GLADSTONE CAPITAL CORP
Form POS 8C
June 04, 2012
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As filed with the Securities and Exchange Commission on June 4, 2012

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

1933 Act File No. 333-162592

Form N-2

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

PRE-EFFECTIVE AMENDMENT NO.	¨
POST-EFFECTIVE AMENDMENT NO. 7	x

GLADSTONE CAPITAL CORPORATION

(Exact name of registrant as specified in charter)

1521 WESTBRANCH DRIVE, SUITE 200

MCLEAN, VA 22102

(Address of principal executive offices)

Registrant s telephone number, including area code: (703) 287-5800

DAVID GLADSTONE

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

GLADSTONE CAPITAL CORPORATION

1521 WESTBRANCH DRIVE, SUITE 200

MCLEAN, VIRGINIA 22102

(Name and address of agent for service)

COPIES TO:

THOMAS R. SALLEY

DARREN K. DESTEFANO

COOLEY LLP

ONE FREEDOM SQUARE

RESTON TOWN CENTER

11951 FREEDOM DRIVE

RESTON, VIRGINIA 20190

(703) 456-8000

(703) 456-8100 (facsimile)

Approximate date of proposed public offering: From time to time after the effective date of this registration statement.

If any securities being registered on this form will be offered on a delayed or continuous basis in reliance on Rule 415 under the Securities Act of 1933, as amended, other than securities offered in connection with a dividend reinvestment plan, check the following box. x

It is proposed that this filing will become effective (check appropriate box):

x When declared effective pursuant to Section 8(c).

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to Section 8(a), may determine.

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The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED June 4, 2012

PROSPECTUS

$300,000,000

COMMON STOCK

PREFERRED STOCK

SUBSCRIPTION RIGHTS

WARRANTS

DEBT SECURITIES

We may offer, from time to time, up to $300,000,000 aggregate initial offering price of our common stock, $0.001 par value per share, preferred stock, $0.001 par value per share, subscription rights, warrants representing rights to purchase shares of our common stock, or debt securities, or a combined offering of these securities, which we refer to in this prospectus collectively as our Securities, in one or more offerings. The Securities may be offered at prices and on terms to be disclosed in one or more supplements to this prospectus. In the case of our common stock and warrants or rights to acquire such common stock hereunder, the offering price per share of our common stock by us, less any underwriting commissions or discounts, will not be less than the net asset value per share of our common stock at the time of the offering except (i) in connection with a rights offering to our existing common stockholders, (ii) with the consent of the holders of the majority of our outstanding stock, or (iii) under such other circumstances as the Securities and Exchange Commission may permit. You should read this prospectus and the applicable prospectus supplement carefully before you invest in our Securities.

Our Securities may be offered directly to one or more purchasers, including existing stockholders in a rights offering, through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See Plan of Distribution. We may not sell any of our Securities through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of such Securities. Our common stock is traded on The NASDAQ Global Select Market (NASDAQ) under the symbol GLAD. As of May 31, 2012, the last reported sales price for our common stock was $7.40. Our 7.125% Series 2016 Term Preferred Stock is also traded on the NASDAQ under the symbol GLADP. As of May 31, 2012, the last reported sales price for our 7.125% Series 2016 Term Preferred Stock was $25.89.

This prospectus contains information you should know before investing, including information about risks. Please read it before you invest and keep it for future reference. Additional information about us, including our annual, quarterly and current reports, has been filed with the Securities and Exchange Commission. This information is available free of charge on our corporate website located at *www.gladstonecapital.com*. See Additional Information. This prospectus may not be used to consummate sales of securities unless accompanied by a prospectus supplement.

An investment in our Securities involves certain risks, including, among other things, risks relating to investments in securities of small, private and developing businesses. We describe some of these risks in the section entitled Risk Factors, which begins on page 8. Common shares of closed-end investment companies frequently trade at a discount to their net asset value and this may increase the risk of loss to purchasers of our Securities. You should carefully consider these risks together with all of the other information contained in this prospectus and any prospectus supplement before making a decision to purchase our Securities.

The Securities being offered have not been approved or disapproved by the Securities and Exchange Commission or any state securities commission nor has the Securities and Exchange Commission or any state securities commission passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

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We have not authorized any dealer, salesman or other person to give any information or to make any representation other than those contained or incorporated by reference in this prospectus or any accompanying supplement to this prospectus. You must not rely upon any information or representation not contained or incorporated by reference in this prospectus or the accompanying prospectus supplement as if we had authorized it. This prospectus and any prospectus supplement do not constitute an offer to sell or a solicitation of any offer to buy any security other than the registered securities to which they relate, nor do they constitute an offer to sell or a solicitation of an offer to buy any securities in any jurisdiction to any person to whom it is unlawful to make such an offer or solicitation in such jurisdiction. The information contained in this prospectus and any prospectus supplement is accurate as of the dates on their respective covers only. Our business, financial condition, results of operations and prospects may have changed since such dates.

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PROSPECTUS SUMMARY

The following summary contains basic information about this offering. It likely does not contain all the information that is important to an investor. For a more complete understanding of this offering, we encourage you to read this entire document and the documents to which we have referred. Except where the context suggests otherwise, the terms we, us, our, the Company and Gladstone Capital refer to Gladstone Capital Corporation; Adviser refers to Gladstone Management Corporation; Administrator refers to Gladstone Administration, LLC; Gladstone Commercial refers to Gladstone Commercial Corporation; Gladstone Investment refers to Gladstone Investment Corporation; Gladstone Land refers to Gladstone Land Corporation; Gladstone Securities refers to Gladstone Securities, LLC; and Gladstone Companies refers to our Adviser and its affiliated companies.

GLADSTONE CAPITAL CORPORATION

General

We were incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001 and completed our initial public offering on August 24, 2001. We operate as a closed-end, non-diversified management investment company and we have elected to be treated as a business development company (BDC) under the Investment Company Act of 1940, as amended (the 1940 Act). For federal income tax purposes, we have elected to be treated as a regulated investment company (RIC) under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code). We currently continue to qualify as a RIC for federal income tax purposes and obtain favorable RIC tax treatment by meeting certain requirements, including certain minimum distribution requirements.

We seek to invest in small and medium-sized private United States (U.S.) businesses that meet certain criteria, including some but not necessarily all of the following: the potential for growth in cash flow, adequate assets for loan collateral, experienced management teams with a significant ownership interest in the borrower, profitable operations based on the borrower s cash flow, reasonable capitalization of the borrower (usually by leveraged buyout funds or venture capital funds) and the potential to realize appreciation and gain liquidity in our equity positions, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering of the borrower s stock or by exercising our right to require the borrower to repurchase our warrants. However, there can be no assurance that we will always have these rights. We lend to borrowers that need funds to finance growth, restructure their balance sheets or effect a change of control. We invest either by ourselves or jointly with other funds or management of the borrower, depending on the opportunity. If we are participating in an investment with one or more co-investors, our investment is likely to be smaller than if we were to investing alone. Our loans typically range from $5 million to $20 million and generally mature in no more than seven years.

Because the majority of the loans in our portfolio consist of term debt of private U.S. companies that typically cannot or will not expend the resources to have their debt securities rated by a credit rating agency, we expect that most, if not all, of the debt securities we acquire will be unrated. Investors should assume that these loans would be at rates below what is today considered investment grade quality. Investments rated below investment grade are often referred to as high yield securities or junk bonds and may be considered high risk as compared to investment-grade debt instruments.

Our Investment Strategy

We were established to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes and senior subordinated notes, of established private U.S. businesses that are substantially owned by leveraged buyout funds, individual investors or are family-owned businesses, with a particular focus on senior notes. In addition, we may acquire from others existing loans that meet this profile. We also seek to provide our stockholders with long-term capital growth through appreciation in the value of warrants or other equity instruments that we may receive when we make loans.

We expect that our target portfolio over time will primarily include the following three categories of investments in private U.S. companies:

Senior Loans: We seek to invest a portion of our assets in senior notes of borrowers. Using its assets as collateral, the borrower typically uses senior notes to cover a substantial portion of the funding needed to operate. The collateral usually takes the form of first priority liens on the assets of the portfolio company. Senior lenders are exposed to the least risk of all providers of debt because they command a senior position with respect to scheduled interest and principal payments and assets of the borrower. However, unlike senior subordinated lenders, these senior lenders typically do not receive any stock, warrants to purchase stock of the borrowers or other yield enhancements. As such, they generally do not participate in the equity appreciation of the value of the business. Senior notes may include revolving lines of credit, senior term loans, senior syndicated loans and senior last-out tranche loans and generally are at variable interest rates in relation to the London Interbank Offered Rate (LIBOR). These loans typically are structured with interest rate floors to protect against declining interest rates.

Senior Subordinated Loans: We seek to invest a portion of our assets in senior subordinated notes, which include second lien notes. Holders of senior subordinated notes, which are typically unsecured, are subordinated to the rights of holders of senior debt in their right to receive principal and interest payments or, in the case of last out tranches of senior debt, liquidation proceeds from the borrower. As a result, senior subordinated notes are riskier than senior notes. Although such loans are sometimes secured by significant collateral (assets of the borrower), the lender is largely dependent on the borrower s cash flow for repayment. Additionally, lenders may receive warrants to acquire shares of stock in borrowers or other yield enhancements in connection with these loans. Senior subordinated notes include second lien loans and syndicated second lien loans. We typically structure these senior subordinated loans with variable interest rates in relation to the LIBOR with interest rate floors to protect against declining interest rates.

Junior Subordinated Loans: We also seek to invest a small portion of our assets in junior subordinated notes, which include mezzanine notes. Holders of junior subordinated notes are subordinated to the rights of the holders of senior debt and senior subordinated debt in their rights to receive principal and interest payments from the borrower and the assets of the borrower. The risk profile of junior subordinated notes is high, which permits the junior subordinated lender to obtain higher variable interest rates and more equity and equity-like compensation.

Preferred and Common Equity/Equivalents: While not a primary focus of our investment strategy, from time to time we also receive yield enhancements in connection with some of our loans, which include warrants to purchase stock or success fees. A portion of our portfolio consists of equity investments that were part of a larger initial investment in a private company. Additionally, we also have equity investments derived from restructurings on some of our investments.

Our Investment Adviser and Administrator

Gladstone Management Corporation (our Adviser) is our affiliate, investment adviser, and a privately-held company led by a management team which has extensive experience in our lines of business. Our Adviser s affiliate, a privately-held company, Gladstone Administration, LLC (our Administrator), employs our chief financial officer, chief compliance officer, internal legal counsel and their respective staffs. Excluding our chief financial officer and treasurer and chief accounting officer, all of our executive officers serve as directors or executive officers, or both, of the following of our affiliates: Gladstone Commercial Corporation (Gladstone Commercial), a publicly-traded real estate investment trust; Gladstone Investment Corporation (Gladstone Investment), a publicly-traded BDC and RIC; our Adviser; and our Administrator. Our chief financial officer and treasurer also serves as an executive officer of Gladstone Investment.

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Our Adviser and Administrator also provide investment advisory and administrative services, respectively, to certain of our affiliates, including, but not limited to, Gladstone Commercial; Gladstone Investment; Gladstone Partners Fund, L.P. (Gladstone Partners), a private partnership fund formed primarily to co-invest with us and Gladstone Investment; Gladstone Land Corporation (Gladstone Land), a private agricultural real estate company owned by David Gladstone, our chairman and chief executive officer; and Gladstone Lending Corporation (Gladstone Lending), a private corporation that was formed to primarily invest in first and second lien term loans that has filed a registration statement on Form N-2 with the Securities and Exchange Commission (the SEC), but which has not yet commenced operations. Our Adviser and Administrator may provide investment advisory and administrative services, respectively, to other funds and companies, both public and private.

We have been externally managed by our Adviser pursuant to an investment advisory agreement since October 1, 2004. Our Adviser was organized as a corporation under the laws of the State of Delaware on July 2, 2002, and is a registered investment adviser under the Investment Advisers Act of 1940, as amended. Our Adviser is headquartered in McLean, Virginia, a suburb of Washington, D.C., and also has offices in several other states.

THE OFFERING

We may offer, from time to time, up to $300,000,000 of our Securities, on terms to be determined at the time of the offering. Our Securities may be offered at prices and on terms to be disclosed in one or more prospectus supplements. In the case of an offering of our common stock and warrants or rights to acquire such common stock hereunder in any offering, the offering price per share, exclusive of any underwriting commission or discount, will not be less than the net asset value per share of our common stock at the time of the offering except (i) in connection with a rights offering to our existing stockholders, (ii) with the consent of the majority of our common stockholders, or (iii) under such other circumstances as the SEC may permit. If we were to sell shares of our common stock below our then current net asset value per share, such sales would result in an immediate dilution to the net asset value per share. This dilution would occur as a result of the sale of shares at a price below the then current net asset value per share of our common stock and a proportionately greater decrease in a stockholder s interest in our earnings and assets and voting interest in us than the increase in our assets resulting from such issuance.

Our Securities may be offered directly to one or more purchasers, including existing stockholders in a rights offering, by us or through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will disclose the terms of the offering, including the name or names of any agents or underwriters involved in the sale of our Securities by us, the purchase price, and any fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See Plan of Distribution. We may not sell any of our Securities through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of our Securities.

Set forth below is additional information regarding the offering of our Securities:

Common Stock Trading Symbol (NASDAQ)	GLAD
7.125% Series 2016 Term Preferred Stock Trading Symbol (NASDAQ)	GLADP

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Use of Proceeds	Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds from the sale of our Securities first to pay down existing short-term debt, then to make investments in small and mid-sized companies in accordance with our investment objective, with any remaining proceeds to be used for other general corporate purposes. See Use of Proceeds.
Dividends and Distributions	We have paid monthly distributions to the holders of our common stock since October 2003 (and prior to that quarterly distributions since January 2002) and generally intend to continue to do so. We made our first distribution on our term preferred stock in December of 2011 and have made monthly distributions thereafter. The amount of monthly distributions on our common stock is determined by our board of directors (the Board of Directors) on a quarterly basis and is based on our estimate of our annual investment company taxable income and net short-term taxable capital gains, if any. See Price Range of Common Stock and Distributions. Certain additional amounts may be deemed as distributed to stockholders for income tax purposes. Other types of securities we might offer will likely pay distributions in accordance with their terms.
Taxation	We intend to continue to elect to be treated for federal income tax purposes as a RIC. So long as we continue to qualify, we generally will pay no corporate-level federal income taxes on any ordinary income or capital gains that we distribute to our stockholders. To maintain our RIC status, we must meet specified source-of-income and asset diversification requirements and distribute annually at least 90% of our taxable ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, out of assets legally available for distribution. See Material U.S. Federal Income Tax Considerations.
Trading at a Discount	Common shares of closed-end investment companies frequently trade at a discount to their net asset value. The possibility that our common shares may trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per common share may decline. We cannot predict whether our common shares will trade above, at or below net asset value, although during the past three years, our common stock has often traded, and at times significantly, below net asset value.
Certain Anti-Takeover Provisions	Our Board of Directors is divided into three classes of directors serving staggered three-year terms. This structure is intended to provide us with a greater likelihood of continuity of management, which may be necessary for us to realize the full value of our investments. A staggered board of directors also may serve to deter hostile takeovers or proxy contests, as may certain provisions of Maryland law and other measures we have adopted. See Certain Provisions of Maryland Law and of Our Articles of Incorporation and Bylaws.
Dividend Reinvestment Plan	We have a dividend reinvestment plan for our common stockholders. This is an opt in dividend reinvestment plan,

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	meaning that stockholders may elect to have their cash dividends automatically reinvested in additional shares of our common stock. Stockholders who do not so elect will receive their dividends in cash. Stockholders who receive distributions in the form of stock will be subject to the same federal, state and local tax consequences as stockholders who elect to receive their distributions in cash. See Dividend Reinvestment Plan.
Management Arrangements	Gladstone Management Corporation serves as our investment adviser, and Gladstone Administration, LLC serves as our administrator. For a description of our Adviser, our Administrator, the Gladstone Companies and our contractual arrangements with these companies, see Management Certain Transactions Investment Advisory and Management Agreement, Management Certain Transactions Administration Agreement and Management Certain Transactions Loan Servicing Agreement.

FEES AND EXPENSES

The following table is intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by us or Gladstone Capital, or that we will pay fees or expenses, stockholders will indirectly bear such fees or expenses as investors in Gladstone Capital. The following annualized percentages were calculated based on actual expenses incurred in the quarter ended March 31, 2012 and average net assets for the quarter ended March 31, 2012.

Stockholder Transaction Expenses:	
Sales load (as a percentage of offering price)	%
Dividend reinvestment plan expenses(1)	None
Annual expenses (as a percentage of net assets attributable to common stock:	
Management fees(2)	2.97%
Incentive fees payable under investment advisory and management agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income)(3)	0.63%
Interest payments on borrowed funds(4)	2.26%
Dividend expense on mandatorily redeemable preferred stock (5)	1.53%
Other expenses(6)	2.11%
Total annual expenses(2)(6)	9.50%

(1) The expenses of the reinvestment plan are included in stock record expenses, a component of other expenses. We do not have a cash purchase plan. The participants in the dividend reinvestment plan will bear a pro rata share of brokerage commissions incurred with respect to open market purchases, if any. See Dividend Reinvestment Plan for information on the dividend reinvestment plan.

(2) Our annual base management fee is 2.0% (0.5% quarterly) of our average gross assets, which are defined as total assets of Gladstone Capital, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings. For the three months ended March 31, 2012, our Adviser voluntarily agreed to waive the annual base management fee of 2.0% to 0.5% for those senior syndicated loan participations that we purchase using borrowings from our credit facility. Although there can be no guarantee that our Adviser will continue to waive any portion of the fees due under the amended and restated investment advisory agreement (Advisory Agreement), on an annual basis after giving effect

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to this waiver, the estimated management fees as a percentage of net assets attributable to common stock were 2.74% and the total estimated annual expenses as a percentage of net assets attributable to common stock were 9.28%. See Management Certain Transactions Investment Advisory and Management Agreement.

(3) The incentive fee consists of two parts: an income-based fee and a capital gains-based fee. The income-based fee is payable quarterly in arrears, and equals 20.0% of the excess, if any, of our pre-incentive fee net investment income that exceeds a 1.75% quarterly (7.0% annualized) hurdle rate of our net assets, subject to a catch-up provision measured as of the end of each calendar quarter. The catch-up provision requires us to pay 100% of our pre-incentive fee net investment income with respect to that portion of such income, if any, that exceeds the hurdle rate but is less than 125.0% of the quarterly hurdle rate (or 2.1875%) in any calendar quarter (8.75% annualized). The catch-up provision is meant to provide our Adviser with 20.0% of our pre-incentive fee net investment income as if a hurdle rate did not apply when our pre-incentive fee net investment income exceeds 125.0% of the quarterly hurdle rate in any calendar quarter (8.75% annualized). The income-based incentive fee is computed and paid on income that may include interest that is accrued but not yet received in cash. Our pre-incentive fee net investment income used to calculate this part of the income-based incentive fee is also included in the amount of our gross assets used to calculate the 2.0% base management fee (see footnote 2 above). The capital gains-based incentive fee equals 20.0% of our net realized capital gains since our inception, if any, computed net of all realized capital losses and unrealized capital depreciation since our inception, less any prior payments, and is payable at the end of each fiscal year. We have not recorded any capital gains-based incentive fee from our inception through March 31, 2012.

