

PENNANTPARK INVESTMENT CORP  
Form 10-Q  
February 03, 2010  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTER ENDED DECEMBER 31, 2009**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_**

**COMMISSION FILE NUMBER: 814-00736**

**PENNANTPARK INVESTMENT**  
**CORPORATION**

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(Exact name of registrant as specified in its charter)

**MARYLAND**  
(State or other jurisdiction of  
incorporation or organization)

**20-8250744**  
(I.R.S. Employer  
Identification No.)

**590 Madison Avenue, 15<sup>th</sup> Floor**

**New York, N.Y.**  
(Address of principal executive offices)

**10022**  
(Zip Code)

**(212)-905-1000**

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90

days. Yes  No .

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

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

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

The number of shares of the issuer's common stock, \$0.001 par value, outstanding as of February 3, 2010 was 25,808,772.

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**PENNANTPARK INVESTMENT CORPORATION**

**FORM 10-Q**

**FOR THE QUARTER ENDED DECEMBER 31, 2009**

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**PART I FINANCIAL INFORMATION**

We are filing this Report in compliance with Rule 13a-13 promulgated by the SEC. In this Report, PennantPark Investment , we , our and us refer to PennantPark Investment Corporation unless the context otherwise requires.

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

	<b>December 31, 2009</b> <b>(unaudited)</b>	<b>September 30, 2009</b>
<b>Assets</b>		
Investments at fair value		
Non-controlled, non-affiliated investments, at fair value (cost \$499,221,096 and \$479,909,805, respectively)	\$ 497,049,288	\$ 453,644,335
Non-controlled, affiliated investments, at fair value (cost \$17,566,905 and \$17,378,081, respectively)	16,092,038	16,115,738
<b>Total of Investments, at fair value (cost \$516,788,001 and \$497,287,886, respectively)</b>	<b>513,141,326</b>	<b>469,760,073</b>
Cash equivalents	7,051,165	33,247,666
Interest receivable	5,714,129	5,539,056
Receivables for investments sold	45,891	2,726,007
Prepaid expenses and other assets	945,283	1,108,567
<b>Total assets</b>	<b>526,897,794</b>	<b>512,381,369</b>
<b>Liabilities</b>		
Distributions payable	6,452,193	5,056,505
Payable for investments purchased		19,489,525
Unfunded investments	6,455,018	6,331,385
Credit facility payable (cost \$245,700,000 and \$225,100,000, respectively) (See Notes 5 and 10)	201,914,294	175,475,380
Interest payable on credit facility	61,834	72,788
Management fee payable (See Note 3)	2,524,653	2,220,110
Performance-based incentive fee payable (See Note 3)	1,809,453	1,508,164
Accrued other expenses	1,532,027	1,647,244
<b>Total liabilities</b>	<b>220,749,472</b>	<b>211,801,101</b>
<b>Net Assets</b>		
Common stock, par value \$0.001 per share, 100,000,000 shares authorized, 25,808,772 and 25,368,772 shares issued and outstanding, respectively	25,809	25,369
Paid-in capital in excess of par	330,405,864	327,062,304
Undistributed net investment income	2,675,930	1,890,235
Accumulated net realized loss on investments and cash equivalents	(67,098,312)	(50,494,447)
Net unrealized depreciation on investments	(3,646,675)	(27,527,813)
Net unrealized depreciation on credit facility (See Note 5)	43,785,706	49,624,620
<b>Total net assets</b>	<b>\$ 306,148,322</b>	<b>\$ 300,580,268</b>
<b>Total liabilities and net assets</b>	<b>\$ 526,897,794</b>	<b>\$ 512,381,369</b>
<b>Net asset value per share</b>	<b>\$ 11.86</b>	<b>\$ 11.85</b>

