (during the 12 months subsequent to the date of the Annual Meeting) at a price below its then current net asset value per share subject to certain limitations as described the proxy statement. The proposal failed pursuant to the voting results set forth below:

|           | With Affiliates |                               | Without Affiliates |                               |
|-----------|-----------------|-------------------------------|--------------------|-------------------------------|
|           | Total Voted     | % of<br>Outstanding<br>Shares | Total Voted        | % of<br>Outstanding<br>Shares |
| For       | 15,244,768      | 42.08%                        | 14,460,027         | 40.89%                        |
| Against   | 3,645,047       | 10.06%                        | 3,645,047          | 10.31%                        |
| Abstain   | 150,310         | 0.41%                         | 90,210             | 0.26%                         |
| Not voted | 12,816,497      | 35.38%                        | 12,816,497         | 36.23%                        |

**Item 5. Other Information**

None.

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**Item 6. Exhibits**

Unless specifically indicated otherwise, the following exhibits are incorporated by reference to exhibits previously filed with the SEC:

- 3.1 Articles of Incorporation (Incorporated by reference to the Registrant's Pre-Effective Amendment No.1 to the Registration Statement on Form N-2/A (File No. 333-140092), filed on March 5, 2007).
- 3.2 Amended and Restated Bylaws of the Registrant (Incorporated by reference to Exhibit 3.2 to Form N-2 (File No. 333-172525), filed on April 15, 2011).
- 4.1 Form of Share Certificate (Incorporated by reference to Exhibit 99(d)(1) to the Registrant's Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
- 11 Computation of Per Share Earnings (included in the notes to the audited consolidated financial statements contained in this Report).
- 31.1 \* Certification of Chief Executive Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
- 31.2 \* Certification of Chief Financial Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
- 32.1 \* Certification of Chief Executive Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
- 32.2 \* Certification of Chief Financial Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
- 99.1 Privacy Policy of the Registrant (Incorporated by reference to Exhibit 99.1 to the Registrant's Annual Report on Form 10-K (File No. 814-00736), filed on December 13, 2007).

\* Filed herewith.

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**SIGNATURES**

Pursuant to the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this Report on Form 10-Q to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: May 4, 2011

PENNANTPARK INVESTMENT CORPORATION

By: */s/ Arthur H. Penn*  
**Arthur H. Penn**  
**Chief Executive Officer**

Date: May 4, 2011

By: */s/ Aviv Efrat*  
**Aviv Efrat**  
**Chief Financial Officer**

**(Principal Accounting and Financial Officer)**