From time to time, our Adviser has voluntarily agreed to waive a portion of the incentive fees to the extent net investment income did not cover 100% of the distributions to common stockholders during the period. However, there can be no guarantee that our Adviser will waive any portion of the fees under the Advisory Agreement in the future.

Examples of how the incentive fee would be calculated are as follows:

Assuming pre-incentive fee net investment income of 0.55%, there would be no income-based incentive fee because such income would not exceed the hurdle rate of 1.75%.

Assuming pre-incentive fee net investment income of 2.00%, the income-based incentive fee would be as follows:

= 100% × (2.00% - 1.75%)

= 0.25%

Assuming pre-incentive fee net investment income of 2.30%, the income-based incentive fee would be as follows:

= (100% × (catch-up : 2.1875% - 1.75%)) + (20% × (2.30% - 2.1875%))

= (100% × 0.4375%) + (20% × 0.1125%)

= 0.4375% + 0.0225%

= 0.46%

Assuming net realized capital gains of 6% and realized capital losses and unrealized capital depreciation of 1%, the capital gains-based incentive fee would be as follows:

= 20% × (6% - 1%)

= 20% × 5%

= 1%

For a more detailed discussion of the calculation of the two-part incentive fee, see Management Certain Transactions Investment Advisory and Management Agreement.

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(4) Includes deferred financing costs. We renewed our revolving credit facility for a three year period, effective January 19, 2012, under which our borrowing capacity is $137.0 million. We have drawn down on this credit facility and we expect to borrow additional funds in the future up to an amount so that our asset coverage, as defined in the 1940 Act, is at least 200% after each issuance of our senior securities. Assuming that we borrowed $137.0 million at an interest rate of 5.25% plus an additional fee related to borrowings of 0.50%, for an aggregate rate of 5.75%, interest payments and amortization of deferred financing costs on borrowed funds would have been 3.80% of our average net assets for the quarter ended March 31, 2012.

(5) In November 2011, we completed a public offering of 7.125% Series 2016 Term Preferred Stock, par value $0.001 per share, at a public offering price of $25.00 per share. In the offering, we issued approximately 1.5 million shares of 7.125% Series 2016 Term Preferred Stock. Dividend expense includes the amounts paid to preferred stockholders during the three months ended March 31, 2012. Also included in this line item is the amortization of the offering costs related to our term preferred stock offering. In addition, See Management Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Series 2016 Term Preferred Stock for additional information.

(6) Includes our overhead expenses, including payments under the administration agreement based on our projected allocable portion of overhead and other expenses incurred by our Administrator in performing its obligations under the administration agreement. See Management Certain Transactions Administration Agreement.

Example

The following example demonstrates the projected dollar amount of total cumulative expenses that would be incurred over various periods with respect to a hypothetical investment in our Securities. In calculating the following expense amounts, we have assumed that our annual operating expenses would remain at the levels set forth in the table above. The amounts set forth below do not reflect the impact of sales load. In the event that securities to which this prospectus related are sold to or through underwriters, a corresponding prospectus supplement will restate this example to reflect the applicable sales load.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$ 100	$ 285	$ 452	$ 802

While the example assumes, as required by the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. Additionally, we have assumed that the entire amount of such 5% annual return would constitute ordinary income as we have not historically realized positive capital gains (computed net of all realized capital losses) on our investments. Because the assumed 5% annual return is significantly below the hurdle rate of 7% (annualized) that we must achieve under the investment advisory and management agreement to trigger the payment of an income-based incentive fee, we have assumed, for purposes of the above example, that no income-based incentive fee would be payable if we realized a 5% annual return on our investments. Additionally, because the capital gains-based incentive fee is calculated on a cumulative basis (computed net of all realized capital losses and unrealized capital depreciation) and because of the significant capital losses realized to date, we have assumed that we will not trigger the payment of any capital gains-based incentive fee in any of the indicated time periods. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our expenses, and returns to our investors after such expenses, would be higher than reflected in the example. The expenses you would pay, based on a $1,000 investment and assuming a 5% annual return resulting entirely from net realized capital gains (disregarding for purposes of this example all net historical realized losses and aggregate unrealized depreciation) (and therefore subject to the capital gains-based incentive fee), and otherwise making the same assumptions in the example above, would be: 1 year, $109; 3 years, $308; 5 years, $484; and 10 years, $841. In addition, while the example assumes reinvestment of all dividends and distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the dividend payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the dividend. See Dividend Reinvestment Plan for additional information regarding our dividend reinvestment plan.

This example and the expenses in the table above should not be considered a representation of our future expenses, and actual expenses (including the cost of debt, incentive fees, if any, and other expenses) may be greater or less than those shown.

ADDITIONAL INFORMATION

We have filed with the SEC a registration statement on Form N-2 under the Securities Act of 1933, as amended, which we refer to as the Securities Act, with respect to the Securities offered by this prospectus. This prospectus, which is a part of the registration statement, does not contain all of the information set forth in the registration statement or exhibits and schedules thereto. For further information with respect to our business and our Securities, reference is made to the registration statement, including the amendments, exhibits and schedules thereto.

We also file reports, proxy statements and other information with the SEC under the Securities Exchange Act of 1934, as amended, which we refer to as the Exchange Act. Such reports, proxy statements and other information, as well as the registration statement and the amendments, exhibits and schedules thereto, can be inspected at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. Information about the operation of the public reference facilities may be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains a website that contains reports, proxy statements and other information regarding registrants, including us, that file such information electronically with the SEC. The address of the SEC s website is *http://www.sec.gov*. Copies of such material may also be obtained from the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates. Our common stock is listed on the NASDAQ and our corporate website is located at *www.gladstonecapital.com*. The information contained on, or accessible through, our website is not a part of this prospectus.

We make available free of charge on our website our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC.

We also furnish to our stockholders annual reports, which include annual financial information that has been examined and reported on, with an opinion expressed, by our independent registered public accounting firm. See Experts.

RISK FACTORS

You should carefully consider the risks described below and all other information provided and incorporated by reference in this prospectus (or any prospectus supplement) before making a decision to purchase our Securities. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties not presently known to us, or not presently deemed material by us, may also impair our operations and performance. If any of the following risks actually occur, our business, financial condition or results of operations could be materially adversely affected. If that happens, the trading price of our Securities could decline, and you may lose all or part of your investment.

Risks Related to the Economy

The current state of the economy and the capital markets increases the possibility of adverse effects on our financial position and results of operations. Continued economic adversity could impair our portfolio

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companies financial positions and operating results and affect the industries in which we invest, which could, in turn, harm our operating results. Continued adversity in the capital markets could impact our ability to raise capital and reduce our volume of new investments.

We believe that the U.S. is continuing to recover from the recession that largely began in late 2007. While economic conditions generally appear to be improving, we remain cautious about a long-term economic recovery. The recession in general, and the disruptions in the capital markets in particular, have impacted our liquidity options and increased the cost of debt and equity capital. As a result, we do not know if adverse conditions will again intensify, and we are unable to gauge the full extent to which the disruptions will continue to affect us. The longer these uncertain conditions persist, the greater the probability that these factors could continue to increase our costs of, and significantly limit our access to, debt and equity capital and, thus, have an adverse effect on our operations and financial results. Many of our portfolio companies and the companies we may invest in the future are also susceptible to these unstable economic conditions, which may affect the ability of one or more of our portfolio companies to repay our loans or engage in a liquidity event, such as a sale, recapitalization or initial public offering. These unstable economic conditions could also disproportionately impact some of the industries in which we invest, causing us to be more vulnerable to losses in our portfolio, which could cause the number of non-performing assets to increase and the fair value of our portfolio to decrease. The unstable economic conditions may also decrease the value of collateral securing some of our loans as well as the value of our equity investments which would decrease our ability to borrow under our line of credit or raise equity capital, thereby further reducing our ability to make new investments.

In November 2011, we completed an offering of 1.5 million shares of 7.125% Series 2016 Term Preferred Stock (the Series 2016 Term Preferred Stock); however, there can be no assurance that we will be able to raise additional equity capital in the near future. See Management Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Series 2016 Term Preferred Stock for additional information.

The unstable economic conditions have affected the availability of credit generally. We do not know when market conditions will stabilize, if adverse conditions will intensify or the full extent to which the disruptions will continue to affect us. Also, it is possible that persistent instability of the financial markets could have other unforeseen material effects on our business.

The recent downgrade of the United States credit rating and the ongoing economic crisis in Europe could negatively impact our liquidity, financial condition and earnings.

Recent U.S. debt ceiling and budget deficit concerns, together with signs of deteriorating sovereign debt conditions in Europe, have increased the possibility of additional credit-rating downgrades and economic slowdowns. Although U.S. lawmakers passed legislation to raise the federal debt ceiling, Standard & Poor s Ratings Services lowered its long-term sovereign credit rating on the U.S. from AAA to AA+ in August 2011. The impact of this or any further downgrades to the U.S. government s sovereign credit rating, or its perceived creditworthiness, and the impact of the current crisis in Europe with respect to the ability of certain European Union countries to continue to service their sovereign debt obligations is inherently unpredictable and could adversely affect the U.S. and global financial markets and economic conditions. There can be no assurance that governmental or other measures to aid economic recovery will be effective. These fairly recent developments, and the government s credit concerns in general, could cause interest rates and borrowing costs to rise, which may negatively impact our ability to access the debt markets on favorable terms. In addition, the decreased credit rating could create broader financial turmoil and uncertainty, which may weigh heavily on our stock price. Continued adverse economic conditions could have a material adverse effect on our business, financial condition and results of operations.

We may experience fluctuations in our quarterly and annual results based on the impact of inflation in the United States.

The majority of our portfolio companies are in industries that are directly impacted by inflation, such as consumer goods and services and manufacturing. Our portfolio companies may not be able to pass on to customers

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increases in their costs of operations which could greatly affect their operating results, impacting their ability to repay our loans. In addition, any projected future decreases in our portfolio companies operating results due to inflation could adversely impact the fair value of those investments. Any decreases in the fair value of our investments could result in future unrealized losses and therefore reduce our net assets resulting from operations.

Risks Related to Our External Management

We are dependent upon our key management personnel and the key management personnel of our Adviser, particularly David Gladstone, George Stelljes III and Terry Lee Brubaker, and on the continued operations of our Adviser, for our future success.

We have no employees. Our chief executive officer, president and chief investment officer, chief operating officer, chief financial officer, and the employees of our Adviser, do not spend all of their time managing our activities and our investment portfolio. We are particularly dependent upon David Gladstone, George Stelljes III and Terry Lee Brubaker in this regard. Our executive officers and the employees of our Adviser allocate some, and in some cases, a material portion, of their time to businesses and activities that are not related to our business. We have no separate facilities and are completely reliant on our Adviser, which has significant discretion as to the implementation and execution of our business strategies and risk management practices. We are subject to the risk of discontinuation of our Adviser s operations or termination of the Advisory Agreement and the risk that, upon such event, no suitable replacement will be found. We believe that our success depends to a significant extent upon our Adviser and that discontinuation of its operations could have a material adverse effect on our ability to achieve our investment objectives.

Our incentive fee may induce our Adviser to make certain investments, including speculative investments.

The management compensation structure that has been implemented under the Advisory Agreement may cause our Adviser to invest in high-risk investments or take other risks. In addition to its management fee, our Adviser is entitled under the Advisory Agreement to receive incentive compensation based in part upon our achievement of specified levels of income. In evaluating investments and other management strategies, the opportunity to earn incentive compensation based on net income may lead our Adviser to place undue emphasis on the maximization of net income at the expense of other criteria, such as preservation of capital, maintaining sufficient liquidity, or management of credit risk or market risk, in order to achieve higher incentive compensation. Investments with higher yield potential are generally riskier or more speculative. This could result in increased risk to the value of our investment portfolio.

We may be obligated to pay our Adviser incentive compensation even if we incur a loss.

The Advisory Agreement entitles our Adviser to incentive compensation for each fiscal quarter in an amount equal to a percentage of the excess of our investment income for that quarter (before deducting incentive compensation, net operating losses and certain other items) above a threshold return for that quarter. When calculating our incentive compensation, our pre-incentive fee net investment income excludes realized and unrealized capital losses that we may incur in the fiscal quarter, even if such capital losses result in a net loss on our statement of operations for that quarter. Thus, we may be required to pay our Adviser incentive compensation for a fiscal quarter even if there is a decline in the value of our portfolio or we incur a net loss for that quarter. For additional information on incentive compensation under the Advisory Agreement with our Adviser, see Business Investment Advisory and Management Agreements Management services and fees under the Advisory Agreement.

Our Adviser s failure to identify and invest in securities that meet our investment criteria or perform its responsibilities under the Advisory Agreement may adversely affect our ability for future growth.

Our ability to achieve our investment objectives will depend on our ability to grow, which in turn will depend on our Adviser s ability to identify and invest in securities that meet our investment criteria.

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Accomplishing this result on a cost-effective basis will be largely a function of our Adviser s structuring of the investment process, its ability to provide competent and efficient services to us, and our access to financing on acceptable terms. The senior management team of our Adviser has substantial responsibilities under the Advisory Agreement. In order to grow, our Adviser will need to hire, train, supervise, and manage new employees successfully. Any failure to manage our future growth effectively could have a material adverse effect on our business, financial condition, and results of operations.

There are significant potential conflicts of interest which could impact our investment returns.

Our executive officers and directors, and the officers and directors of our Adviser, serve or may serve as officers, directors, or principals of entities that operate in the same or a related line of business as we do or of investment funds managed by our affiliates. Accordingly, they may have obligations to investors in those entities, the fulfillment of which might not be in the best interests of us or our stockholders. For example, Mr. Gladstone, our chairman and chief executive officer, is the chairman of the board and chief executive officer of our Adviser, Gladstone Investment, Gladstone Commercial, Gladstone Lending and the chairman, chief executive officer and the sole stockholder of Gladstone Land. In addition, Mr. Brubaker, our vice chairman, chief operating officer and secretary is the vice chairman, chief operating officer and secretary of our Adviser, Gladstone Investment, Gladstone Commercial, Gladstone Land and Gladstone Lending. Mr. Stelljes, our president and chief investment officer, is also the president and chief investment officer of our Adviser, Gladstone Lending and Gladstone Land and vice chairman and chief investment officer of Gladstone Commercial and vice chairman and chief investment officer of Gladstone Investment. Moreover, our Adviser may establish or sponsor other investment vehicles which from time to time may have potentially overlapping investment objectives with those of ours and accordingly may invest in, whether principally or secondarily, asset classes similar to those we target. While our Adviser generally has broad authority to make investments on behalf of the investment vehicles that it advises, our Adviser has adopted investment allocation procedures to address these potential conflicts and intends to direct investment opportunities to the Gladstone affiliate with the investment strategy that most closely fits the investment opportunity. Nevertheless, the management of our Adviser may face conflicts in the allocation of investment opportunities to other entities managed by our Adviser. As a result, it is possible that we may not be given the opportunity to participate in certain investments made by other members of the Gladstone Companies or investment funds managed by investment managers affiliated with our Adviser.

In certain circumstances, we may make investments in a portfolio company in which one of our affiliates has or will have an investment, subject to satisfaction of any regulatory restrictions and, where required, to the prior approval of our Board of Directors. Our Board of Directors has approved the following types of co-investment transactions:

- Our affiliate, Gladstone Commercial, may lease property to portfolio companies that we do not control under certain circumstances. We may pursue such transactions only if (i) the portfolio company is not controlled by us or any of our affiliates, (ii) the portfolio company satisfies the tenant underwriting criteria of Gladstone Commercial, and (iii) the transaction is approved by a majority of our independent directors and a majority of the independent directors of Gladstone Commercial. We expect that any such negotiations between Gladstone Commercial and our portfolio companies would result in lease terms consistent with the terms that the portfolio companies would be likely to receive were they not portfolio companies of ours.

- We may invest simultaneously with our affiliate Gladstone Investment in senior syndicated loans whereby neither we nor any affiliate has the ability to dictate the terms of the loans.

- Additionally, pursuant to an exemptive order granted by the SEC, our Adviser may sponsor a private investment fund to co-invest with either us or Gladstone Investment in accordance with the terms and conditions of the order. We have also submitted an application for an exemptive order from the SEC that, if granted would supersede the existing exemptive order and expand our ability to co-invest with certain affiliates by permitting us, under certain circumstances, to co-invest with Gladstone Investment, Gladstone Partners, Gladstone Lending and any future BDC or closed-end management investment company that is advised by our Adviser (or sub-advised by our Adviser if it controls the fund) or any combination of the foregoing.

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Certain of our officers, who are also officers of our Adviser, may from time to time serve as directors of certain of our portfolio companies. If an officer serves in such capacity with one of our portfolio companies, such officer will owe fiduciary duties to all stockholders of the portfolio company, which duties may from time to time conflict with the interests of our stockholders.

In the course of our investing activities, we will pay management and incentive fees to our Adviser and will reimburse our Administrator for certain expenses it incurs. As a result, investors in our common stock will invest on a gross basis and receive distributions on a net basis after expenses, resulting in, among other things, a lower rate of return than one might achieve through our investors themselves making direct investments. As a result of this arrangement, there may be times when the management team of our Adviser has interests that differ from those of our stockholders, giving rise to a conflict. In addition, as a BDC, we make available significant managerial assistance to our portfolio companies and provide other services to such portfolio companies. Although, neither we nor our Adviser currently receives fees in connection with managerial assistance, our Adviser and Gladstone Securities have, at various times, provided other services to certain of our portfolio companies and received fees for these other services. For example, during the year ended September 30, 2011, certain of our portfolio companies contracted directly with our Adviser for the provision of various consulting services and with Gladstone Securities for the provision of investment banking and due diligence services, in each case, in return for fees.

Our Adviser is not obligated to provide a waiver of the base management fee, which could negatively impact our earnings and our ability to maintain our current level of distributions to our common stockholders.

The Advisory Agreement provides for a base management fee based on our gross assets. Since our 2007 fiscal year, our Board of Directors has accepted on a quarterly basis voluntary, unconditional and irrevocable waivers to reduce the annual 2.0% base management fee on senior syndicated loan participations to 0.5% to the extent that proceeds resulting from borrowings were used to purchase such syndicated loan participations, and any waived fees may not be recouped by our Adviser in the future. However, our Adviser is not required to issue these or other waivers of fees under the Advisory Agreement, and to the extent our investment portfolio grows in the future, we expect these fees will increase. If our Adviser does not issue these waivers in future quarters, it could negatively impact our earnings and may compromise our ability to maintain our current level of distributions to our common stockholders, which could have a material adverse impact on the price of our common stock.

Our business model is dependent upon developing and sustaining strong referral relationships with investment bankers, business brokers and other intermediaries.

We are dependent upon informal relationships with investment bankers, business brokers and traditional lending institutions to provide us with deal flow. If we fail to maintain our relationship with such funds or institutions, or if we fail to establish strong referral relationships with other funds, we will not be able to grow our portfolio of loans and fully execute our business plan.

Risks Related to Our External Financing

In addition to regulatory limitations on our ability to raise capital, our credit facility contains various covenants which, if not complied with, could accelerate our repayment obligations under the facility, thereby materially and adversely affecting our liquidity, financial condition, results of operations and ability to pay distributions.