SEE NOTES TO FINANCIAL STATEMENTS



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

	<b>Three months ended</b>	
	<b>December 31, 2009</b>	<b>December 31, 2008</b>
<b>Investment income:</b>		
From non-controlled, non-affiliated investments:		
Interest	\$ 12,951,233	\$ 11,712,010
Other	319,603	
From non-controlled, affiliated investments:		
Interest	327,649	364,499
<b>Total investment income</b>	<b>13,598,485</b>	<b>12,076,509</b>
<b>Expenses:</b>		
Base management fee (See Note 3)	2,524,653	1,820,188
Performance-based incentive fee (See Note 3)	1,809,380	1,441,982
Interest and other credit facility expenses	818,683	1,837,220
Administrative services expenses (See Note 3)	557,504	620,402
Other general and administrative expenses	543,415	588,788
<b>Expenses before taxes</b>	<b>6,253,635</b>	<b>6,308,580</b>
Excise tax (See Note 2)	106,962	
<b>Total expenses</b>	<b>6,360,597</b>	<b>6,308,580</b>
<b>Net investment income</b>	<b>7,237,888</b>	<b>5,767,929</b>
<b>Realized and unrealized gain (loss) on investments and credit facility:</b>		
Net realized loss on non-controlled, non-affiliated investments	(16,603,865)	(887,070)
Net change in unrealized appreciation (depreciation) on:		
Non-controlled, non-affiliated investments	24,093,662	(40,663,091)
Non-controlled, affiliated investments	(212,524)	(1,693,186)
Credit facility unrealized (appreciation) depreciation (See Note 5)	(5,838,914)	5,718,694
Net change in unrealized appreciation (depreciation)	18,042,224	(36,637,583)
<b>Net realized and unrealized gain (loss) from investments and credit facility</b>	<b>1,438,359</b>	<b>(37,524,653)</b>
Net increase (decrease) in net assets resulting from operations	\$ 8,676,247	\$ (31,756,724)
Net increase (decrease) in net assets resulting from operations per common share (See Note 8)	\$ 0.34	\$ (1.51)
Net investment income per common share	0.28	0.27

SEE NOTES TO FINANCIAL STATEMENTS

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

	<b>Three months ended</b>	
	<b>December 31, 2009</b>	<b>December 31, 2008</b>
<b>Increase (decrease) in net assets from operations:</b>		
Net investment income	\$ 7,237,888	\$ 5,767,929
Net realized loss on investments	(16,603,865)	(887,070)
Net change in unrealized appreciation (depreciation) on investments	23,881,138	(42,356,277)
Net change in unrealized (appreciation) depreciation on credit facility	(5,838,914)	5,718,694
<b>Net increase (decrease) in net assets resulting from operations</b>	<b>8,676,247</b>	<b>(31,756,724)</b>
<b>Dividends to Stockholders:</b>		
Dividends from net investment income	(6,452,193)	(5,056,505)
<b>Capital Share Transactions:</b>		
Issuance of shares of common stock, net of offering costs	3,344,000	
<b>Total increase (decrease) in net assets</b>	<b>5,568,054</b>	<b>(36,813,229)</b>
<b>Net Assets:</b>		
Beginning of period	300,580,268	210,728,260
Cumulative effect of adoption of fair value option (See Note 5)		41,796,000
Adjusted beginning of period balance	300,580,268	252,524,260
End of period	\$ 306,148,322	\$ 215,711,031
Undistributed net investment income, at period end	2,675,930	108,764
<b>Capital Share Activity:</b>		
Shares issued in connection with public offering	440,000	