In January 2012, we renewed our fourth amended and restated credit agreement, which provides for a $137.0 million revolving line of credit arranged by Key Equipment Finance Inc. (Keybank) as administrative agent (the Credit Facility). Branch Banking and Trust Company (BB&T) and ING Capital LLC (ING) are also committed lenders under the Credit Facility. Subject to certain terms and conditions, the Credit Facility may

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be expanded up to $237.0 million through the addition of other committed lenders to the facility. However, if additional lenders are unwilling to join the facility on its terms, we will be unable to expand the facility and thus will continue to have limited availability to finance new investments under our line of credit. The Credit Facility matures on January 18, 2015, and, if the facility is not renewed or extended by this date, all principal and interest will be due and payable on January 18, 2016. As of May 31, 2012, we had $40.8 million of borrowing capacity remaining under the Credit Facility.

We will have a continuing need for capital to finance our loans. The Credit Facility permits us to fund additional loans and investments as long as we are within the conditions set forth in the credit agreement. Pursuant to the terms of the Credit Facility, we are subject to certain limitations on the type of loan investments we make, including restrictions on geographic concentrations, sector concentrations, loan size, dividend payout, payment frequency and status, average life and lien property. The credit agreement also requires us to comply with other financial and operational covenants, which require us to, among other things, maintain certain financial ratios, including asset and interest coverage and a minimum net worth and a minimum number of obligors required in the borrowing base of the credit agreement. As of March 31, 2012, we were in compliance with these covenants; however, our continued compliance depends on many factors, some of which are beyond our control. Current market conditions have forced us to write down the value of a portion of our assets, as required by the 1940 Act and fair value accounting rules. These are not realized losses, but constitute adjustment in asset values for purposes of financial reporting and for collateral value for the Credit Facility. As assets are marked down in value, the amount we can borrow on the Credit Facility decreases. As of March 31, 2012, our net assets were $202.0 million, down from $213.7 million as of September 30, 2011, primarily a result of net losses on investments of $13.1 million ($8.2 million in net realized losses and $4.9 million of net unrealized depreciation) during the six months ended March 31, 2012. As of March 31, 2012, the cumulative net unrealized depreciation on our investments was $84.8 million, compared to cumulative net unrealized depreciation of $79.9 million as of September 30, 2011.

The minimum net worth covenant contained in the Credit Facility requires our net assets to be at least $190.0 million plus 50.0% of all equity and subordinated debt raised after January 19, 2012. Given the continued uncertainty in the capital markets, the cumulative unrealized depreciation in our portfolio may increase in future periods and threaten our ability to comply with the minimum net worth covenant and other covenants under the Credit Facility. Under the Credit Facility, we are also required to maintain our status as a BDC under the 1940 Act and as a RIC under the Code. There are no assurances that we will continue to comply with these covenants. Our failure to satisfy these covenants could result in foreclosure by our lenders, which would accelerate our repayment obligations under the facility and thereby have a material adverse effect on our business, liquidity, financial condition, results of operations and ability to pay distributions to our stockholders.

In recent years, creditors have significantly curtailed their lending to BDCs, including us. Any inability to renew, extend or replace our line of credit on terms favorable to us, or at all, could adversely impact our liquidity and ability to fund new investments or maintain distributions to our stockholders.

As described earlier, we extended our Credit Facility for a three year period in January 2012, so that it will terminate on January 18, 2015 and if the facility is not renewed or extended by such date, all principal and interest will be due and payable on January 18, 2016, one year after the date of maturity. During the fiscal year ended September 30, 2011, outstanding borrowings under the Credit Facility increased significantly from $16.8 million to $99.4 million. We were able to pay down a portion of the outstanding borrowings under the Credit Facility with the net proceeds from our offering of Series 2016 Term Preferred Stock in November 2011, leaving a balance of $56.9 million as of December 31, 2011. As of March 31, 2012, our balance on the Credit Facility was $65.8 million. If additional lenders are unwilling to join the facility on its terms, we will be unable to expand our Credit Facility and thus will have limited availability to finance new investments under our line of credit.

There can be no guarantee that we will be able to renew, extend or replace the Credit Facility on terms that are favorable to us, or at all. Our ability to obtain replacement financing will be constrained by current economic

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conditions affecting the credit markets. Consequently, any renewal, extension or refinancing of the Credit Facility will potentially result in significantly higher interest rates and related charges and may impose significant restrictions on the use of borrowed funds with regard to our ability to fund investments or maintain distributions to our stockholders. If we are unable to secure replacement financing, we may be forced to sell certain assets on disadvantageous terms, which may result in realized losses, and such realized losses could materially exceed the amount of any unrealized depreciation on these assets as of our most recent balance sheet date, which would have a material adverse effect on our results of operations. Such circumstances would also increase the likelihood that we would be required to redeem some or all of our outstanding Series 2016 Term Preferred Stock, which would potentially require us to sell even more assets. In addition to selling assets, or as an alternative, we may issue equity to repay amounts outstanding under the line of credit. Based on the recent trading prices of our common stock, such an equity offering may have a substantial dilutive impact on our existing common stockholders interest in our earnings and assets and voting interest in us.

Our business plan is dependent upon external financing, which is constrained by the limitations of the 1940 Act.

Our business requires a substantial amount of cash to operate and grow. We may acquire such additional capital from the following sources:

Senior Securities. We may issue debt securities, other evidences of indebtedness (including borrowings under our line of credit), senior securities representing indebtedness, and senior securities that are stock up to the maximum amount permitted by the 1940 Act. The 1940 Act currently permits us, as a BDC, to issue senior securities representing indebtedness and senior securities which are stock, which we refer to collectively as Senior Securities, in amounts such that our asset coverage, as defined in Section 18(h) of the 1940 Act, is at least 200% immediately after each issuance of Senior Securities. As a result of incurring indebtedness (in whatever form), we will be exposed to the risks associated with leverage. Although borrowing money for investments increases the potential for gain, it also increases the risk of a loss. A decrease in the value of our investments will have a greater impact on the value of our common stock to the extent that we have borrowed money to make investments. There is a possibility that the costs of borrowing could exceed the income we receive on the investments we make with such borrowed funds. In addition, our ability to pay distributions, issue Senior Securities or repurchase shares of our common stock would be restricted if the asset coverage on our Senior Securities is not at least 200%. If the value of our assets declines, we might be unable to satisfy that 200% requirement. To satisfy the 200% asset coverage requirement in the event that we are seeking to pay a distribution, we might either have to (i) liquidate a portion of our loan portfolio to repay a portion of our indebtedness or (ii) issue common stock. This may occur at a time when a sale of a portfolio asset may be disadvantageous, or when we have limited access to capital markets on agreeable terms. In addition, any amounts that we use to service our indebtedness or for offering expenses will not be available for distributions to our stockholders. Furthermore, if we have to issue common stock at below net asset value per share, any non-participating shareholders will be subject to dilution, as described below. Pursuant to Section 61(a)(2) of the 1940 Act, we are permitted, under specified conditions, to issue multiple classes of senior securities representing indebtedness. However, pursuant to Section 18(c) of the 1940 Act, we are permitted to issue only one class of senior securities that is stock. As a result, we would be prohibited from issuing senior common stock to the extent that such a security was deemed to be a separate class of stock from our recently issued Series 2016 Term Preferred Stock.

Common and Convertible Preferred Stock. Because we are constrained in our ability to issue debt for the reasons given above, we are dependent on the issuance of equity as a financing source. If we raise additional funds by issuing more common stock or senior securities convertible into or exchangeable for our common stock, the percentage ownership of our common stockholders at the time of the issuance would decrease and our common stock may experience dilution. In addition, any convertible or exchangeable securities that we issue in the future may have rights, preferences and privileges more favorable than those of our common stock. In addition, under the 1940 Act, we will generally not be able to issue additional shares of our common stock at a price below net asset value per share to purchasers, other than to our existing common

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stockholders through a rights offering, without first obtaining the approval of our common stockholders and our independent directors. If we were to sell shares of our common stock below our then current net asset value per share, such sales would result in an immediate dilution to the net asset value per share. This dilution would occur as a result of the sale of shares at a price below the then current net asset value per share of our common stock and a proportionately greater decrease in a common stockholder s interest in our earnings and assets and voting interest in us than the increase in our assets resulting from such issuance. For example, if we issue and sell an additional 10% of our common stock at a 5% discount from net asset value, a common stockholder who does not participate in that offering for its proportionate interest will suffer net asset value dilution of up to 0.5% or $5 per $1,000 of net asset value. This imposes constraints on our ability to raise capital when our common stock is trading at below net asset value, as it has for the last year. As noted previously, the 1940 Act prohibits the issuance of multiple classes of senior securities that are stock. As a result, we would be prohibited from issuing convertible preferred stock to the extent that such a security was deemed to be a separate class of stock from our recently issued Series 2016 Term Preferred Stock.

We finance our investments with borrowed money and capital from the issuance of Senior Securities, which will magnify the potential for gain or loss on amounts invested and may increase the risk of investing in us.

The following table illustrates the effect of leverage on returns from an investment in our common stock assuming various annual returns on our portfolio, net of expenses. The calculations in the table below are hypothetical, and actual returns may be higher or lower than those appearing in the table below.

	Assumed Return on Our Portfolio (Net of Expenses)				
	(10)%	(5)%	0%	5%	10%
Corresponding return to common stockholder(1)	(17.39)%	(9.68)%	(1.98)%	5.73%	13.43%

(1) The hypothetical return to common stockholders is calculated by multiplying our total assets as of March 31, 2012 by the assumed rates of return and subtracting all interest accrued on our debt and dividends on our preferred stock for the quarter ended March 31, 2012; and then dividing the resulting difference by our total assets attributable to common stock. Based on $311.3 million in total assets, $65.8 million in debt, $38.5 million in aggregate liquidation preference of preferred stock, and $202.0 million in net assets, each as of March 31, 2012.

Based on an outstanding indebtedness of $65.8 million as of March 31, 2012 and the effective annual interest rate of 6.1% as of that date, and aggregate liquidation prefrence of our 2016 Series Term Preferred Stock of $38.5 million, our investment portfolio at fair value would have been required to experience an annual return of at least 2.2% to cover annual interest payments on the outstanding debt and dividends on the Series 2016 Term Preferred Stock.

A change in interest rates may adversely affect our profitability.

We anticipate using a combination of equity and long-term and short-term borrowings to finance our investment activities. As a result, a portion of our income will depend upon the difference between the rate at which we borrow funds and the rate at which we loan these funds. Higher interest rates on our borrowings will decrease the overall return on our portfolio.

Ultimately, we expect approximately 90% of the loans in our portfolio to be at variable rates determined on the basis of the LIBOR and approximately 10% to be at fixed rates. As of March 31, 2012, our portfolio had approximately 87.6% of the total loan cost value at variable rates with floors, approximately 6.0% of the total of the loan cost value at variable rates without a floor or ceiling and approximately 6.4% of the total loan portfolio cost basis at fixed rates.

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Risks Related to Our Investments

We operate in a highly competitive market for investment opportunities.

A large number of entities compete with us and make the types of investments that we seek to make in small and mid-sized companies. We compete with public and private buyout funds, commercial and investment banks, commercial financing companies, and, to the extent they provide an alternative form of financing, hedge funds. Many of our competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which would allow them to consider a wider variety of investments and establish more relationships than us. Furthermore, many of our competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a BDC. The competitive pressures we face could have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this competition, we may not be able to take advantage of attractive investment opportunities from time to time and we can offer no assurance that we will be able to identify and make investments that are consistent with our investment objective. We do not seek to compete based on the interest rates we offer, and we believe that some of our competitors may make loans with interest rates that will be comparable to or lower than the rates we offer. We may lose investment opportunities if we do not match our competitors pricing, terms, and structure. However, if we match our competitors pricing, terms, and structure, we may experience decreased net interest income and increased risk of credit loss.

Our investments in small and medium-sized portfolio companies are extremely risky and could cause you to lose all or a part of your investment.

Investments in small and medium-sized portfolio companies are subject to a number of significant risks including the following:

Small and medium-sized businesses are likely to have greater exposure to economic downturns than larger businesses. Our portfolio companies may have fewer resources than larger businesses, and thus the recent recession, and any further economic downturns or recessions, are more likely to have a material adverse effect on them. If one of our portfolio companies is adversely impacted by a recession, its ability to repay our loan or engage in a liquidity event, such as a sale, recapitalization or initial public offering would be diminished.

Small and medium-sized businesses may have limited financial resources and may not be able to repay the loans we make to them. Our strategy includes providing financing to portfolio companies that typically is not readily available to them. While we believe that this provides an attractive opportunity for us to generate profits, this may make it difficult for the portfolio companies to repay their loans to us upon maturity. A borrower s ability to repay its loan may be adversely affected by numerous factors, including the failure to meet its business plan, a downturn in its industry, or negative economic conditions. Deterioration in a borrower s financial condition and prospects usually will be accompanied by a deterioration in the value of any collateral and a reduction in the likelihood of us realizing on any guaranties we may have obtained from the borrower s management. At March 31, 2012, eight portfolio companies were either fully or partially on non-accrual with an aggregate cost basis of approximately $43.8 million, or 12.1% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of approximately $4.6 million, or 1.7% of the fair value of all debt investments in our portfolio. While we are working with the portfolio companies to improve their profitability and cash flows, there can be no assurance that our efforts will prove successful. Although we will sometimes seek to be the senior, secured lender to a borrower, in most of our loans we expect to be subordinated to a senior lender, and our interest in any collateral would, accordingly, likely be subordinate to another lender s security interest.

Small and medium-sized businesses typically have narrower product lines and smaller market shares than large businesses. Because our target portfolio companies are smaller businesses, they will tend to be more vulnerable to competitors actions and market conditions, as well as general economic downturns. In addition, our portfolio companies may face intense competition, including competition from companies with greater financial resources, more extensive development, manufacturing, marketing, and other capabilities and a larger number of qualified managerial, and technical personnel.

There is generally little or no publicly available information about these businesses. Because we seek to invest in privately owned businesses, there is generally little or no publicly available operating and financial information about our potential portfolio companies. As a result, we rely on our officers, our Adviser, and its employees and consultants to perform due diligence investigations of these portfolio companies, their operations, and their prospects. We may not learn all of the material information we need to know regarding these businesses through our investigations.

Small and medium-sized businesses generally have less predictable operating results. We expect that our portfolio companies may have significant variations in their operating results, may from time to time be parties to litigation, may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence, may require substantial additional capital to support their operations, to finance expansion or to maintain their competitive position, may otherwise have a weak financial position, or may be adversely affected by changes in the business cycle. Our portfolio companies may not meet net income, cash flow, and other coverage tests typically imposed by their senior lenders. A borrower s failure to satisfy financial or operating covenants imposed by senior lenders could lead to defaults and, potentially, foreclosure on its senior credit facility, which could additionally trigger cross-defaults in other agreements. If this were to occur, it is possible that the borrower s ability to repay our loan would be jeopardized.

Small and medium-sized businesses are more likely to be dependent on one or two persons. Typically, the success of a small or medium-sized business also depends on the management talents and efforts of one or two persons or a small group of persons. The death, disability, or resignation of one or more of these persons could have a material adverse impact on our borrower and, in turn, on us.

Small and medium-sized businesses may have limited operating histories. While we intend to target stable companies with proven track records, we may make loans to new companies that meet our other investment criteria. Portfolio companies with limited operating histories will be exposed to all of the operating risks that new businesses face and may be particularly susceptible to, among other risks, market downturns, competitive pressures and the departure of key executive officers.

Because the loans we make and equity securities we receive when we make loans are not publicly-traded, there is uncertainty regarding the value of our privately held securities that could adversely affect our determination of our net asset value.

Our portfolio investments are, and we expect will continue to be, in the form of securities that are not publicly-traded. The fair value of securities and other investments that are not publicly-traded may not be readily determinable. Our Board of Directors has established an investment valuation policy and consistently applied valuation procedures used to determine the fair value of these securities quarterly. These procedures for the determination of value of many of our debt securities rely on the opinions of value submitted to us by Standard & Poor s Securities Evaluations, Inc. (SPSE) or the use of internally developed discounted cash flow (DCF) methodologies or indicative bid prices (IBP) offered by the respective originating syndication agent s trading desk, or secondary desk, specifically for our syndicated loans, or internal methodologies based on the total enterprise value (TEV) of the issuer used for certain of our equity investments. SPSE will only evaluate the debt portion of our investments for which we specifically request evaluation, and SPSE may decline to make requested evaluations for any reason in its sole discretion. However, to date, SPSE has accepted each of our requests for evaluation.

Our use of these fair value methods is inherently subjective and is based on estimates and assumptions of each security. In the event that we are required to sell a security, we may ultimately sell for an amount materially less than the estimated fair value calculated by SPSE, or utilizing the TEV, IBP or the DCF methodology.

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Our procedures also include provisions whereby our Adviser will establish the fair value of any equity securities we may hold where SPSE or third-party agent banks are unable to provide evaluations. The types of factors that may be considered in determining the fair value of our debt and equity securities include some or all of the following:

- the nature and realizable value of any collateral;
- the portfolio company s earnings and cash flows and its ability to make payments on its obligations;
- the markets in which the portfolio company does business;
- the comparison to publicly-traded companies; and
- discounted cash flow and other relevant factors.

Because such valuations, particularly valuations of private securities and private companies, are not susceptible to precise determination, may fluctuate over short periods of time, and may be based on estimates, our determinations of fair value may differ from the values that might have actually resulted had a readily available market for these securities been available.

A portion of our assets are, and will continue to be, comprised of equity securities that are valued based on internal assessment using our own valuation methods approved by our Board of Directors, without the input of SPSE or any other third-party evaluator. We believe that our equity valuation methods reflect those regularly used as standards by other professionals in our industry who value equity securities. However, determination of fair value for securities that are not publicly-traded, whether or not we use the recommendations of an independent third-party evaluator, necessarily involves the exercise of subjective judgment. Our net asset value could be adversely affected if our determinations regarding the fair value of our investments were materially higher than the values that we ultimately realize upon the disposal of such securities.

The lack of liquidity of our privately held investments may adversely affect our business.

We will generally make investments in private companies whose securities are not traded in any public market. Substantially all of the investments we presently hold and the investments we expect to acquire in the future are, and will be, subject to legal and other restrictions on resale and will otherwise be less liquid than publicly-traded securities. The illiquidity of our investments may make it difficult for us to quickly obtain cash equal to the value at which we record our investments if the need arises. This could cause us to miss important investment opportunities. In addition, if we are required to liquidate all or a portion of our portfolio quickly, we may record substantial realized losses upon liquidation. We may also face other restrictions on our ability to liquidate an investment in a portfolio company to the extent that we, our Adviser, or our respective officers, employees or affiliates have material non-public information regarding such portfolio company.

Due to the uncertainty inherent in valuing these securities, our determinations of fair value may differ materially from the values that could be obtained if a ready market for these securities existed. Our net asset value could be materially affected if our determinations regarding the fair value of our investments are materially different from the values that we ultimately realize upon our disposal of such securities.

Our financial results could be negatively affected if a significant portfolio investment fails to perform as expected.

Our total investment in companies may be significant individually or in the aggregate. As a result, if a significant investment in one or more companies fails to perform as expected, our financial results could be more negatively affected and the magnitude of the loss could be more significant than if we had made smaller investments in more companies.

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When we are a debt or minority equity investor in a portfolio company, which we expect will generally be the case, we may not be in a position to control the entity, and its management may make decisions that could decrease the value of our investment.

We anticipate that most of our investments will continue to be either debt or minority equity investments in our portfolio companies. Therefore, we are and will remain subject to risk that a portfolio company may make business decisions with which we disagree, and the shareholders and management of such company may take risks or otherwise act in ways that do not serve our best interests. As a result, a portfolio company may make decisions that could decrease the value of our portfolio holdings.