SEE NOTES TO FINANCIAL STATEMENTS



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

	<b>Three Months Ended</b>	
	<b>December 31, 2009</b>	<b>December 31, 2008</b>
<b>Cash flows from operating activities:</b>		
Net increase (decrease) in net assets resulting from operations	\$ 8,676,247	\$ (31,756,724)
Adjustments to reconcile net increase (decrease) in net assets resulting from operations to net cash (used for) provided by operating activities:		
Net change in unrealized (appreciation) depreciation on investments	(23,881,138)	42,356,277
Net change in unrealized appreciation (depreciation) on credit facility	5,838,914	(5,718,694)
Net realized loss on investments	16,603,865	887,070
Net accretion of discount and amortization of premium	(1,271,930)	(524,615)
Purchase of investments	(50,481,259)	(803,896)
Payment-in-kind interest	(1,159,733)	(860,532)
Proceeds from dispositions of investments	16,808,942	2,280,140
(Increase) decrease in interest receivable	(175,073)	215,927
Decrease in receivables for investments sold	2,680,116	
Decrease in prepaid expenses and other assets	163,284	130,375
Decrease in payables for investments purchased	(19,489,525)	
Increase in unfunded investments	123,633	278,533
(Decrease) increase in interest payable on credit facility	(10,954)	80,042
Increase in management fee payable	304,543	1,734,292
Increase in performance-based incentive fee payable	301,289	1,318,949
(Decrease) increase in accrued expenses	(115,217)	391,700
Net cash (used for) provided by operating activities	(45,083,996)	10,008,844
<b>Cash flows from financing activities:</b>		
Issuance of shares of common stock, net of offering costs	3,344,000	
Distributions paid to stockholders	(5,056,505)	(5,056,505)
Borrowings under credit facility (See Note 10)	51,300,000	7,500,000
Repayments under credit facility (See Note 10)	(30,700,000)	(52,100,000)
Net cash provided by (used for) financing activities	18,887,495	(49,656,505)
<b>Net decrease in cash and cash equivalents</b>	<b>(26,196,501)</b>	<b>(39,647,661)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>33,247,666</b>	<b>40,249,201</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 7,051,165</b>	<b>\$ 601,540</b>
Supplemental disclosure of cash flow information and non-cash financing activity (See Note 5):		
Interest paid	\$ 762,328	\$ 1,757,177
Cumulative effect of adoption of fair value option on credit facility	\$	\$ 41,796,000

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENTS

DECEMBER 31, 2009

(Unaudited)

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies 162.4%<sup>(1),(2)</sup></b>							
<b>Subordinated Debt/Corporate Notes 56.1%</b>							
Affinion Group Holdings, Inc.	03/01/2012	Consumer Products	8.27% <sup>(6)</sup>	L+750	\$ 23,572,133	\$ 22,993,485	\$ 22,346,382
Aquilex Holdings, LLC <sup>(5)</sup>	12/15/2016	Diversified / Conglomerate Manufacturing	11.13%		10,000,000	9,596,022	9,975,000
Consolidated Foundries, Inc.	04/17/2015	Aerospace and Defense	14.25% <sup>(6)</sup>		8,109,468	7,957,538	8,190,563
CT Technologies Intermediate Holdings, Inc.	03/22/2014	Business Services	14.00% <sup>(6)</sup>		20,413,161	19,995,129	21,025,556
Digicel Limited <sup>(5)</sup>	04/01/2014	Telecommunications	12.00%		1,000,000	995,803	1,110,000
i2 Holdings Ltd.	06/06/2014	Aerospace and Defense	14.75% <sup>(6)</sup>		22,810,883	22,451,159	22,993,370
IDQ Holdings, Inc.	05/20/2012	Auto Sector	13.75%		15,000,000	14,746,483	15,000,000
Learning Care Group, Inc.	12/28/2015	Education	13.50% <sup>(6)</sup>		10,390,942	10,267,437	9,975,304
Realogy Corp.	04/15/2015	Buildings and Real Estate	12.38%		10,000,000	8,955,185	7,775,000
TRAK Acquisition Corp.	12/29/2015	Business Services	15.00% <sup>(6)</sup>		11,500,000	11,126,218	11,470,560
Trizetto Group, Inc.	10/01/2016	Insurance	13.50% <sup>(6)</sup>		20,349,340	20,165,943	20,807,200
UP Acquisitions Sub Inc.	02/08/2015	Oil and Gas	13.50%		21,000,000	20,489,864	21,000,000
<b>Total Subordinated Debt/Corporate Notes</b>						169,740,266	171,668,935
<b>Second Lien Secured Debt 45.5%</b>							
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	6.31%	L+600	13,600,000	13,167,599	12,185,600
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	7.29%	L+700	12,000,000	11,745,828	11,124,000
Generics International (U.S.), Inc.	04/30/2015	Healthcare, Education and Childcare	7.75%	L+750	12,000,000	11,951,224	11,496,000
Greatwide Logistics Services, L.L.C.	03/01/2014	Cargo Transport	11.00% <sup>(6)</sup>	L+700 <sup>(8)</sup>	2,309,343	2,309,344	2,309,343
Mohegan Tribal Gaming Authority <sup>(5)</sup>	11/01/2017	Hotels, Motels, Inns and Gaming	11.50%		5,000,000	4,814,489	5,100,000
QMG Acquisition, LLC, Term Loan A	12/15/2014	Other Media	9.50%	L+650 <sup>(8)</sup>	3,243,646	3,243,646	3,243,646
(formerly Questex Media Group, Inc.)							
QMG Acquisition, LLC, Term Loan B	12/15/2015	Other Media	11.50% <sup>(6)</sup>	L+850 <sup>(8)</sup>	1,629,488	1,629,488	1,629,488
(formerly Questex Media Group, Inc.)							
Realogy Corp.	10/15/2017	Buildings and Real Estate	13.50%		10,000,000	10,000,000	10,566,670
Saint Acquisition Corp. <sup>(5)</sup>	05/15/2015	Transportation	8.02%	L+775	10,000,000	9,943,805	7,512,500
Saint Acquisition Corp. <sup>(5)</sup>	05/15/2017	Transportation	12.50%		19,000,000	16,930,027	15,983,750
Sheridan Holdings, Inc.	06/15/2015	Healthcare, Education and	5.98% <sup>(6)</sup>	L+575	21,500,000	18,938,779	19,694,000