In addition, we will generally not be in a position to control any portfolio company by investing in its debt securities. This is particularly true when we invest in syndicated loans, which are loans made by a larger group of investors whose investment objectives of the other lenders may not be completely aligned with ours. During the year ended September 30, 2011, we significantly increased the number of our syndicated loan investments, and therefore we have become increasingly subject to the risk that other lenders in these investments may make decisions that could decrease the value of our portfolio holdings.

Our portfolio companies may incur debt that ranks equally with, or senior to, our investments in such companies.

We invest primarily in debt securities issued by our portfolio companies. In some cases portfolio companies will be permitted to have other debt that ranks equally with, or senior to, the debt securities in which we invest. By their terms, such debt instruments may provide that the holders thereof are entitled to receive payment of interest and principal on or before the dates on which we are entitled to receive payments in respect of the debt securities in which we invest. Also, in the event of insolvency, liquidation, dissolution, reorganization, or bankruptcy of a portfolio company, holders of debt instruments ranking senior to our investment in that portfolio company would typically be entitled to receive payment in full before we receive any distribution in respect of our investment. After repaying such senior creditors, such portfolio company may not have any remaining assets to use for repaying its obligation to us. In the case of debt ranking equally with debt securities in which we invest, we would have to share on an equal basis any distributions with other creditors holding such debt in the event of an insolvency, liquidation, dissolution, reorganization, or bankruptcy of a portfolio company.

Prepayments of our investments by our portfolio companies could adversely impact our results of operations and reduce our return on equity.

In addition to risks associated with delays in investing our capital, we are also subject to the risk that investments that we make in our portfolio companies may be repaid prior to maturity. For the year ended September 30, 2011, we received principal payments prior to maturity of $17.5 million. For the six months ended March 31, 2012, we received principal payments prior to maturity of $14.9 million. We will first use any proceeds from prepayments to repay any borrowings outstanding on the Credit Facility. In the event that funds remain after repayment of our outstanding borrowings, then we will generally reinvest these proceeds in government securities, pending their future investment in new debt and/or equity securities. These government securities will typically have substantially lower yields than the debt securities being prepaid and we could experience significant delays in reinvesting these amounts. As a result, our results of operations could be materially adversely affected if one or more of our portfolio companies elect to prepay amounts owed to us. Additionally, prepayments could negatively impact our return on equity, which could result in a decline in the market price of our common stock.

Higher taxation of our portfolio companies may impact our quarterly and annual operating results.

The recession s adverse effect on federal, state, and municipality revenues may induce these government entities to raise various taxes to make up for lost revenues. Additional taxation may have an adverse affect on our portfolio companies earnings and reduce their ability to repay our loans to them, thus affecting our quarterly and annual operating results.

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Our portfolio is concentrated in a limited number of companies and industries, which subjects us to an increased risk of significant loss if any one of these companies does not repay us or if the industries experience downturns.

As of March 31, 2012 we had investments in 55 portfolio companies, of which there were five investments that comprised approximately $94.8 million or 32.9% of our total investment portfolio, at fair value. A consequence of a concentration in a limited number of investments is that the aggregate returns we realize may be substantially adversely affected by the unfavorable performance of a small number of such investments or a substantial write-down of any one investment. Beyond our regulatory and income tax diversification requirements, we do not have fixed guidelines for industry concentration and our investments could potentially be concentrated in relatively few industries. In addition, while we do not intend to invest 25.0% or more of our total assets in a particular industry or group of industries at the time of investment, it is possible that as the values of our portfolio companies change, one industry or a group of industries may comprise in excess of 25.0% of the value of our total assets. As a result, a downturn in an industry in which we have invested a significant portion of our total assets could have a materially adverse effect on us. As of March 31, 2012, 18.6% of our total assets at fair value were invested in electronics companies, 11.1% were invested in mining, steel, iron and non-precious metal companies, and 10.4% were invested in healthcare, education and childcare companies. As a result, we are susceptible to the economic circumstances in these industries, and a downturn in one or more of these industries could have a material adverse effect on our results of operations and financial condition.

Our investments are typically long term and will require several years to realize liquidation events.

Since we generally make five to seven year term loans and hold our loans and related warrants or other equity positions until the loans mature, you should not expect realization events, if any, to occur over the near term. In addition, we expect that any warrants or other equity positions that we receive when we make loans may require several years to appreciate in value and we cannot give any assurance that such appreciation will occur.

The disposition of our investments may result in contingent liabilities.

Currently, all of our investments involve private securities. In connection with the disposition of an investment in private securities, we may be required to make representations about the business and financial affairs of the underlying portfolio company typical of those made in connection with the sale of a business. We may also be required to indemnify the purchasers of such investment to the extent that any such representations turn out to be inaccurate or with respect to certain potential liabilities. These arrangements may result in contingent liabilities that ultimately yield funding obligations that must be satisfied through our return of certain distributions previously made to us.

There may be circumstances where our debt investments could be subordinated to claims of other creditors or we could be subject to lender liability claims.

Even though we have structured some of our investments as senior loans, if one of our portfolio companies were to go bankrupt, depending on the facts and circumstances, including the extent to which we actually provided managerial assistance to that portfolio company, a bankruptcy court might re-characterize our debt investments and subordinate all, or a portion, of our claims to that of other creditors. Holders of debt instruments ranking senior to our investments typically would be entitled to receive payment in full before we receive any distributions. After repaying such senior creditors, such portfolio company may not have any remaining assets to use to repay its obligation to us. We may also be subject to lender liability claims for actions taken by us with respect to a borrower s business or in instances in which we exercised control over the borrower. It is possible that we could become subject to a lender s liability claim, including as a result of actions taken in rendering significant managerial assistance.

Portfolio company litigation could result in additional costs and the diversion of management time and resources.

In the course of providing significant managerial assistance to certain of our portfolio companies, our executive officers sometimes serve as directors on the boards of such companies. To the extent that litigation arises out of our investments in these companies, such executive officers may be named as defendants in such litigation, which could result in additional costs and the diversion of management time and resources.

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We may not realize gains from our equity investments and other yield enhancements.

When we make a subordinated loan, we may receive warrants to purchase stock issued by the borrower or other yield enhancements, such as success fees. Our goal is to ultimately dispose of these equity interests and realize gains upon our disposition of such interests. We expect that, over time, the gains we realize on these warrants and other yield enhancements will offset any losses we experience on loan defaults. However, any

warrants we receive may not appreciate in value and, in fact, may decline in value and any other yield enhancements, such as success fees, may not be realized. Accordingly, we may not be able to realize gains from our equity interests or other yield enhancements and any gains we do recognize may not be sufficient to offset losses we experience on our loan portfolio.

Any unrealized depreciation we experience on our investment portfolio may be an indication of future realized losses, which could reduce our income available for distribution.

As a BDC, we are required to carry our investments at market value or, if no market value is ascertainable, at fair value as determined in good faith by or under the direction of our Board of Directors. Decreases in the market values or fair values of our investments will be recorded as unrealized depreciation. Since our inception, we have, at times, incurred a cumulative net unrealized depreciation of our portfolio. Any unrealized depreciation in our investment portfolio could result in realized losses in the future and ultimately in reductions of our income available for distribution to stockholders in future periods.

Risks Related to Our Regulation and Structure

We will be subject to corporate-level tax if we are unable to satisfy Code requirements for RIC qualification.

To maintain our qualification as a RIC, we must meet income source, asset diversification, and annual distribution requirements. The annual distribution requirement is satisfied if we distribute at least 90% of our ordinary income and short-term capital gains to our stockholders on an annual basis. Because we use leverage, we are subject to certain asset coverage ratio requirements under the 1940 Act and could, under certain circumstances, be restricted from making distributions necessary to qualify as a RIC. Warrants we receive with respect to debt investments will create original issue discount, which we must recognize as ordinary income, increasing the amounts we are required to distribute to maintain RIC status. Because such warrants will not produce distributable cash for us at the same time as we are required to make distributions in respect of the related original issue discount, we will need to use cash from other sources to satisfy such distribution requirements. The asset diversification requirements must be met at the end of each calendar quarter. If we fail to meet these tests, we may need to quickly dispose of certain investments to prevent the loss of RIC status. Since most of our investments will be illiquid, such dispositions, if even possible, may not be made at prices advantageous to us and, in fact, may result in substantial losses. If we fail to qualify as a RIC for any reason and become fully subject to corporate income tax, the resulting corporate taxes could substantially reduce our net assets, the amount of income available for distribution, and the actual amount distributed. Such a failure would have a material adverse effect on us and our shares. For additional information regarding asset coverage ratio and RIC requirements, see Material U.S. Federal Income Tax Considerations Regulated Investment Company Status.

From time to time, some of our debt investments may include success fees that would generate payments to us if the business is ultimately sold. Because the satisfaction of these success fees, and the ultimate payment of these fees, is uncertain, we do not recognize them as income until we have received payment. We sought and received approval for a change in accounting method from the IRS related to our tax treatment for success fees. As a result, we, in effect, will continue to account for the recognition of income from the success fees upon receipt, or when the amount becomes fixed. Prior to January 1, 2011, we treated the success fee amount as a capital gain for tax characterization purposes. However, starting January 1, 2011, the tax characterization of the success fee amount was and will be treated as ordinary income. The approved change in accounting method does

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not require us to retroactively change the capital gains treatment of the success fees received prior to January 1, 2011. As a result, we will be required to distribute such amounts to our stockholders in order to maintain RIC status for success fees we receive after January 1, 2011.

Changes in laws or regulations governing our operations, or changes in the interpretation thereof, and any failure by us to comply with laws or regulations governing our operations may adversely affect our business.

We and our portfolio companies are subject to regulation by laws at the local, state and federal levels. These laws and regulations, as well as their interpretation, may be changed from time to time. Accordingly, any change in these laws or regulations, or their interpretation, or any failure by us or our portfolio companies to comply with these laws or regulations may adversely affect our business. For additional information regarding the regulations to which we are subject, see Material U.S. Federal Income Tax Considerations Regulated Investment Company Status and Regulation as a Business Development Company.

We are subject to restrictions that may discourage a change of control. Certain provisions contained in our articles of incorporation and Maryland law may prohibit or restrict a change of control and adversely impact the price of our shares.

Our Board of Directors is divided into three classes, with the term of the directors in each class expiring every third year. At each annual meeting of stockholders, the successors to the class of directors whose term expires at such meeting will be elected to hold office for a term expiring at the annual meeting of stockholders held in the third year following the year of their election. After election, a director may only be removed by our stockholders for cause. Election of directors for staggered terms with limited rights to remove directors makes it more difficult for a hostile bidder to acquire control of us. The existence of this provision may negatively impact the price of our securities and may discourage third-party bids to acquire our securities. This provision may reduce any premiums paid to stockholders in a change in control transaction.

Certain provisions of Maryland law applicable to us prohibit business combinations with:

- any person who beneficially owns 10% or more of the voting power of our common stock (an interested stockholder);
- an affiliate of ours who at any time within the two-year period prior to the date in question was an interested stockholder; or
- an affiliate of an interested stockholder.

These prohibitions last for five years after the most recent date on which the interested stockholder became an interested stockholder. Thereafter, any business combination with the interested stockholder must be recommended by our Board of Directors and approved by the affirmative vote of at least 80% of the votes entitled to be cast by holders of our outstanding shares of common stock and two-thirds of the votes entitled to be cast by holders of our common stock other than shares held by the interested stockholder. These requirements could have the effect of inhibiting a change in control even if a change in control were in our stockholders interest. These provisions of Maryland law do not apply, however, to business combinations that are approved or exempted by our Board of Directors prior to the time that someone becomes an interested stockholder.

Our articles of incorporation permit our Board of Directors to issue up to 50.0 million shares of capital stock. In addition, our Board of Directors, without any action by our stockholders, may amend our articles of incorporation from time to time to increase or decrease the aggregate number of shares or the number of shares of any class or series of stock that we have authority to issue. Our Board of Directors may classify or reclassify any unissued common stock or preferred stock and establish the preferences, conversion or other rights, voting powers, restrictions, limitations as to distributions, qualifications and terms or conditions of redemption of any such stock. Thus, our Board of Directors could authorize the issuance of preferred stock with terms and conditions that could have a priority as to distributions and amounts payable upon liquidation over the rights of the holders of

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our common stock, which it did in connection with our issuance in November 2011 of approximately 1.5 million shares of Series 2016 Term Preferred Stock. Preferred stock, including the Series 2016 Term Preferred Stock, could also have the effect of delaying, deferring or preventing a change in control of us, including an extraordinary transaction (such as a merger, tender offer or sale of all or substantially all of our assets) that might provide a premium price for holders of our common stock.

Risks Related to an Investment in Our Common Stock and Our Preferred Stock

We may experience fluctuations in our quarterly and annual operating results.

We may experience fluctuations in our quarterly and annual operating results due to a number of factors, including, among others, variations in our investment income, the interest rates payable on the debt securities we acquire, the default rates on such securities, the level of our expenses, variations in and the timing of the recognition of realized and unrealized gains or losses, the level of our expenses, the degree to which we encounter competition in our markets, and general economic conditions, including the impacts of inflation. The majority of our portfolio companies are in industries that are directly impacted by inflation, such as manufacturing and consumer goods and services. Our portfolio companies may not be able to pass on to customers increases in their costs of production which could greatly affect their operating results, impacting their ability to repay our loans. In addition, any projected future decreases in our portfolio companies operating results due to inflation could adversely impact the fair value of those investments. Any decreases in the fair value of our investments could result in future realized and unrealized losses and therefore reduce our net assets resulting from operations. As a result of these factors, results for any period should not be relied upon as being indicative of performance in future periods.

There is a risk that you may not receive distributions.

Our current intention is to distribute at least 90% of our ordinary income and short-term capital gains to our stockholders on a quarterly basis by paying monthly distributions. On an annual basis, we intend to distribute net long-term capital gains, after giving effect to any prior year realized losses that are carried forward, by paying a one-time distribution. However, our Board of Directors may determine in certain cases to retain net realized long-term capital gains through a deemed distribution to supplement our equity capital and support the growth of our portfolio. We cannot assure you that we will achieve investment results or maintain a tax status that will allow or require any specified level of cash distributions.

Distributions by us have included and may in the future include a return of capital.

Our Board of Directors declares monthly distributions based on estimates of net investment income for each fiscal year, which may differ, and in the past have differed, from actual results. Because our distributions are based on estimates of net investment income that may differ from actual results, future distributions payable to our stockholders may also include a return of capital. Moreover, to the extent that we distribute amounts that exceed our accumulated earnings and profits, these distributions constitute a return of capital. A return of capital represents a return of a stockholder s original investment in shares of our stock and should not be confused with a distribution from earnings and profits. Although return of capital distributions may not be taxable, such distributions may increase an investor s tax liability for capital gains upon the sale of our shares by reducing the investor s tax basis for such shares. Such returns of capital reduce our asset base and also adversely impact our ability to raise debt capital as a result of the leverage restrictions under the 1940 Act, which could have a material adverse impact on our ability to make new investments.

The market price of our shares may fluctuate significantly.

The trading price of our common stock and our preferred stock may fluctuate substantially. The extreme volatility and disruption that have affected the capital and credit markets for over a year have reached unprecedented levels in recent months. We have experienced greater than usual stock price volatility.

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The market price and marketability of our shares may from time to time be significantly affected by numerous factors, including many over which we have no control and that may not be directly related to us. These factors include, but are not limited to, the following:

- general economic trends and other external factors;
- price and volume fluctuations in the stock market from time to time, which are often unrelated to the operating performance of particular companies;
- significant volatility in the market price and trading volume of shares of RICs, BDCs or other companies in our sector, which is not necessarily related to the operating performance of these companies;
- changes in regulatory policies or tax guidelines, particularly with respect to RICs or BDCs;
- loss of BDC or RIC status;
- changes in our earnings or variations in our operating results;
- changes in prevailing interest rates;
- changes in the value of our portfolio of investments;
- any shortfall in our revenue or net income or any increase in losses from levels expected by securities analysts;
- departure of key personnel;
- operating performance of companies comparable to us;
- short-selling pressure with respect to our shares or BDCs generally;
- the announcement of proposed, or completed, offerings of our securities, including a rights offering; and
- loss of a major funding source.

Fluctuations in the trading prices of our shares may adversely affect the liquidity of the trading market for our shares and, if we seek to raise capital through future equity financings, our ability to raise such equity capital.

The issuance of subscription rights to our existing stockholders may dilute the ownership and voting powers by existing stockholders in our common stock, dilute the net asset value of their shares and have a material adverse effect on the trading price of our common stock.

There are significant capital raising constraints applicable to us under the 1940 Act when our stock is trading below its net asset value per share. In the event that we issue subscription rights to our existing common stockholders, there is a significant possibility that the rights offering will dilute the ownership interest and voting power of stockholders who do not fully exercise their subscription rights. Stockholders who do not fully exercise their subscription rights should expect that they will, upon completion of the rights offering, own a smaller proportional interest in Gladstone Capital than would otherwise be the case if they fully exercised their subscription rights. In addition, because the subscription price of the rights offering is likely to be less than our most recently determined net asset value per share, our common stockholders are likely to experience an immediate dilution of the per share net asset value of their shares as a result of the offer. As a result of these factors, any future rights offerings of our common stock, or our announcement of our intention to conduct a rights offering, could have a material adverse impact on the trading price of our common stock.

Shares of closed-end investment companies frequently trade at a discount from net asset value.

Shares of closed-end investment companies frequently trade at a discount from net asset value. Since our inception, our common stock has at times traded above net asset value, and at times traded below net asset value. During the past three years, our common stock has often traded, and at times significantly, below net asset value. Subsequent to September 30, 2011, our common stock has traded at discounts of up to 34.5% of our net asset

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value as of September 30, 2011. As of May 31, 2012, our common stock was trading at a discount of 23.1% of our net asset value as of March 31, 2012. This characteristic of shares of closed-end investment companies is separate and distinct from the risk that our net asset value per share will decline. As with any stock, the price of our shares will fluctuate with market conditions and other factors. If shares are sold, the price received may be more or less than the original investment. Whether investors will realize gains or losses upon the sale of our shares will not depend directly upon our net asset value, but will depend upon the market price of the shares at the time of sale. Since the market price of our shares will be affected by such factors as the relative demand for and supply of the shares in the market, general market and economic conditions and other factors beyond our control, we cannot predict whether the shares will trade at, below or above our net asset value. Under the 1940 Act, we are generally not able to issue additional shares of our common stock at a price below net asset value per share to purchasers other than our existing common stockholders through a rights offering without first obtaining the approval of our voting stockholders and our independent directors. Additionally, at times when our stock is trading below its net asset value per share, our dividend yield may exceed the weighted average returns that we would expect to realize on new investments that would be made with the proceeds from the sale of such stock, making it unlikely that we would determine to issue additional shares in such circumstances. Thus, for as long as our common stock trades below net asset value we will be subject to significant constraints on our ability to raise capital through the issuance of common stock. Additionally, an extended period of time in which we are unable to raise capital may restrict our ability to grow and adversely impact our ability to increase or maintain our distributions.

Common stockholders may incur dilution if we sell shares of our common stock in one or more offerings at prices below the then current net asset value per share of our common stock.