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		Childcare					
Specialized Technology Resources, Inc.	12/15/2014	Chemical, Plastics and Rubber	7.23% <sup>(6)</sup>	L+700	22,500,000	22,488,167	22,500,000
TransFirst Holdings, Inc.	06/15/2015	Financial Services	7.01% <sup>(6)</sup>	L+675	17,094,214	16,569,492	15,675,394

**Total Second Lien Secured Debt** 143,731,888 139,020,391

**Preferred Equity/Partnership Interests<sup>(7)</sup> 3.6%**

AHC Mezzanine (Advanstar Inc.)		Other Media			319	318,896	
CFHC Holdings, Inc., Class A (Consolidated Foundries, Inc.)		Aerospace and Defense	12.00%		797	797,288	978,806
i2 Holdings Ltd.		Aerospace and Defense	12.00%		4,137,240	4,137,240	4,927,099
TZ Holdings, L.P., Series A (Trizetto Group, Inc.)		Insurance			686	685,820	685,820
TZ Holdings, L.P., Series B (Trizetto Group, Inc.)		Insurance	6.50%		1,312	1,312,006	1,410,604
UP Holdings Inc., Class A-1 (UP Acquisitions Sub Inc.)		Oil and Gas	8.00%		91,608	2,499,066	2,879,746

**Total Preferred Equity/Partnership Interests** 9,750,316 10,882,075

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENTS

DECEMBER 31, 2009

(Unaudited)

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Common Equity/Warrants/Partnership Interests <sup>(7)</sup> 4.8%</b>							
CFHC Holdings, Inc. (Consolidated Foundries, Inc.)		Aerospace and Defense			\$ 1,627	\$ 16,271	\$ 245,762
CT Technologies Holdings, LLC (CT Technologies Intermediate Holdings, Inc.)		Business Services			5,556	3,200,000	6,977,888
i2 Holdings Ltd.		Aerospace and Defense			457,322	454,030	1,043,777
QMG HoldCo, LLC, Class A (formerly Questex Media Group, Inc.)		Other Media			4,325	1,306,167	1,306,126
QMG HoldCo, LLC, Class B (formerly Questex Media Group, Inc.)		Other Media			531		160,323
TRAK Acquisition Corp., (warrants)	12/29/2019	Business Services			3,500	29,400	29,400
Transportation 100 Holdco, L.L.C. (Greatwide Logistics Services, L.L.C.)		Cargo Transport			137,923	2,433,112	3,449,041
TZ Holdings, L.P. (Trizetto Group, Inc.)		Insurance			2	6,467	1,242,185
UP Holdings Inc. (UP Acquisitions Sub Inc.)		Oil and Gas			91,608	916	312,765
<b>Total Common Equity/Warrants/Partnership Interests</b>						<b>7,446,363</b>	<b>14,767,267</b>
<b>First Lien Secured Debt 52.2%</b>							
1-800 Contacts, Inc.	03/04/2015	Distribution	7.70%	P+295 <sup>(8)</sup>	13,894,737	11,907,829	13,269,474
Ceva Group PLC <sup>(5)</sup>	10/01/2016	Logistics	11.63%		7,500,000	7,289,802	7,696,875
Chester Downs and Marina, LLC	07/31/2016	Hotels, Motels, Inns and Gaming	12.38%	L+988 <sup>(8)</sup>	10,000,000	9,436,259	10,037,500
Columbus International, Inc. <sup>(5)</sup>	11/20/2014	Communication	11.50%		10,000,000	10,000,000	10,500,000
EnviroSolutions, Inc.	07/07/2012	Environmental Services	11.00% <sup>(6)</sup>	P+775 <sup>(8)</sup>	14,228,928	13,502,355	10,628,954
Fairway Group Acquisition Company	10/01/2014	Grocery	12.00%	L+950	10,000,000	9,701,353	9,800,000
Hanley-Wood, L.L.C.	03/08/2014	Other Media	2.53%	L+225	8,797,500	8,797,500	5,225,715
Headwaters Incorporated <sup>(5)</sup>	11/01/2014	Diversified /Conglomerate	11.38%		3,000,000	2,972,827	3,127,500
		Manufacturing					
Hughes Network Systems, L.L.C.	04/15/2014	Telecommunications	2.81%	L+250	5,000,000	5,000,000	4,587,500
Jacuzzi Brands Corp.	02/07/2014	Home and Office Furnishings, Housewares and Durable Consumer Products	2.53%	L+225	9,799,324	9,799,324	6,712,537
Lyondell Chemical Co.	04/06/2010	Chemicals, Plastics and Rubber	13.00%	L+1,000 <sup>(8)</sup>	12,668,615	13,002,337	13,175,360
Lyondell Chemical Co. <sup>(9)</sup>	04/06/2010	Chemicals, Plastics and Rubber			6,331,385	6,488,872	6,584,640
Mattress Holding Corp.	01/18/2014		2.51%	L+225	3,900,225	3,900,225	2,730,158

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		Home and Office Furnishings, Housewares and Durable Consumer Products					
National Bedding Co., L.L.C.	02/28/2013	Home and Office Furnishings, Housewares and Durable Consumer Products	2.31%	L+200	6,790,000	6,793,783	6,207,194
Penton Media, Inc.	02/01/2013	Other Media	2.53%	L+225	4,862,500	4,862,500	3,215,328
Philosophy, Inc.	03/16/2014	Consumer Products	2.24%	L+200	1,426,506	1,426,506	1,184,000
QMG Acquisition, LLC	04/03/2010	Other Media	10.50%	L+650 <sup>(8)</sup>	277,174	277,174	277,174
(formerly Questex Media Group, Inc.)							
QMG Acquisition, LLC <sup>(9)</sup>	04/03/2010	Other Media			123,634	123,634	123,634
(formerly Questex Media Group, Inc.)							
Rexnord, L.L.C.	07/19/2013	Manufacturing/Basic Industry	2.50%	L+225	2,880,457	2,880,457	2,698,628
Sitel, L.L.C.	01/30/2014	Business Services	5.77%	L+550	2,682,328	2,682,328	2,320,214
Sugarhouse HSP Gaming Prop.	09/23/2014	Hotels, Motels, Inns and Gaming	11.25%	L+825 <sup>(8)</sup>	20,000,000	19,241,573	19,625,000
U.S. Xpress Enterprises, Inc.	10/12/2014	Cargo Transportation	6.50%	L+450 <sup>(8)</sup>	14,915,634	10,407,364	12,230,820
World Color Press Inc.	07/21/2012	Printing	9.00%	P+500 <sup>(8)</sup>	3,493,681	3,196,579	3,502,415
Yonkers Racing Corp. <sup>(5)</sup>	07/15/2016	Hotels, Motels, Inns and Gaming	11.38%		5,000,000	4,861,682	5,250,000
Total First Lien Secured Debt						168,552,263	160,710,620
<b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies</b>						499,221,096	497,049,288