At our most recent annual meeting on February 16, 2012, our stockholders approved a proposal designed to allow us to sell shares of our common stock below the then current net asset value per share of our common stock in one or more offerings for a period of one year, subject to certain conditions (including, but not limited to, that the cumulative number of shares issued and sold pursuant to such authority does not exceed 25% of our then outstanding common stock immediately prior to each such sale). During the past three years, our common stock has often traded, and at times significantly, below net asset value. Any decision to sell shares of our common stock below the then current net asset value per share of our common stock would be subject to the determination by our Board of Directors that such issuance is in our and our stockholders best interests.

If we were to sell shares of our common stock below net asset value per share, such sales would result in an immediate dilution to the net asset value per share. This dilution would occur as a result of the sale of shares at a price below the then current net asset value per share of our common stock and a proportionately greater decrease in a stockholder s interest in our earnings and assets and voting interest in us than the increase in our assets resulting from such issuance. The greater the difference between the sale price and the net asset value per share at the time of the offering, the more significant the dilutive impact would be. Because the number of shares of common stock that could be so issued and the timing of any issuance is not currently known, the actual dilutive effect, if any, cannot be currently predicted. However, if for example, we sold an additional 10% of our common stock at a 5% discount from net asset value, a common stockholder who did not participate in that offering for its proportionate interest would suffer net asset value dilution of up to 0.5% or $5 per $1,000 of net asset value.

If we fail to pay dividends on our Series 2016 Term Preferred Stock dividends for two years, the holders thereof will be entitled to elect a majority of our directors.

The terms of our Series 2016 Term Preferred Stock provide for annual dividends in the amount of $1.7813 per outstanding share. In accordance with the terms of our Series 2016 Term Preferred Stock, if we fail to pay dividends on the Series 2016 Term Preferred Stock for a period of two years, the holders of Series 2016 Term Preferred Stock will be entitled to elect a majority of our Board of Directors.

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Our Series 2016 Term Preferred Stock magnifies the potential for gain or loss for our holders of common stock and the risks of investing in our common stock in the same way as our borrowings.

Preferred stock, which is another form of leverage, has the same risks to our common stockholders as borrowings because the dividends on any preferred stock we issue must be cumulative. Payment of such dividends and repayment of the liquidation preference of such preferred stock must take preference over any dividends or other payments to our common stockholders, and preferred stockholders are less subject to our expenses or losses and are not entitled to participate in any income or appreciation in excess of their stated preference.

An investment in Series 2016 Term Preferred Stock with a fixed interest rate bears interest rate risk.

Our Series 2016 Term Preferred Stock, in general, pays dividends at a fixed dividend rate of 7.125% per year. Prices of fixed income investments generally vary inversely with changes in market yields. The market yields on securities comparable to the Series 2016 Term Preferred Stock may increase, which would likely result in a decline in the secondary market price of the Series 2016 Term Preferred Stock prior to the term redemption date. This risk may be even more significant in light of the low nature of the currently prevailing market interest rates.

A liquid secondary trading market for our Series 2016 Term Preferred Stock may not develop.

Because we have no prior trading history for exchange-listed preferred stock, we cannot predict the trading patterns of the Series 2016 Term Preferred Stock, including the effective costs of trading the stock. Although our Series 2016 Term Preferred Stock is listed for trading on the NASDAQ, there is a risk that such shares may be thinly traded, and the market for such shares may be relatively illiquid compared to the market for other types of securities, with the spread between the bid and asked prices considerably greater than the spreads of other securities with comparable terms and features.

The Series 2016 Term Preferred Stock is not rated.

We have not had the Series 2016 Term Preferred Stock rated by any rating agency. Unrated securities usually trade at a discount to similar, rated securities. As a result, there is a risk that the shares of our Series 2016 Term Preferred Stock may trade at a price that is lower than they might otherwise trade if they were rated by a rating agency.

The Series 2016 Term Preferred Stock bears a risk of early redemption by us.

We may voluntarily redeem some or all of the Series 2016 Term Preferred Stock on or after December 31, 2012. We also may be forced to redeem some or all of the Series 2016 Term Preferred Stock to meet regulatory requirements and the asset coverage requirements of such shares and any such redemption may occur at a time that is unfavorable to holders of the Series 2016 Term Preferred Stock. We may have an incentive to redeem the Series 2016 Term Preferred Stock voluntarily before the mandatory redemption date if market conditions allow us to issue other preferred stock or debt securities at a rate that is lower than the fixed dividend rate on the Series 2016 Term Preferred Stock.

Claims of holders of our Series 2016 Term Preferred Stock are subject to a risk of subordination relative to holders of our debt instruments.

Rights of holders of our Series 2016 Term Preferred Stock are subordinated to the rights of holders of our indebtedness. Therefore, dividends, distributions and other payments to holders of Series 2016 Term Preferred Stock in liquidation or otherwise may be subject to prior payments due to the holders of our indebtedness. In addition, under some circumstances the 1940 Act may provide debt holders with voting rights that are superior to the voting rights of holders of the Series 2016 Term Preferred Stock.

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Holders of our Series 2016 Term Preferred Stock are subject to inflation risk.

Inflation is the reduction in the purchasing power of money resulting from the increase in the price of goods and services. Inflation risk is the risk that the inflation-adjusted, or real, value of an investment in Series 2016 Term Preferred Stock or the income from that investment will be worth less in the future. As inflation occurs, the real value of the Series 2016 Term Preferred Stock and dividends payable on such shares declines.

Holders of our Series 2016 Term Preferred Stock bear reinvestment risk.

Given the five-year term and potential for early redemption of the Series 2016 Term Preferred Stock, holders of such shares may face an increased reinvestment risk, which is the risk that the return on an investment purchased with proceeds from the sale or redemption of the Series 2016 Term Preferred Stock may be lower than the return previously obtained from the investment in such shares.

Holders of our Series 2016 Term Preferred Stock bear dividend risk.

We may be unable to pay dividends on the Series 2016 Term Preferred Stock under some circumstances. The terms of our indebtedness preclude the payment of dividends in respect of equity securities, including the Series 2016 Term Preferred Stock, under certain conditions.

There is a risk of delay in our redemption of our Series 2016 Term Preferred Stock, and we may fail to redeem such securities as required by their terms.

We will generally make investments in private companies whose securities are not traded in any public market. Substantially all of the investments we presently hold and the investments we expect to acquire in the future are, and will be, subject to legal and other restrictions on resale and will otherwise be less liquid than publicly-traded securities. The illiquidity of our investments may make it difficult for us to obtain cash equal to the value at which we record our investments quickly if a need arises. If we are unable to obtain sufficient liquidity prior to the term redemption date, we may be forced to engage in a partial redemption or to delay a required redemption. If such a partial redemption or delay were to occur, the market price of the Series 2016 Term Preferred Stock might be adversely affected.

Other Risks

We could face losses and potential liability if intrusion, viruses or similar disruptions to our technology jeopardize our confidential information, whether through breach of our network security or otherwise.

Maintaining our network security is of critical importance because our systems store highly confidential financial models and portfolio company information. Although we have implemented, and will continue to implement, security measures, our technology platform is and will continue to be vulnerable to intrusion, computer viruses or similar disruptive problems caused by transmission from unauthorized users. The misappropriation of proprietary information could expose us to a risk of loss or litigation.

Terrorist attacks, acts of war, or national disasters may affect any market for our common stock, impact the businesses in which we invest, and harm our business, operating results, and financial conditions.

Terrorist acts, acts of war, or national disasters have created, and continue to create, economic and political uncertainties and have contributed to global economic instability. Future terrorist activities, military or security operations, or national disasters could further weaken the domestic/global economies and create additional uncertainties, which may negatively impact the businesses in which we invest directly or indirectly and, in turn, could have a material adverse impact on our business, operating results, and financial condition. Losses from terrorist attacks and national disasters are generally uninsurable.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

All statements contained in this prospectus or any accompanying prospectus supplement, other than historical facts, may constitute forward-looking statements. These statements may relate to, among other things, future events or our future performance or financial condition. In some cases, you can identify forward-looking statements by terminology such as may, might, believe, will, provided, anticipate, futur growth, plan, intend, expect, should, would, if, seek, possible, potential, likely or the negative of such terms or comparable forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others: (1) further adverse changes in the economy and the capital markets; (2) risks associated with negotiation and consummation of pending and future transactions; (3) the loss of one or more of our executive officers, in particular David Gladstone, Terry Lee Brubaker or George Stelljes III; (4) changes in our business strategy; (5) availability, terms and deployment of capital; (6) changes in our industry, interest rates, exchange rates or the general economy; (7) the degree and nature of our competition; and (8) those factors described in the Risk Factors section of this prospectus. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this prospectus. The forward-looking statements contained in this prospectus or any accompanying prospectus supplement are excluded from the safe harbor protection provided by the Private Securities Litigation Reform Act of 1995 and Section 27A of the Securities Act.

USE OF PROCEEDS

Unless otherwise specified in any prospectus supplement accompanying this prospectus, we intend to use the net proceeds from the sale of the Securities for general corporate purposes. We expect the proceeds to be used first to pay down existing short-term debt, then to make investments in small and mid-sized businesses in accordance with our investment objective, with any remaining proceeds to be used for other general corporate purposes. Indebtedness under our credit facility currently accrues interest at the rate of approximately 5.25% and matures on January 18, 2015. We anticipate that substantially all of the net proceeds of any offering of Securities will be utilized in the manner described above within three months of the completion of such offering. Pending such utilization, we intend to invest the net proceeds of any offering of Securities primarily in cash, cash equivalents, U.S. government securities, and other high-quality debt investments that mature in one year or less from the date of investment, consistent with the requirements for continued qualification as a RIC for federal income tax purposes.

PRICE RANGE OF COMMON STOCK AND DISTRIBUTIONS

We currently intend to distribute in the form of cash dividends, a minimum of 90% of our ordinary income and short-term capital gains, if any, on a quarterly basis to our stockholders in the form of monthly dividends. We intend to retain long-term capital gains and treat them as deemed distributions for tax purposes. We report the estimated tax characteristics of each dividend when declared while the actual tax characteristics of dividends are reported annually to each stockholder on Form 1099 DIV. There is no assurance that we will achieve investment results or maintain a tax status that will permit any specified level of cash distributions or year-to-year increases in cash distributions. At the option of a holder of record of common stock, all cash distributions can be reinvested automatically under our dividend reinvestment plan in additional whole and fractional shares. A stockholder whose shares are held in the name of a broker or other nominee should contact the broker or nominee regarding participation in our dividend reinvestment plan on the stockholder s behalf. See Risk Factors We will be subject to corporate-level tax if we are unable to satisfy Code requirements for RIC qualification; Dividend Reinvestment Plan; and Material U.S. Federal Income Tax Considerations.

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Our common stock is quoted on the NASDAQ under the symbol GLAD. Our common stock has historically traded at prices both above and below its net asset value. There can be no assurance, however, that any premium to net asset value will be attained or maintained. As of May 31, 2012, we had 63 stockholders of record, meaning individuals or entities that we carry in our records as the registered holder (although not necessarily the beneficial owner) of our common stock.

The following table sets forth the range of high and low intraday sale prices of our common stock as reported on the NASDAQ and the dividends declared by us for the last two completed fiscal years and the current fiscal year through May 31, 2012.

COMMON SHARE PRICE DATA

	NAV(1)	High	Low	Dividend Declared	(Discount) Premium of High Sales Price to NAV(2)	Discount of Low Sales Price to NAV(2)
Fiscal Year ended September 30, 2010						
First Quarter	$ 11.92	$ 9.50	$ 7.50	$ 0.21	(20)%	(37)%
Second Quarter	12.10	12.32	7.10	0.21	2	(41)
Third Quarter	11.81	14.06	9.58	0.21	19	(19)
Fourth Quarter	11.85	12.73	10.15	0.21	7	(14)
Fiscal Year ending September 30, 2011						
First Quarter	11.74	12.17	10.83	0.21	4	(8)
Second Quarter	11.18	12.12	10.46	0.21	8	(6)
Third Quarter	10.34	11.66	9.22	0.21	13	(11)
Fourth Quarter	10.16	9.75	6.86	0.21	(4)	(32)
Fiscal Year ending September 30, 2012						
First Quarter	9.90	8.74	6.46	0.21	(12)	(35)
Second Quarter	9.62	9.33	7.69	0.21	(3)	(20)
Third Quarter (through May 31, 2012)	*	8.46	7.31	0.21	*	*

(1) Net asset value (NAV) per share is determined as of the last day in the relevant quarter and therefore may not reflect the NAV per share on the date of the high and low intraday sale prices. The NAV per shares shown are based on outstanding shares at the end of each period.

(2) The (discounts) premiums set forth in these columns represent the high or low, as applicable, intraday sale price per share for the relevant quarter minus the NAV per share as of the end of such quarter, and therefore may not reflect the (discount) premium to NAV per share on the date of the high and low intraday sale prices.

* Not yet available, as the NAV per share as of the end of this quarter has not yet been determined.

The following are our outstanding classes of securities as of March 31, 2012.

(1) Title of Class	(2) Amount Authorized	(3) Amount Held by us or for Our Account	(4) Amount Outstanding Exclusive of Amounts Shown Under(3)
Common Stock	46,000,000		21,000,160
Term Preferred Stock	4,000,000		1,539,882

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RATIOS OF EARNINGS TO FIXED CHARGES

For the six months ended March 31, 2012 and 2011 and the years ended September 30, 2011, 2010, 2009, 2008 and 2007, the ratios of three income metrics to fixed charges of the Company, computed as set forth below, were as follows

	Six Months Ended March 31,		Year Ended September 30,				
	2012	2011	2011	2010	2009	2008	2007
Net investment income plus fixed charges to fixed charges	5.1x	6.5x	5.5x	4.0x	3.0x	3.7x	4.0x
Net investment income plus realized gains (losses) plus fixed charges to fixed charges	5.1x	6.5x	5.2x	3.5x	0.5x	3.6x	4.0x
Net (decrease) increase in net assets resulting from operations plus fixed charges to fixed charges	(0.3x)	(8.9x)	(4.2x)	3.8x	1.4x	(1.2x)	3.0x

For purposes of computing the ratios, fixed charges include interest expense on borrowings, dividend expense on mandatorily redeemable preferred stock and amortization of deferred financing fees.

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CONSOLIDATED SELECTED FINANCIAL DATA

The following table summarizes our consolidated selected financial data and other data. The consolidated selected financial data as of September 30, 2011 and 2010 and for the fiscal years ended September 30, 2011, 2010 and 2009 is derived from our audited consolidated financial statements included in this prospectus. The consolidated selected financial data as of and for the six months ended March 31, 2012 and 2011 is derived from our unaudited condensed consolidated financial statements included in this prospectus. The consolidated selected financial data as of September 30, 2009, 2008 and 2007 and for the fiscal years ended September 30, 2008 and 2007 is derived from our audited consolidated financial statements that are not included in this prospectus. The other data included in the second table is unaudited. You should read this data together with our consolidated financial statements and notes thereto presented elsewhere in this prospectus and the information under Management s Discussion and Analysis of Financial Condition and Results of Operations for more information.

	Six Months Ended March 31,		Year Ended September 30,				
	2012 (unaudited)	**2011 (unaudited)**	**2011**	**2010**	**2009**	**2008**	**2007**
Statement of operations data:							
Total investment income	**$ 20,317**	$ 16,405	$ 35,211	$ 35,539	$ 42,618	$ 45,725	$ 36,687
Total expenses net of credits from Adviser	**10,683**	7,339	16,799	17,780	21,587	19,172	14,426
Net investment income	**9,634**	9,066	18,412	17,759	21,031	26,553	22,261
Net realized and unrealized (loss) gain on investments, derivatives and borrowings	**(12,526)**	(15,316)	(39,511)	(1,365)	(17,248)	(47,815)	(7,309)
Net (decrease) increase in net assets resulting from operations	**$ (2,892)**	$ (6,250)	$ (21,099)	$ 16,394	$ 3,783	$ (21,262)	$ 14,952
Per common share data(1):							
Net (decrease) increase in net assets resulting from operations per common share							
Basic	**$ (0.14)**	$ (0.30)	$ (1.00)	$ (0.78)	$ (0.18)	$ (1.08)	$ 1.13
Diluted	**(0.14)**	(0.30)	(1.00)	(0.78)	(0.18)	(1.08)	1.13
Net investment income per common share							
Basic	**0.46**	0.43	0.88	0.84	1.00	1.35	1.69
Diluted	**0.46**	0.43	0.88	0.84	1.00	1.35	1.69
Cash distributions declared per common share	**(0.42)**	(0.42)	(0.84)	(0.84)	(1.26)	(1.68)	(1.68)
Weighted common shares outstanding (basic and diluted)	**21,022,087**	21,039,242	21,039,242	21,060,351	21,087,574	19,699,796	13,173,822
Statement of assets and liabilities data:							
Total assets	**$ 311,311**	$ 272,536	$ 317,624	$ 270,518	$ 335,910	$ 425,698	$ 367,729
Net assets	**202,002**	235,215	213,721	249,246	249,076	271,748	220,959
Net asset value per common share	**9.62**	11.18	10.16	11.85	11.81	12.89	14.97
Common shares outstanding	**21,000,160**	21,039,242	21,039,242	21,039,242	21,087,574	21,087,574	14,762,574
Senior securities data:							
Borrowings under line of credit, at cost(2)	**$ 65,800**	$ 33,200	$ 100,012	$ 17,940	$ 83,350	$ 151,030	$ 144,440
Mandatorily redeemable preferred stock	**38,497**						
Asset coverage ratio(3)	**292%**	807%	314%	1,419%	396%	279%	252%
Asset coverage per unit(4)	**$ 2,922**	$ 8,073	$ 3,144	$ 14,187	$ 3,963	$ 2,792	$ 2,294

(1) Per share data for net (decrease) increase in net assets resulting from operations is based on the weighted average common stock outstanding for both basic and diluted.

(2) See Management s Discussion and Analysis of Financial Condition and Results of Operations for more information regarding our level of indebtedness.

(3) As a business development company, we are generally required to maintain an asset coverage ratio (as defined in Section 18(h) of the 1940 Act) of at least 200% on our senior securities representing indebtedness and our senior securities that are stock. Our mandatorily redeemable preferred stock is a senior security that is stock.

(4) Asset coverage per unit is the asset coverage ratio expressed in terms of dollar amounts per one thousand of indebtedness.

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	Six Months Ended March 31,		Year Ended September 30,				
	2012	**2011**	**2011**	**2010**	**2009**	**2008**	**2007**
	(Dollar amounts in thousands, except per unit data)						
Other unaudited data:							
Number of portfolio companies as of end of period	**55**	45	59	39	48	63	56
Average size of portfolio company investment at cost	**$ 6,781**	$ 6,983	$ 6,488	$ 7,647	$ 7,592	$ 7,315	$ 6,352
Principal amount of new investments	**(29,609)**	(52,424)	(110,903)	(10,580)		(141,017)	(214,825)
Proceeds from loan repayments and investments sold	**31,219**	36,004	50,002	85,634	96,693	70,482	121,818
Weighted average yield on investments(1):	**10.91%**	11.36%	11.16%	10.85%	10.07%	10.38%	12.39%
Total return(2)	**24.46**	4.12	(33.77)	37.46	(30.94)	(13.90)	(4.40)

(1) Weighted average yield on investments equals interest income on investments divided by the annualized weighted average investment balance throughout the period.

(2) Total return equals the (decrease) increase of the ending market value over the beginning market value, taking into account monthly distributions reinvested in accordance with our dividend reinvestment plan, divided by the monthly beginning market value.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(dollar amounts in thousands, except per share data or unless otherwise indicated)

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

OVERVIEW

General

We were incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001. Our investment objective is to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, senior subordinated notes and junior subordinated notes, with a particular focus on senior notes, of established private businesses in the United States that are substantially owned by leveraged buyout funds, individual investors or are family-owned businesses. In addition, we may acquire existing loans that meet this profile from other funds. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants or other equity instruments that we may receive when we make loans. We operate as a closed-end, non-diversified management investment company, and have elected to be treated as a business development company (BDC) under the Investment Company Act of 1940, as amended (the 1940 Act). In addition, for tax purposes we have elected to be treated as a regulated investment company (RIC) under the Internal Revenue Code of 1986, as amended (the Code).

We focus on investing in small and medium-sized private U.S. businesses that meet certain criteria, including some but not all of the following: the potential for growth in cash flow, adequate assets for loan collateral, experienced management teams with a significant ownership interest in the borrower, profitable operations based on the borrower s cash flow, reasonable capitalization of the borrower (usually by leveraged buyout funds or venture capital funds) and the potential to realize appreciation and gain liquidity in our equity position, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering of the borrower s stock or by exercising our right to require the borrower to repurchase our warrants, though there can be no assurance that we will always have these rights. We lend to borrowers that need funds to finance growth, restructure their balance sheets or effect a change of control. We invest by ourselves or jointly with other funds and/or management of the portfolio company, depending on the opportunity. If we are participating in an investment with one or more co-investors, our investment is likely to be smaller than if we were investing alone.

Business Environment

While economic conditions generally appear to be improving, we remain cautious about a long-term economic recovery. The recent recession in general, and the disruptions in the capital markets in particular, have impacted our liquidity options and increased the cost of debt and equity capital. Many of our portfolio companies, as well as those that we evaluate for possible investment, are impacted by these economic conditions, and if these conditions continue to persist, it may affect their ability to repay our loans or engage in a liquidity event, such as a sale, recapitalization or initial public offering. The economic conditions could also disproportionately impact some of the industries in which we have invested, causing us to be more vulnerable to losses in our portfolio, which could cause the number of our non-performing assets to increase and the fair market value of our portfolio to decrease. We do not know when market conditions will continue to improve again or if adverse conditions will again intensify, and we do not know the full extent to which the economic downturn will affect us. If market instability persists or intensifies, we may experience continued difficulty in raising additional capital.

However, during these distressed economic times, we have been able to complete both a preferred stock public offering and a renewal of our $137.0 million line of credit (our Credit Facility defined under Financing

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Highlights discussion further below) for a three year period. In November 2011, we issued approximately 1.5 million shares of 7.125% Series 2016 Term Preferred Stock for gross proceeds of $38.5 million. In addition, in January 2012 we closed on an amendment on our $137.0 million line of credit to extend its maturity until 2015. Both of these events are discussed in further detail below under Financing Highlights.

Market conditions have affected the trading price of our common stock and our ability to finance new investments through the issuance of equity. On May 31, 2012, the closing market price of our common stock was $7.40, a 23.1% discount to our March 31, 2012 net asset value (NAV) per common share of $9.62. When our stock trades below NAV, as it has often traded over the last three years, our ability to issue equity is constrained by provisions of the 1940 Act, which generally prohibits the issuance and sale of our common stock below NAV per common share without stockholder approval other than through sales to our then-existing stockholders pursuant to a rights offering. At our annual meeting of stockholders held on February 16, 2012, our stockholders approved a proposal which authorizes us to sell shares of our common stock at a price below our then current NAV per common share subject to certain limitations (including, but not limited to, that the cumulative number of shares issued and sold pursuant to such authority does not exceed 25% of our then outstanding common stock immediately prior to each such sale) for a period of one year from the date of approval, provided that our Board of Directors makes certain determinations prior to any such sale. We expect that at the next annual stockholders meeting scheduled in February 2013, our stockholders will again be asked to vote in favor of renewing this proposal for another year.

Challenges in the current market are intensified for us by certain regulatory limitations under the Code and the 1940 Act, as well as contractual restrictions under the agreement governing our Credit Facility that further constrain our ability to access the capital markets. To maintain our qualification as a RIC, we must satisfy, among other requirements, an annual distribution requirement to pay out at least 90% of our ordinary income and short-term capital gains to our stockholders. Because we are required to distribute our income in this manner, and because the illiquidity of many of our investments makes it difficult for us to finance new investments through the sale of current investments, our ability to make new investments is highly dependent upon external financing. Our external financing sources include the issuance of equity securities, debt securities or other leverage, such as borrowings under our line of credit. Our ability to seek external debt financing, to the extent that it is available under current market conditions, is further subject to the asset coverage limitations of the 1940 Act, which require us to have an asset coverage ratio (as defined in Section 18(h) of the 1940 Act), of at least 200% immediately after each issuance of senior securities representing indebtedness and senior securities that are stock, to which we refer collectively as Senior Securities.

The continued unsteady economic recovery may also continue to cause the value of the collateral securing some of our loans to fluctuate, as well as the value of our equity investments, which has impacted and may continue to impact our ability to borrow under our Credit Facility. Additionally, our Credit Facility contains covenants regarding the maintenance of certain minimum loan concentrations and net worth covenants, which are affected by the decrease in value of our portfolio. Failure to meet these requirements would result in a default which, if we are unable to obtain a waiver from our lenders, would cause an acceleration of our repayment obligations under our Credit Facility. As of March 31, 2012, we were in compliance with all of our Credit Facility s covenants.

We expect that, given these regulatory and contractual constraints in combination with current market conditions, debt and equity capital may be costly or difficult for us to access in the near term. However, we believe that our recent public offering of Series 2016 Term Preferred Stock and our three year renewal on our Credit Facility will increase our ability to make conservative investments in businesses that we believe will weather the current economic conditions and will be likely to produce attractive long-term returns for our stockholders.

Investment Highlights

During the six months ended March 31, 2012, we extended an aggregate of $10.1 million of investments to two new portfolio companies and an aggregate of $19.5 million of investments to existing portfolio companies

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through existing revolver draws, new term notes or additions to term notes and equity. Also, during the six months ended March 31, 2012, we sold three portfolio companies for aggregate proceeds of approximately $6.5 million, and we received scheduled and unscheduled contractual principal repayments of approximately $24.8 million from existing portfolio companies, including four early payoffs.

During the fiscal year ended September 30, 2011, we extended $110.9 million in new debt and equity investments to 25 new portfolio companies, and we extended $25.4 million of investments to existing portfolio companies through revolver draws or additions to term notes. Also, during the fiscal year ended September 30, 2011, we exited five portfolio companies for aggregate proceeds of approximately $25.8 million, and we received scheduled and unscheduled contractual principal repayments of approximately $20.0 million from existing portfolio companies. Since our initial public offering in August 2001, we have made 315 different loans to, or investments in, 157 companies for a total of approximately $1.1 billion, before giving effect to principal repayments on investments and divestitures.

During the six months ended March 31, 2012, we executed the following transactions with certain of our portfolio companies:

Repayments and Exits:

During the six months ended March 31, 2012, borrowers made principal repayments totaling $24.8 million in the aggregate, consisting of $14.9 million of unscheduled early payoffs as well as $9.9 million in contractual amortization, revolver repayments and principal payments. Included in the principal payments were the net proceeds at par from early payoffs by Northern Contours, Inc. (Northern Contours) of $6.1 million, Global Materials Technology Inc. (GMT) of $2.4 million, RCS Management Holding Co. (RCS) of $4.4 million, and Ernest Health Inc. (Ernest Health) of $2.0 million. In relation to these exits, we received $1.1 million in success fees from GMT and $0.9 million in success fees from RCS.

In December 2011, we sold our investments in Newhall Holdings Inc. (Newhall) for net proceeds of $3.3 million, which resulted in a realized loss of $7.4 million recorded in the three months ended December 31, 2011.

Workouts:

Effective October 2011, we restructured Sunshine Media Holdings (Sunshine), by reducing the interest rates on its line of credit, senior term debt and LOT senior term debt to preserve Sunshine s capital to further enable it to invest in new and existing initiatives. We have also invested $1.6 million in preferred equity and $2.1 million in line of credit draws to Sunshine during the six months ended March 31, 2012. We placed our investment in Sunshine s LOT senior term debt on non-accrual status effective January 1, 2012.

In November 2011, we invested $1.6 million in Ohana Media Group (Ohana) to facilitate its purchase of certain of KMBQ Corporation s (KMBQ) assets out of receivership. In connection with this transaction, we received net proceeds of $1.2 million and recorded a realized loss during the three months ended December 31, 2011 totaling $1.0 million. Ohana replaced KMBQ on our *Condensed Consolidated Schedule of Investments* as a Non-Control/Non-Affiliate investment at December 31, 2011.

Effective January 2012, we restructured our investment in Viapack, Inc. (Viapack) by reducing the interest rates on its line of credit, senior real estate term debt and senior term debt to preserve Viapack s capital to enable it to invest in existing initiatives. We have also invested $1.8 million in line of credit draws to Viapack during the six months ended March 31, 2012. We placed our investment in Viapack s LOT senior term debt on non-accrual status effective January 1, 2012.

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During the fiscal year ended September 30, 2011, we executed the following transactions with certain of our portfolio companies:

Purchases

During the year ended September 30, 2011, we extended $95.7 million of senior term or senior subordinated syndicated loan investments to 23 new portfolio companies and $15.2 million of investments to two new proprietary portfolio companies (North American Aircraft Services LLC and Westland Technologies, Inc.). In monitoring the market activity during the year ended September 30, 2011, we noted favorable syndicate loan marketplace conditions and consequently increased our investment in such loans. The majority of our senior syndicated loan investments occurred during the quarters ended March 31 and June 30, 2011.

Repayments and Exits

During the year ended September 30, 2011, 36 borrowers made principal repayments totaling $45.8 million in the aggregate, consisting of $16.6 million in unscheduled payoffs as well as $29.2 million in contractual amortization, revolver repayments and principal payments. Included in the principal payments were payoffs of four portfolio companies at par, Interfilm Holdings, Inc., Puerto Rico Cable Acquisition Company, Inc., Pinnacle Treatment Centers, Inc. and Airvana Network Solutions, Inc. Additionally, we sold one portfolio company, Finn Corporation, for $37 in net proceeds.

Workouts

In January 2011, we purchased common stock for $1.5 million from existing shareholders of Sunshine Media Holdings (Sunshine), a publisher of regional B2B trade magazines, which gave us a controlling interest in the company and resulted in the reclassification of the investment from Non-Control/Non-Affiliate to Control during the quarter ended March 31, 2011. Additionally, we have extended $1.3 million to Sunshine Media through revolver draws between January 2011 and September 2011.

In July 2011, we increased our investment in Viapack, Inc. (Viapack), a manufacturer of polyethylene film, by adding a line of credit facility and purchasing preferred equity; which gave us a controlling interest in the company and resulted in the reclassification of the investment from Non-Control/Non-Affiliate to Control during the quarter ended September 30, 2011. The facility had $1.6 million drawn as of September 30, 2011.

In August 2011, we restructured our loan to SCI Cable, Inc. (SCI), a cable, internet and voice services provider, through a UCC Article 9 sale. This resulted in a new control entity, Kansas Cable Holdings, Inc., obtaining certain of the assets of SCI and we recognized a realized loss of $1.3 million during the quarter ended September 30, 2011. Kansas Cable Holdings, Inc. replaced SCI on the Schedule of Investments and remains on non-accrual status as of March 31, 2012.

Subsequent to March 31, 2012, we have made several investments in existing and new portfolio companies, including a $16.0 million combined senior subordinated debt and equity investment in Francis Drilling Fluids, Ltd. and a $12.0 million senior term debt investment in POP Radio LP.

Financing Highlights

Renewal of Credit Facility

On January 19, 2012, we entered into Amendment No. 3 to the fourth amended and restated credit agreement (the Credit Facility), through Gladstone Business Loan, LLC (Business Loan), to extend the maturity date of our $137.0 million line of credit from March 15, 2012 to January 18, 2015 (the Maturity Date). The interest rates remained unchanged. The Credit Facility was arranged by Key Equipment Finance Inc.

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(Keybank) as administrative agent, with Branch Banking and Trust Company (BB&T) and ING Capital LLC (ING) also joining the Credit Facility as committed lenders. Subject to certain terms and conditions, the Credit Facility may be expanded to a maximum of $237.0 million through the addition of other committed lenders to the facility. If the Credit Facility is not renewed or extended by the Maturity Date, all principal and interest will be due and payable on or before January 18, 2016 (one year after the Maturity Date). The Credit Facility also limits payments on distributions to the aggregate net investment income for each of the twelve month periods ended September 30, 2011, 2012, 2013, 2014 and 2015. The interest rates on advances under the Credit Facility remained unchanged at 30-day London Interbank Offered Rate (LIBOR) subject to a minimum rate of 1.5%, plus 3.75% per annum, with a commitment fee of 0.5% per annum on undrawn amounts when the Credit Facility is drawn more than 50% and 1.0% per annum on undrawn amounts when the Credit Facility is drawn less than 50%. We incurred fees of $1.4 million in connection with this amendment. All other terms of the Credit Facility remained substantially unchanged.

Term Preferred Stock Offering

On November 4, 2011, we completed an offering of 1.4 million shares of 7.125% Series 2016 Term Preferred Stock, par value $0.001 per share at a public offering price of $25.00 per share under a shelf registration statement on Form N-2 (File No. 333-162592) and pursuant to a prospectus dated July 15, 2011, as supplemented by a final prospectus supplement dated October 28, 2011, which was filed with the SEC on October 31, 2011. Net proceeds of the offering, after deducting underwriting discounts and estimated offering expenses borne by us were approximately $33.0 million and were used to repay a portion of outstanding borrowings under our Credit Facility. On November 17, 2011, the underwriters exercised their option to purchase an additional 139,882 shares of our Series 2016 Term Preferred Stock to cover over-allotments, for which we received net proceeds, after deducting underwriting discounts and other offering expenses, of $3.4 million. These proceeds were also used to repay a portion of outstanding borrowings under our Credit Facility.

Investment Strategy

Our strategy is to make loans at favorable interest rates to small and medium-sized U.S. businesses. Our loans typically range from $5 million to $20 million, although this investment size may vary proportionately as the size of our capital base changes, generally mature in no more than seven years and accrue interest at variable rates and to a lesser extent fixed rates. Because the majority of our portfolio loans consist of term debt of private companies that typically cannot or will not expend the resources to have their debt securities rated by a credit rating agency, we expect that most, if not all, of the debt securities we acquire will be unrated. Accordingly, we cannot accurately predict what ratings these loans might receive if they were rated, and thus cannot determine whether or not they could be considered investment grade quality.

To the extent possible, our loans generally are collateralized by a security interest in the borrower s assets. Interest payments are generally made monthly or quarterly with amortization of principal generally being deferred for several years. The principal amount of the loans and any accrued but unpaid interest generally become due in no more than seven years.

Original issue discount (OID) arises when we extend a loan and receive an equity interest in the borrower at the same time, or purchase a loan at a discount to par. To the extent that the price paid for the equity is not at market value, we must allocate part of the price paid for the loan, to the value of the equity. Then the amount allocated to the equity, the OID, must be amortized over the life of the loan. The amortization of OID also produces income that must be recognized for purposes of satisfying the distribution requirements for a RIC under Subchapter M of the Code, whereas the cash is received, if at all, when the equity instrument is sold. As of September 30, 2011, we had 27 loans with OID income, as compared to four OID loans as of September 30, 2010. We increased the number of syndicated loan investments in our portfolio during 2011, which generally have an OID component. We recorded OID income of $0.2 million for the year ended September 30, 2011, as compared to $21 for the year ended September 30, 2010. The unamortized balance of OID investments as of September 30, 2011 and 2010 totaled $1.5 million and $0.3 million, respectively.

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Some of our loans may contain a provision that calls for some portion of the interest payments to be deferred and added to the principal balance so that the interest is paid, together with the principal, at maturity. This form of deferred interest is often called paid in kind (PIK) interest and, when earned, we record PIK interest as interest income and add the PIK interest to the principal balance of the loans. We seek to avoid PIK interest with all potential investments under review. During the quarter ended June 30, 2011, our sole PIK investment was restructured and the PIK interest component was eliminated, therefore as of September 30, 2011, we had no investments that bore PIK interest, as compared to one investments with PIK interest as of September 30, 2010.

In addition, as a BDC under the 1940 Act, we are required to make available significant managerial assistance to our portfolio companies. Our investment adviser, Gladstone Management Corporation (the Adviser) provides these services on our behalf through its officers who are also our officers. Currently, neither we nor our Adviser charges a fee for managerial assistance; however, if our Adviser does receive fees for managerial assistance, our Adviser will credit the managerial assistance fees to the base management fee due from us to our Adviser.

Our Adviser and Gladstone Securities, LLC (Gladstone Securities) a broker-dealer registered with the FINRA, each an affiliate of ours, receive fees for certain services they separately provide to certain of our portfolio companies. Such fees are generally paid directly to our Adviser or Gladstone Securities, as applicable. When our Adviser receives such fees, 50% of certain of those fees and 100% of others are credited against the base management fee that we pay to our Adviser. Gladstone Securities provides certain of our portfolio companies with investment banking and due diligence services; these fees do not impact the overall fees that we pay the Adviser.

Our Adviser also receives fees for monitoring and reviewing portfolio company investments. These fees are recurring and are generally paid annually or quarterly in advance to our Adviser throughout the life of the investment. Fees of this nature are recorded as revenue by our Adviser when earned and are not credited against the base management fee. We may receive fees for the origination and closing services we provide to portfolio companies through our Adviser. These fees are paid directly to us and are recognized as other income upon closing of the originated investment.

Prior to making an investment, we ordinarily enter into a non-binding term sheet with the potential borrower. These non-binding term sheets are generally subject to a number of conditions, including, but not limited to, the satisfactory completion of our due diligence investigations of the potential borrower s business, reaching agreement on the legal documentation for the loan, and the receipt of all necessary consents. Upon execution of the non-binding term sheet, the potential borrower generally pays the Adviser a non-refundable fee for services rendered by the Adviser through the date of the non-binding term sheet. These fees are received by the Adviser and are offset against the base management fee payable to the Adviser, which has the effect of reducing our expenses to the extent of any such fees received by the Adviser.

In the event that we expend significant effort in considering and negotiating a potential investment that ultimately is not consummated, we generally will seek reimbursement from the proposed borrower for our reasonable expenses incurred in connection with the transaction, including legal fees. Any amounts collected for expenses incurred by the Adviser in connection with unconsummated investments will be reimbursed to the Adviser. Amounts collected for these expenses incurred by us will be reimbursed to us and will be recognized in the period in which such reimbursement is received, however, there can be no guarantee that we will be successful in collecting any such reimbursements.

Our Adviser and Administrator

Our Adviser is led by a management team which has extensive experience in our lines of business. Our Adviser is controlled by David Gladstone, our chairman and chief executive officer. Mr. Gladstone is also the chairman and chief executive officer of our Adviser. Terry Lee Brubaker, our vice chairman, chief operating officer, secretary and director, is a member of the board of directors of our Adviser and its vice chairman and

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chief operating officer and has substantial experience in acquisitions and operations of companies. George Stelljes III, our president, chief investment officer and director, is a member of the board of directors of our Adviser and its president and chief investment officer and has extensive experience in leveraged finance. Gladstone Administration, LLC (the Administrator), an affiliate of our Adviser, employs our chief financial officer, chief accounting officer, chief compliance officer, internal counsel, and their respective staffs.