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENTS

DECEMBER 31, 2009

(Unaudited)

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Investments in Non-Controlled, Affiliated Portfolio Companies 5.3%<sup>(1),(2)</sup></b>							
<b>Subordinated Debt/Corporate Notes 1.7%</b>							
Performance Holdings, Inc.	07/02/2014	Leisure, Amusement, Motion Pictures and Entertainment	14.25% <sup>(6)</sup>		\$ 5,258,719	\$ 5,066,905	\$ 5,127,251
<b>Second Lien Secured Debt 2.7%</b>							
Performance, Inc.	07/02/2013	Leisure, Amusement, Motion Pictures and Entertainment	6.04%	L+575	8,750,000	8,750,000	8,115,625
<b>Common Equity/Partnership Interest <sup>(7)</sup></b>							
<b>0.9%</b>							
NCP-Performance (Performance Holdings, Inc.)		Leisure, Amusement, Motion Pictures and Entertainment			37,500	3,750,000	2,849,162
<b>Investments in Non-Controlled, Affiliated Portfolio Companies</b>						17,566,905	16,092,038
<b>Total Investments 167.6%</b>						516,788,001	513,141,326
<b>Cash Equivalents 2.3%</b>					7,051,165	7,051,165	7,051,165
<b>Total Investments and Cash Equivalents 169.9%</b>						\$ 523,839,166	\$ 520,192,491
<b>Liabilities in Excess of Other Assets (69.9%)</b>							(214,044,169)
<b>Net Assets 100.0%</b>							\$ 306,148,322

(1) As used in this Schedule of Investments and in accordance with the 1940 Act, non-controlled means we own less than 25% of a portfolio company's voting securities.

(2) As used in this Schedule of Investments and in accordance with the 1940 Act, non-affiliated means we own less than 5% of a portfolio company's voting securities and affiliated means that we own 5% or more, but less than 25%, of a portfolio company's voting securities.

(3) Valued based on our accounting policy (see Note 2 to our financial statements).

(4) Represents floating rate instruments that accrue interest at a predetermined spread relative to an index, typically the applicable London Interbank Offer Rate (LIBOR or L ) or Prime Rate (Prime or P ).

(5)

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Security is exempt from registration under Rule 144A promulgated under the Securities Act of 1933. The security may be resold in transactions that are exempt from registration, normally to qualified institutional buyers.

- (6) Coupon is payable in cash and/or in-kind ( PIK ).
- (7) Non-income producing securities.
- (8) Coupon is subject to a LIBOR or Prime rate floor.
- (9) Represents the purchase of a security with delayed settlement. This security does not have a basis point spread above an index.