Our Adviser and Administrator also provide investment advisory and administrative services to certain of our affiliates, including but not limited to, Gladstone Commercial Corporation (Gladstone Commercial), a publicly-traded real estate investment trust; Gladstone Investment Corporation (Gladstone Investment), a publicly-traded BDC and RIC; Gladstone Lending Corporation (Gladstone Lending), a private corporation that was formed to primarily invest in first and second lien term loans that has filed a registration statement on Form N-2 with the SEC, but which has not yet commenced operations; Gladstone Partners Fund, L.P., a private partnership fund formed primarily to co-invest with us and Gladstone Investment and Gladstone Land Corporation (Gladstone Land), a private agricultural real estate company. Excluding our chief financial officer and treasurer and chief accounting officer, all of our executive officers serve as either directors or executive officers, or both, of our Adviser, our Administrator, Gladstone Commercial, Gladstone Investment and Gladstone Land. Our chief financial officer and treasurer also serves as an executive officer of Gladstone Investment. In the future, our Adviser and Administrator may provide investment advisory and administrative services, respectively, to other funds, both public and private.

Investment Advisory and Management Agreement

Under the amended and restated investment advisory agreement (Advisory Agreement), we pay our Adviser an annual base management fee of 2% of our average gross assets, which is defined as total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings, valued 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.

We also pay our Adviser a two-part incentive fee under the Advisory Agreement. The first part of the incentive fee is an income-based incentive fee which rewards our Adviser if our quarterly net investment income (before giving effect to any incentive fee) exceeds 1.75% of our net assets (the hurdle rate). The second part of the incentive fee is a capital gains-based incentive fee that is determined and payable in arrears as of the end of each fiscal year (or upon termination of the Advisory Agreement, as of the termination date), and equals 20% of our realized capital gains as of the end of the fiscal year. In determining the capital gains-based incentive fee payable to our Adviser, we will calculate the cumulative aggregate realized capital gains and cumulative aggregate realized capital losses since our inception, and the aggregate unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in our portfolio. The Adviser has not earned the capital gains-based portion of the incentive fee since our inception.

We pay our direct expenses including, but not limited to, directors fees, legal and accounting fees, stockholder related expenses, and directors and officers insurance under the Advisory Agreement.

Beginning in April 2006, our Board of Directors has accepted from the Adviser, unconditional and irrevocable voluntarily waivers on a quarterly basis to reduce the annual 2.0% base management fee on senior syndicated loans to 0.5% to the extent that proceeds resulting from borrowings were used to purchase such syndicated loan participations. In addition to the base management and incentive fees under the Advisory Agreement, 50% of certain fees and 100% of others received by the Adviser from our portfolio companies are credited against the investment advisory fee and paid to the Adviser.

The Adviser services our loan portfolio, pursuant to a loan servicing agreement with our wholly-owned subsidiary Business Loan, in return for a 1.5% annual fee, based on the monthly aggregate outstanding loan balance of the loans pledged under the Credit Facility.

On July 12, 2011, our Board of Directors approved the renewal of the Advisory Agreement with our Adviser through August 31, 2012. We expect that our Board of Directors will approve a further one year renewal in July 2012.

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Administration Agreement

We are party to an administration agreement with our Administrator (the Administration Agreement), whereby we pay separately for administrative services. The Administration Agreement provides for payments equal to our allocable portion of the Administrator s overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent and our allocable portion of the salaries and benefits expenses of our chief financial officer, chief accounting officer, chief compliance officer, internal counsel, and their respective staffs. Our allocable portion of expenses is generally derived by multiplying our Administrator s total allocable expenses by the percentage of our total assets at the beginning of the quarter in comparison to the total assets at the beginning of the quarter of all companies managed by our Adviser under similar agreements. On July 12, 2011, our Board of Directors approved the renewal of this Administration Agreement through August 31, 2012. We expect that our Board of Directors will approve a further one year renewal in July 2012.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with GAAP requires management to make estimates and assumptions that affect the reported consolidated amounts of assets and liabilities, including disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ materially from those estimates. We have identified our investment valuation process as our most critical accounting policy.

Investment Valuation

The most significant estimate inherent in the preparation of our *Condensed Consolidated Financial Statements* is the valuation of investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

General Valuation Policy: We value our investments in accordance with the requirements of the 1940 Act. As discussed more fully below, we value securities for which market quotations are readily available and reliable at their market value. We value all other securities and assets at fair value as determined in good faith by our Board of Directors. Such determination of fair values may involve subjective judgments and estimates.

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value and expands disclosures about assets and liabilities measured at fair value. ASC 820 provides a consistent definition of fair value that focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. ASC 820 also establishes the following three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;

Level 2 inputs to the valuation methodology include quoted prices for similar assets and liabilities in active or inactive markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level 2 inputs are in those markets for which there are few transactions, the prices are not current, little public information exists or instances where prices vary substantially over time or among brokered market makers; and

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs are those inputs that reflect the assumptions that market participants would use when pricing the asset or liability and can include our own assumptions, based upon the best available information.

As of March 31, 2012 and September 30, 2011, all of our investments were valued using Level 3 inputs. See Note 3 *Investments* in the accompanying notes to our *Condensed Consolidated Financial Statements* included

elsewhere in this prospectus for additional information regarding fair value measurements and our application of ASC 820.

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We use generally accepted valuation techniques to value our portfolio unless we have specific information about the value of an investment to determine otherwise. From time to time we may accept an appraisal of a business in which we hold securities. These appraisals are expensive and occur infrequently, but provide a third-party valuation opinion that may differ in results, techniques and scope used to value our investments. When these specific third-party appraisals are obtained, we would use estimates of value provided by such appraisals and our own assumptions including estimated remaining life, current market yield and interest rate spreads of similar securities, as of the measurement date, to value our investments.

In determining the value of our investments, our Adviser has established an investment valuation policy (the Policy). The Policy has been approved by our Board of Directors, and each quarter our Board of Directors reviews whether our Adviser has applied the Policy consistently and votes whether or not to accept the recommended valuation of our investment portfolio.

The Policy, which is summarized below, applies to the following categories of securities:

- Publicly traded securities;

- Securities for which a limited market exists; and

- Securities for which no market exists.

Valuation Methods:

Publicly traded securities: We determine the value of publicly traded securities based on the closing price for the security on the exchange or securities market on which it is listed and primarily traded on the valuation date. To the extent that we own restricted securities that are not freely tradable, but for which a public market otherwise exists, we will use the market value of that security adjusted for any decrease in value resulting from the restrictive feature.

Securities for which a limited market exists: We value securities that are not traded on an established secondary securities market, but for which a limited market for the security exists, such as certain participations in, or assignments of, syndicated loans, at the quoted bid price (which are non-binding). In valuing these assets, we assess trading activity in an asset class, evaluate variances in prices and other market insights to determine if any available quote prices are reliable. If we conclude that quotes based on active markets or trading activity may be relied upon, firm bid prices are requested; however, if a firm bid price is unavailable, we base the value of the security upon the indicative bid price (IBP) offered by the respective originating syndication agent s trading desk, or secondary desk, on or near the valuation date. To the extent that we use the IBP as a basis for valuing the security, our Adviser may take further steps to consider additional information to validate that price in accordance with the Policy.

In the event these limited markets become illiquid to a degree that market prices are no longer readily available, we will value our syndicated loans using alternative methods, such as estimated net present values of the future cash flows or discounted cash flows (DCF). The use of a DCF methodology follows that prescribed by ASC 820, which provides guidance on the use of a reporting entity s own assumptions about future cash flows and risk-adjusted discount rates when relevant observable inputs, such as quotes in active markets, are not available. When relevant observable market data does not exist, the alternative outlined in ASC 820 is the valuation of investments based on DCF. For the purposes of using DCF to provide fair value estimates, we consider multiple inputs such as a risk-adjusted discount rate that incorporates adjustments that market participants would make both for nonperformance and liquidity risks. As such, we developed a modified discount rate approach that incorporates risk premiums including, among other things, increased probability of default, or higher loss given default, or increased liquidity risk. The DCF valuations applied to the syndicated loans provide an estimate of what we believe a market participant would pay to purchase a syndicated loan in an active market, thereby establishing a fair value. We apply the DCF methodology in illiquid markets until quoted prices are available or are deemed reliable based on trading activity.

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As of March 31, 2012 and September 30, 2011, we determined that the indicative bid prices were reliable indicators of fair value for our syndicated investments. However, because of the private nature of this marketplace (meaning actual transactions are not publicly-reported), we determined that these valuation inputs were classified as Level 3 within the fair value hierarchy as defined in ASC 820.

Securities for which no market exists: The valuation methodology for securities for which no market exists falls into four categories: (1) portfolio investments comprised solely of debt securities; (2) portfolio investments in controlled companies comprised of a bundle of securities, which can include debt and equity securities; (3) portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities; and (4) portfolio investments comprised of non-publicly traded non-control equity securities of other funds.

(1) *Portfolio investments comprised solely of debt securities:* Debt securities that are not publicly traded on an established securities market, or for which a limited market does not exist (Non-Public Debt Securities), and that are issued by portfolio companies in which we have no equity or equity-like securities, are fair valued in accordance with the terms of the Policy, which utilizes opinions of value submitted to us by Standard & Poor s Securities Evaluations, Inc. (SPSE). We may also submit paid-in-kind (PIK) interest to SPSE for their evaluation when it is determined that PIK interest is likely to be received.

In the case of Non-Public Debt Securities, we have engaged SPSE to submit opinions of value for our debt securities that are issued by portfolio companies in which we own no equity, or equity-like securities. SPSE will only evaluate the debt portion of our investments for which we specifically request evaluation and may decline to make requested evaluations for any reason, at its sole discretion. Upon completing our collection of data with respect to the investments (which may include the information described below under Credit Information, the risk ratings of the loans described below under Loan Grading and Risk Rating and the factors described hereunder), this valuation data is forwarded to SPSE for review and analysis. SPSE makes its independent assessment of the data that we have assembled and assesses its independent data to form an opinion as to what they consider to be the market values for the securities. With regard to its work, SPSE has issued the following paragraph:

SPSE provides evaluated price opinions which are reflective of what SPSE believes the bid side of the market would be for each loan after careful review and analysis of descriptive, market and credit information. Each price reflects SPSE s best judgment based upon careful examination of a variety of market factors. Because of fluctuation in the market and in other factors beyond its control, SPSE cannot guarantee these evaluations. The evaluations reflect the market prices, or estimates thereof, on the date specified. The prices are based on comparable market prices for similar securities. Market information has been obtained from reputable secondary market sources. Although these sources are considered reliable, SPSE cannot guarantee their accuracy.

SPSE opinions of the value of our debt securities that are issued by portfolio companies in which we do not own equity, or equity-like securities, are submitted to our Board of Directors along with our Adviser s supplemental assessment and recommendation regarding valuation of each of these investments. Our Adviser generally accepts the opinion of value given by SPSE; however, in certain limited circumstances, such as when our Adviser may learn new information regarding an investment between the time of submission to SPSE and the date of our Board of Directors assessment, our Adviser s conclusions as to value may differ from the opinion of value delivered by SPSE. Our Board of Directors then reviews whether our Adviser has followed its established procedures for determinations of fair value and votes to accept or reject the recommended valuation of our investment portfolio. Our Adviser and our management recommended, and our Board of Directors voted to accept, the opinions of value delivered by SPSE on the loans in our portfolio as denoted on our accompanying *Condensed Consolidated Schedule of Investments*.

Because there is a delay between when we close an investment and when the investment can be evaluated by SPSE, new loans are not valued immediately by SPSE; rather, management makes its own determination about the value of these investments in accordance with our valuation policy using the methods described herein.

(2) *Portfolio investments in controlled companies comprised of a bundle of investments, which can include debt and equity securities:* The fair value of these investments is determined based on the total enterprise value

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(TEV) of the portfolio company, or issuer, utilizing a liquidity waterfall approach. Under ASC 820 for Non-Public Debt Securities and equity or equity-like securities (e.g. preferred equity, common equity, or other equity-like securities) that are purchased together as part of a package, where we have control or could gain control through an option or warrant security, both the debt and equity securities of the portfolio investment would exit in the mergers and acquisitions market as the principal market, generally through a sale of the portfolio company. We manage our risk related to these investments at the aggregated issuer level and generally exit the debt and equity securities together. Applying the liquidity waterfall approach to all of the investments of an issuer, we first calculate the TEV of the issuer by incorporating some or all of the following factors:

the issuer s ability to make payments;

the earnings of the issuer;

recent sales to third parties of similar securities;

the comparison to publicly traded securities; and

DCF or other pertinent factors.

In gathering the sales to third parties of similar securities, we may gather and analyze industry statistics and use outside experts. TEV is only an estimate of value and may not be the value received in an actual sale. Once we have estimated the TEV of the issuer, we subtract the value of all the debt securities of the issuer, which are valued at the contractual principal balance. Fair values of these debt securities are discounted for any shortfall of TEV over the total debt outstanding for the issuer. Once the values for all outstanding senior securities (which include the debt securities) have been subtracted from the TEV of the issuer, the remaining amount, if any, is used to determine the value of the issuer s equity or equity like securities. If, in our Adviser s judgment, the liquidity waterfall approach does not accurately reflect the value of the debt component, our Adviser may recommend that we use a valuation by SPSE, or if that is unavailable, a DCF valuation technique.

(3) *Portfolio investments in non-controlled companies comprised of a bundle of investments, which can include debt and equity securities:* We value Non-Public Debt Securities that are purchased together with equity or equity-like securities from the same portfolio company, or issuer, for which we do not control or cannot gain control as of the measurement date, using a hypothetical secondary market as our principal market. In accordance with ASC 820 (as amended by the FASB s Accounting Standards Update No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (IFRS), (ASU 2011-04)), we have defined our unit of account at the investment level (either debt or equity) and as such determine our fair value of these non-control investments assuming the sale of an individual security using the standalone premise of value. As such, we estimate the fair value of the debt component using estimates of value provided by SPSE and our own assumptions in the absence of observable market data, including synthetic credit ratings, estimated remaining life, current market yield and interest rate spreads of similar securities as of the measurement date. For equity or equity-like securities of investments for which we do not control or cannot gain control as of the measurement date, we estimate the fair value of the equity based on factors such as the overall value of the issuer, the relative fair value of other units of account including debt, or other relative value approaches. Consideration also is given to capital structure and other contractual obligations that may impact the fair value of the equity. Furthermore, we may utilize comparable values of similar companies, recent investments and indices with similar structures and risk characteristics or DCF valuation techniques and, in the absence of other observable market data, our own assumptions.

(4) *Portfolio investments comprised of non-publicly traded non-control equity securities of other funds:* We value any uninvested capital of the non-control fund at par value and value any invested capital at the value provided by the non-control fund.

Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly and materially from the values that would have been obtained had a ready market for the securities existed.

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Additionally, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. There is no single standard for determining fair value in good faith, as fair value depends upon circumstances of each individual case. In general, fair value is the amount that we might reasonably expect to receive upon the current sale of the security in an orderly transaction between market participants at the measurement date.

Valuation Considerations: From time to time, depending on certain circumstances, the Adviser may use the following valuation considerations, including but not limited to:

- the nature and realizable value of the collateral;
- the portfolio company s earnings and cash flows and its ability to make payments on its obligations;
- the markets in which the portfolio company does business;
- the comparison to publicly traded companies; and
- DCF and other relevant factors.

Because such valuations, particularly valuations of private securities and private companies, are not susceptible to precise determination, may fluctuate over short periods of time, and may be based on estimates, our determinations of fair value may differ from the values that might have actually resulted had a readily available market for these securities been available.

Credit Information: Our Adviser monitors a wide variety of key credit statistics that provide information regarding our portfolio companies to help us assess credit quality and portfolio performance. We and our Adviser participate in the periodic board meetings of our portfolio companies in which we hold Control and Affiliate investments and also require them to provide annual audited and monthly unaudited financial statements. Using these statements or comparable information and board discussions, our Adviser calculates and evaluates the credit statistics.

Loan Grading and Risk Rating: As part of our valuation procedures above, we risk rate all of our investments in debt securities. For syndicated loans that have been rated by a Nationally Recognized Statistical Rating Organization (NRSRO), we use the NRSRO s risk rating for such security. For all other debt securities, we use a proprietary risk rating system. Our risk rating system uses a scale of 0 to 10, with 10 being the lowest probability of default. This system is used to estimate the probability of default on debt securities and the probability of loss if there is a default. These types of systems are referred to as risk rating systems and are used by banks and rating agencies. The risk rating system covers both qualitative and quantitative aspects of the business and the securities we hold.

For the debt securities for which we do not use a third-party NRSRO risk rating, we seek to have our risk rating system mirror the risk rating systems of major risk rating organizations, such as those provided by an NRSRO. While we seek to mirror the NRSRO systems, we cannot provide any assurance that our risk rating system will provide the same risk rating as an NRSRO for these securities. The following chart is an estimate of the relationship of our risk rating system to the designations used by two NRSROs as they risk rate debt securities of major companies. Because our system rates debt securities of companies that are unrated by any NRSRO, there can be no assurance that the correlation to the NRSRO set out below is accurate. We believe our risk rating would be significantly higher than a typical NRSRO risk rating because the risk rating of the typical NRSRO is designed for larger businesses. However, our risk rating has been designed to risk rate the securities of smaller businesses that are not rated by a typical NRSRO. Therefore, when we use our risk rating on larger business securities, the risk rating is higher than a typical NRSRO rating. The primary difference between our risk rating and the rating of a typical NRSRO is that our risk rating uses more quantitative determinants and includes qualitative determinants that we believe are not used in the NRSRO rating. It is our understanding that most debt securities of medium-sized companies do not exceed the grade of BBB on an NRSRO scale, so there would be no debt securities in the middle market that would meet the definition of AAA, AA or A. Therefore, our scale begins with the designation >10 as the best risk rating which may be equivalent to a BBB from an NRSRO; however, no assurance can be given that a >10 on our scale is equal to a BBB or Baa2 on an NRSRO scale.

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Company s System	First NRSRO	Second NRSRO	Gladstone Capital s Description[(A)]
>10	Baa2	BBB	Probability of Default (PD) during the next ten years is 4% and the Expected Loss upon Default (EL) is 1% or less
10	Baa3	BBB-	PD is 5% and the EL is 1% to 2%
9	Ba1	BB+	PD is 10% and the EL is 2% to 3%
8	Ba2	BB	PD is 16% and the EL is 3% to 4%
7	Ba3	BB-	PD is 17.8% and the EL is 4% to 5%
6	B1	B+	PD is 22% and the EL is 5% to 6.5%
5	B2	B	PD is 25% and the EL is 6.5% to 8%
4	B3	B-	PD is 27% and the EL is 8% to 10%
3	Caa1	CCC+	PD is 30% and the EL is 10% to 13.3%
2	Caa2	CCC	PD is 35% and the EL is 13.3% to 16.7%
1	Caa3	CC	PD is 65% and the EL is 16.7% to 20%
0	N/A	D	PD is 85% or there is a payment default and the EL is greater than 20%

(A) *The default rates set forth are for a ten year term debt security. If a debt security is less than ten years, then the probability of default is adjusted to a lower percentage for the shorter period, which may move the security higher on our risk rating scale.*

The above scale gives an indication of the probability of default and the magnitude of the loss if there is a default. Generally, our policy is to stop accruing interest on an investment if we determine that interest is no longer collectable. At March 31, 2012, eight portfolio companies were either fully or partially on non-accrual with an aggregate cost basis of approximately $43.8 million, or 12.1% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of approximately $4.6 million, or 1.7% of the fair value of all debt investments in our portfolio. At September 30, 2011, eight portfolio companies were on non-accrual with an aggregate cost basis of $41.1 million, or 11.0% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of $5.3 million, or 1.8% of the fair value of all debt investments in our portfolio. Additionally, we do not risk rate our equity securities.

The following table lists the risk ratings for all non-syndicated loans in our portfolio at March 31, 2012, September 30, 2011 and September 30, 2010, representing approximately 66%, 70% and 94%, respectively, of all loans in our portfolio at fair value at the end of each period:

Rating	March 31, 2012	Sept. 30, 2011	Sept. 30, 2010
Highest	10.0	9.0	10.0
Average	5.8	5.5	6.1
Weighted Average	6.2	5.9	5.7
Lowest	1.0	1.0	1.0

The following table lists the risk ratings for all syndicated loans in our portfolio that were not rated by an NRSRO at March 31, 2012, September 30, 2011 and September 30, 2010, representing approximately 12%, 6% and 2%, respectively, of all loans in our portfolio at fair value at the end of each period:

Rating	March 31, 2012	Sept. 30, 2011	Sept. 30, 2010
Highest	7.0	7.0	7.0
Average	5.0	5.0	7.0
Weighted Average	4.9	5.0	7.0
Lowest	4.0	4.0	7.0

For syndicated loans that are currently rated by an NRSRO, we risk rate such loans in accordance with the risk rating systems of major risk rating organizations, such as those provided by an NRSRO. The following table

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lists the risk ratings for all syndicated loans in our portfolio that were rated by an NRSRO at March 31, 2012, September 30, 2011 and September 30, 2010, representing approximately 22%, 24% and 4%, respectively, of all loans in our portfolio at the end of each period:

Rating	March 31, 2012	Sept. 30, 2011	Sept. 30, 2010
Highest	B+/B1	B+/B1	B+/B2
Average	B/B2	B/B2	B+/B2
Weighted Average	B/B2	B/B2	B+/B2
Lowest	NR/Caa1	NR/Caa2	B2

Tax Status

Federal Income Taxes

We intend to continue to qualify for treatment as a RIC under Subtitle A, Chapter 1 of Subchapter M of the Code. As a RIC, we are not subject to federal income tax on the portion of our taxable income and gains distributed to stockholders. To qualify as a RIC, we must meet certain source-of-income, asset diversification and annual distribution requirements. Under the annual distribution requirements, we are required to distribute to stockholders at least 90% of our investment company taxable income, as defined by the Code. Our practice has been to pay out as distributions up to 100% of that amount.

In an effort to limit certain excise taxes imposed on RICs, we generally distribute, during each calendar year, an amount at least equal to the sum of: (1) 98% of our ordinary income for the calendar year, (2) 98.2% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year, and (3) any ordinary income and net capital gains from preceding years that were not distributed during such years. Under the RIC Modernization Act (the RIC Act), we will be permitted to carry forward capital losses incurred in taxable years beginning after September 30, 2011, for an unlimited period. However, any losses incurred during those future taxable years will be required to be utilized prior to the losses incurred in pre-enactment taxable years, which carry an expiration date. As a result of this ordering rule, pre-enactment capital loss carryforwards may be more likely to expire unused. Additionally, post-enactment capital loss carryforwards will retain their character as either short-term or long-term capital losses rather than being considered all short-term as permitted under the previous regulation.

In 2011, we received approval for a change in accounting method from the IRS related to our tax treatment for success fees. As a result, we, in effect, will continue to account for the recognition of income from the success fees upon receipt, or when the amount becomes fixed. However, starting January 1, 2011, the tax characterization of the success fee amount was and will continue to be treated as ordinary income. Prior to January 1, 2011, we had treated the success fee amount as a capital gain for tax characterization purposes. The approved change in accounting method does not require us to retroactively change the capital gains treatment of the success fees received prior to January 1, 2011.

Revenue Recognition

Investment Income Recognition

Interest income, adjusted for amortization of premiums and acquisition costs and for the accretion of discounts, is recorded on an accrual basis to the extent that such amounts are expected to be collected. Generally, when a loan becomes 90 days or more past due or if our qualitative assessment indicates that the debtor is unable to service its debt or other obligations, we will place the loan on non-accrual status and cease recognizing interest income on that loan until the borrower has demonstrated the ability and intent to pay contractual amounts due. However, we remain contractually entitled to this interest. Interest payments received on non-accrual loans may be recognized as income or applied to the cost basis 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

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likely to remain current, or due to a restructuring such that the interest income is deemed to be collectible. At March 31, 2012, eight portfolio companies were either fully or partially on non-accrual with an aggregate cost basis of approximately $43.8 million, or 12.1% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of approximately $4.6 million, or 1.7% of the fair value of all debt investments in our portfolio. As of September 30, 2011, eight portfolio companies were on non-accrual with an aggregate cost basis of $41.1 million, or 11.0%, of the cost basis of all debt investments in our portfolio, and an aggregate fair value of $5.3 million, or 1.8%, of the fair value of all debt investments in our portfolio. As of September 30, 2010, six portfolio companies were on non-accrual with an aggregate cost basis of $29.9 million, or 10.2%, of the cost basis of all debt investments in our portfolio, and an aggregate fair value of $8.7 million, or 3.4%, of the fair value of all debt investments in our portfolio.

As of March 31, 2012 and September 30, 2011, we had no loans in our portfolio which contained a PIK provision. As of September 30, 2010, we had one loan in our portfolio which contained a PIK provision. Any PIK interest, computed at the contractual rate specified in each loan agreement, is added to the principal balance of the loan and recorded as income. To maintain our status as a RIC, this non-cash source of income must be paid out to common stockholders in the form of distributions, even though we have not yet collected the cash. We recorded no PIK income for the three and six months ended March 31, 2012 and $4 and $8 for the three and six months ended March 31, 2011. We recorded PIK income of $12, $67 and $166 for the years ended September 30, 2011, 2010 and 2009, respectively.

We also transfer past due interest to the principal balance as stipulated in certain loan amendments with portfolio companies. We did not transfer any past due interest to principal balances during the three and six months ended March 31, 2012 and we transferred past due interest to the principal balance of $0.2 million for both the three and six months ended March 31, 2011, respectively. For the years ended September 30, 2011, 2010 and 2009, we rolled over past due interest to the principal balance of $0.2 million, $1.2 million and $1.5 million, respectively.

As of March 31, 2012, we had 27 OID loans. We recorded OID income of $74 and $0.2 million for the three and six months ended March 31, 2012 and $29 and $53 for the three and six months ended March 31, 2011. For the years ended September 30, 2011, 2010 and 2009, we recorded OID income of $0.2 million, $21 and $206, respectively. The unamortized balance of OID investments as of March 31, 2012, September 30, 2011 and September 30, 2010 totaled $1.4 million, $1.5 million and $0.3 million, respectively.

Success fees are recorded upon receipt. Success fees are contractually due upon a change of control in a portfolio company and are recorded in other income in our accompanying condensed consolidated statements of operations. We recorded $2.0 million of success fees during the six months ended March 31, 2012, which resulted from our exit of Global Materials Technologies, Inc. (GMT) and RCS Management Holding Co. (RCS). We recorded $0.6 million of success fees during the six months ended March 31, 2011, which resulted from our exits of Interfilm Holdings, Inc. (Interfilm) and Pinnacle Treatment Centers, Inc. (Pinnacle). For the years ended September 30, 2011, 2010 and 2009, we recorded success fees of $1.0 million, $1.9 million and $0.4 million, respectively.

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RESULTS OF OPERATIONS

COMPARISON OF THE THREE MONTHS ENDED MARCH 31, 2012 TO THE THREE MONTHS ENDED MARCH 31, 2011

A comparison of our operating results for the three months ended March 31, 2012 and 2011 is below:

	For the Three Months Ended March 31,			
	2012	2011	$ Change	% Change
INVESTMENT INCOME				
Interest income	$ 8,954	$ 7,290	$ 1,664	22.8%
Other income	2,042	1,108	934	84.3
Total investment income	10,996	8,398	2,598	30.9
EXPENSES				
Base management fee	1,538	1,365	173	12.7
Incentive fee	1,304	1,102	202	18.3
Administration fee	209	175	34	19.4
Interest expense	999	478	521	109.0
Dividend expense on mandatorily redeemable preferred stock	686		686	NM
Amortization of deferred financing fees	277	368	(91)	(24.7)
Professional fees	362	201	161	80.1
Other expenses	528	383	145	37.9
Expenses before credits from Adviser	5,903	4,072	1,831	45.0
Credits to fees from Adviser	(123)	(102)	(21)	(20.6)
Total expenses net of credits	5,780	3,970	1,810	45.6
NET INVESTMENT INCOME	5,216	4,428	788	17.8
REALIZED AND UNREALIZED (LOSS) GAIN:				
Net realized gain on investments	37	5	32	640.0
Net unrealized depreciation on investments	(7,169)	(13,069)	5,900	45.1
Net unrealized depreciation on borrowings	313	255	58	22.7
Net loss on investments and borrowings	(6,819)	(12,809)	5,990	46.8
NET DECREASE IN NET ASSETS RESULTING FROM OPERATIONS	$ (1,603)	$ (8,381)	$ 6,778	80.9%

NM = Not Meaningful

Investment Income

Interest income from our investments in debt securities increased for the three months ended March 31, 2012 by 22.8%, as compared to the three months ended March 31, 2011, for several reasons, but primarily due to the increased investment activity during the second half of fiscal year 2011, partially offset by a decline in our weighted average yield when comparing the quarter ended March 31, 2012 to the prior year quarter. The increase in investment activity was primarily in syndicated investments, which increased from 12 investments as of March 31, 2011, to 24 investments as of March 31, 2012. The level of interest income from investments is directly related to the principal balance of the interest-bearing investment portfolio outstanding during the period multiplied by the weighted average yield. The weighted average principal balance of our interest-bearing investment portfolio during the quarter ended March 31, 2012 was $325.6 million, compared to $256.9 million for the prior year quarter. The annualized weighted average yield on our interest-bearing investment portfolio for the three months ended March 31, 2012 was 11.0%, compared to 11.3% for the prior year period. The weighted average yield varies from period to period based on the current stated interest rate on interest-bearing

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investments. The decrease in the weighted average yield on our portfolio for the quarter ended March 31, 2012 resulted primarily from the purchase of syndicated loans, which generally bear lower interest rates than our existing proprietary debt investments and the restructuring of our debt investments in certain of our portfolio companies to lower interest rates. During the three months ended March 31, 2012, eight portfolio companies were either fully or partially on non-accrual, for an aggregate of $43.8 million at cost, or 12.1% of the aggregate cost of our debt investment portfolio, and during the prior year period, six portfolio companies were on non-accrual, for an aggregate of $30.4 million at cost, or 9.9% of the aggregate cost of our debt investment portfolio.

Other income for the three months ended March 31, 2012 consisted primarily of $1.1 million in success fees from the early payoff of GMT and $0.9 million in success fees from the early payoff of RCS. During the three months ended March 31, 2011, we received $0.6 million in a settlement related, in part, to US Healthcare Communications, Inc. (US Healthcare) and $0.5 million in success fees earned from our exit in Pinnacle.

The following tables list the investment income from investments in our five largest portfolio company investments at fair value during the respective periods:

	As of March 31, 2012		Three Months Ended March 31, 2012	
Company	**Fair Value**	**% of Portfolio**	**Investment Income**	**% of Total Revenues**
Reliable Biopharmaceutical Holdings, Inc.	$ 27,392	9.5%	$ 801	7.3%
Westlake Hardware, Inc.	19,340	6.7	645	5.9
Midwest Metal Distribution, Inc.	17,870	6.2	559	5.1
Defiance Integrated Technologies, Inc.	16,041	5.6	204	1.8
CMI Acquisition, LLC	14,194	4.9	507	4.6
Subtotal five largest investments	**94,837**	**32.9**	**2,716**	**24.7**
Other portfolio companies	193,330	67.1	8,217	74.7
Other non-portfolio company revenue			63	0.6
Total investment portfolio	**$ 288,167**	**100.0%**	**$ 10,996**	**100.0%**

	As of March 31, 2011		Three Months Ended March 31, 2011	
Company	**Fair Value**	**% of Portfolio**	**Investment Income**	**% of Total Revenues**
Reliable Biopharmaceutical Holdings, Inc.	$ 25,699	10.0%	$ 770	9.2%
Westlake Hardware, Inc.	19,570	7.6	638	7.6
Midwest Metal Distribution, Inc.	16,179	6.3	553	6.6
Defiance Integrated Technologies, Inc.	13,680	5.3	225	2.7
Sunshine Media Holdings	13,161	5.1	637	7.6
Subtotal five largest investments	**88,289**	**34.3**	**2,823**	**33.7**
Other portfolio companies	168,824	65.7	5,453	64.9
Other non-portfolio company revenue			122	1.4
Total investment portfolio	**$ 257,113**	**100.0%**	**$ 8,398**	**100.0%**

Operating Expenses

Operating expenses, net of credits to fees from the Adviser, increased for the three months ended March 31, 2012 by 45.6%, as compared to the prior year period. This increase was primarily due to an increase in interest expense on our Credit Facility and the distributions on our Term Preferred Stock during the quarter ended March 31, 2012.

Interest expense increased for the three months ended March 31, 2012, as compared to the prior year period, primarily due to increased borrowings under our Credit Facility to facilitate our increased investment activity

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during the three months ended March 31, 2012, as compared to the prior year period. The weighted average balance outstanding on our Credit Facility during the quarter ended March 31, 2012 was approximately $62.0 million, as compared to $14.5 million in the prior year period, an increase of 328.8%.

During the three months ended March 31, 2012, we paid $0.7 million of dividends on our Term Preferred Stock. We classify these dividends as dividend expense on our Condensed Consolidated Statements of Operations. There were no preferred stock dividends paid in the three months ended March 31, 2011, as our Term Preferred Stock offering occurred in November 2011.

The base management fee increased for the three months ended March 31, 2012, as compared to the prior year period, primarily due to the greater amount of total assets subject to the base management fee that we held, resulting from a net increase in investment production. An incentive fee was earned by the Adviser during the three months ended March 31, 2012, due primarily to increased investment income.

The base management and incentive fees are computed quarterly, as described under Investment Advisory and Management Agreement in Note 4 of the notes to our accompanying Condensed Consolidated Financial Statements and are summarized in the following table:

	Three Months Ended March 31, 2012	**2011**
Average total assets subject to base management fee [(A)]	**$ 307,600**	$ 273,000
Multiplied by prorated annual base management fee of 2.0%	**0.5%**	0.5%
Gross base management fee [(B)]	**$ 1,538**	$ 1,365
Reduction for loan servicing fees	**(864)**	(757)
Base management fee	**674**	608
Credit for fees received by Adviser from the portfolio companies	**(5)**	
Fee reduction for the voluntary, irrevocable waiver of 2.0% fee on senior syndicated loans to 0.5% per annum	**(118)**	(81)
Net base management fee	**$ 551**	$ 527
Incentive fee [(B)]	**1,304**	1,102
Credit from voluntary, irrevocable waiver issued by Adviser s board of directors		(21)
Net incentive fee	**$ 1,304**	$ 1,081
Credit for fees received by Adviser from the portfolio companies	**(5)**	
Fee reduction for the voluntary, irrevocable waiver of 2.0% fee on senior syndicated loans to 0.5% per annum	**(118)**	(81)
Incentive fee credit		(21)
Credit to base management and incentive fees from Adviser [(B)]	**$ (123)**	$ (102)

(A) Average total assets subject to the base management fee is defined as total assets, including investments made with proceeds of borrowings, less any uninvested cash and cash equivalents resulting from borrowings, valued at the end of the applicable quarters within the respective periods and appropriately adjusted for any share issuances or repurchases during the periods.

(B) Reflected as a line item on our *Condensed Consolidated Statements of Operations*.

Professional expenses increased for the three months ended March 31, 2012, as compared to the period year period, due to an increase in audit and legal expenses.

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Realized and Unrealized Gains (Losses) on Investments

Net Realized (Loss) Gain

For the three months ended March 31, 2012, we recorded a realized gain on investments of $37 primarily due to a realized gain from an unamortized discount on the early payoff of Ernest Health, Inc. (Ernest). There were $5 in net realized gains for the three months ended March 31, 2011, primarily due to realized gains from unamortized discounts on exits during the quarter, partially offset by realized losses in connection with workout expenditures on Sunshine.

Net Unrealized Depreciation

Net unrealized depreciation of investments is the net change in the fair value of our investment portfolio during the reporting period, including the reversal of previously-recorded unrealized appreciation or depreciation when gains and losses are actually realized. During the quarter ended March 31, 2012, we recorded net unrealized depreciation of investments in the aggregate amount of $7.2 million. Over our entire portfolio, the net unrealized depreciation is comprised of approximately $6.6 million on our debt investments and approximately $0.6 million on our equity investments for the three months ended March 31, 2012.

During the prior year period ended March 31, 2011, we recorded net unrealized depreciation of investments in the aggregate amount of $13.1 million. Over our entire portfolio, the net unrealized depreciation consisted of approximately $12.9 million on our debt investments and approximately $0.2 million on our equity investments for the three months ended March 31, 2011.

The realized gains and unrealized appreciation (depreciation) across our investments for the three months ended March 31, 2012 were as follows:

	Three Months Ended March 31, 2012			
Portfolio Company	**Realized Gain**	**Unrealized Appreciation (Depreciation)**	**Reversal of Unrealized Depreciation**	**Net Gain (Loss)**
Legend Communications of Wyoming, LLC	$	$ 320	$ 110	$ 430
North American Aircraft Services, LLC		329		329
RCS Management Holding Co.			306	306
WP Evenflo Group Holdings, Inc.		299		299
International Junior Golf Training Acquisition Company		(408)		(408)
LocalTel, LLC		(428)		(428)
Precision Acquisition Group Holdings, Inc.		(482)		(482)
Viapack, Inc.		(522)		(522)
Lindmark Acquisition, LLC		(556)		(556)
Saunders & Associates		(816)		(816)
Sunburst Media Louisiana, LLC		(900)		(900)
BAS Broadcasting		(1,120)		(1,120)
GFRC Holdings, LLC		(1,157)		(1,157)
Sunshine Media Holdings		(2,379)		(2,379)
Other, net (<$250)	37	193	42	272
Total:	**$ 37**	**$ (7,627)**	**$ 458**	**$ (7,132)**

The largest drivers of our net unrealized depreciation for the three months ended March 31, 2012, were the unrealized depreciation on Sunshine of $2.4 million, GFRC Holdings, LLC of $1.2 million and BAS Broadcasting of $1.1 million, which were all due to a continued decline in these portfolio companies financial and operational performance.

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The realized (losses) gains and net unrealized appreciation (depreciation) across our investments for the three months ended March 31, 2011, were as follows:

	Three Months Ended March 31, 2011			
Portfolio Company	Realized (Loss) Gain	Net Unrealized Appreciation (Depreciation)	Reversal of Unrealized Depreciation (Appreciation)	Net Gain (Loss)
Defiance Integrated Technologies, Inc.	$	$ 1,003	$	$ 1,003
Midwest Metal Distribution, Inc.		364		364
Kansas Cable Holdings, Inc. (formerly known as SCI Cable, Inc.)		(316)		(316)
Reliable Biopharmaceutical Holdings, Inc.		(346)	6	(340)
LocalTel, LLC		(361)		