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENT

SEPTEMBER 30, 2009

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Investments in Non-Controlled, Non-Affiliated Portfolio Companies 150.9%<sup>(1),(2)</sup></b>							
<b>Subordinated Debt/Corporate Notes 50.6%</b>							
Affinion Group Holdings, Inc.	03/01/2012	Consumer Products	8.27% <sup>(6)</sup>	L+750	\$ 23,572,133	\$ 22,930,475	\$ 21,497,875
Consolidated Foundries, Inc.	04/17/2015	Aerospace and Defense	14.25% <sup>(6)</sup>		8,109,468	7,952,769	8,190,563
CT Technologies Intermediate Holdings, Inc.	03/22/2014	Business Services	14.00% <sup>(6)</sup>		20,311,603	19,875,880	20,463,940
Digicel Limited <sup>(5)</sup>	04/01/2014	Telecommunications	12.00%		1,000,000	995,610	1,115,000
i2 Holdings Ltd.	06/06/2014	Aerospace and Defense	14.75% <sup>(6)</sup>		22,653,857	22,279,800	22,880,395
IDQ Holdings, Inc.	05/20/2012	Auto Sector	13.75%		20,000,000	19,632,400	20,060,000
Learning Care Group, Inc.	12/28/2015	Education	13.50% <sup>(6)</sup>		10,324,976	10,190,682	10,324,976
Realogy Corp.	04/15/2015	Buildings and Real Estate	12.38%		10,000,000	8,921,187	5,525,000
Trizetto Group, Inc.	10/01/2016	Insurance	13.50% <sup>(6)</sup>		20,197,856	20,010,210	20,652,308
UP Acquisitions Sub Inc.	02/08/2015	Oil and Gas	13.50%		21,000,000	20,472,809	21,420,000
<b>Total Subordinated Debt/Corporate Notes</b>						153,261,822	152,130,057
<b>Second Lien Secured Debt 42.1%</b>							
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	6.36%	L+600	13,600,000	13,153,077	12,416,800
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	7.44%	L+700	12,000,000	11,735,965	11,364,000
Generics International (U.S.), Inc.	04/30/2015	Healthcare, Education and Childcare	7.78%	L+750	12,000,000	11,949,634	11,376,000
Greatwide Logistics Services, L.L.C.	03/01/2014	Cargo Transport	11.00% <sup>(6)</sup>	L+700 <sup>(8)</sup>	2,309,343	2,309,344	2,309,344
Questex Media Group, Inc.	11/04/2014	Other Media	6.91% <sup>(7)</sup>	L+650	10,000,000	10,000,000	
Realogy Corp.	10/15/2017	Buildings and Real Estate	13.50%		10,000,000	10,000,000	10,387,500
Saint Acquisition Corp. <sup>(5)</sup>	05/15/2015	Transportation	8.19%	L+775	10,000,000	9,941,121	7,100,000
Saint Acquisition Corp. <sup>(5)</sup>	05/15/2017	Transportation	12.50%		19,000,000	16,890,972	14,250,000
Sheridan Holdings, Inc.	06/15/2015	Healthcare, Education and Childcare	6.00% <sup>(6)</sup>	L+575	21,500,000	18,855,728	19,414,500
Specialized Technology Resources, Inc.	12/15/2014	Chemical, Plastics and Rubber	7.25% <sup>(6)</sup>	L+700	22,500,000	22,488,166	22,500,000
TransFirst Holdings, Inc.	06/15/2015	Financial Services	7.04% <sup>(6)</sup>	L+675	16,792,105	16,247,489	15,264,023
<b>Total Second Lien Secured Debt</b>						143,571,496	126,382,167
<b>Preferred Equity/Partnership Interests<sup>(7)</sup> 3.6%</b>							
CFHC Holdings, Inc., Class A (Consolidated Foundries, Inc.)		Aerospace and Defense	12.00%		797	797,288	949,648
i2 Holdings Ltd.		Aerospace and Defense	12.00%		4,137,240	4,137,240	4,793,729
TZ Holdings, L.P., Series A (Trizetto Group, Inc.)		Insurance			686	685,820	685,820
TZ Holdings, L.P., Series B (Trizetto Group, Inc.)		Insurance	6.50%		1,312	1,312,006	1,410,604
		Oil and Gas	8.00%		91,608	2,499,067	3,094,252



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UP Holdings Inc., Class A-1 (UP  
Acquisitions Sub Inc.)

VSS-AHC Holdings, LLC (Advanstar  
Inc.)

Other Media

319

318,896

Total Preferred Equity/Partnership  
Interests

9,750,317

10,934,053

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENT

SEPTEMBER 30, 2009

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Common Equity/Warrants/Partnership Interests<sup>(7)</sup> 4.5%</b>							
AHC Mezzanine (Advanstar Inc.)		Other Media			3,000	\$ 3,005,163	\$
CFHC Holdings, Inc. (Consolidated Foundries, Inc.)		Aerospace and Defense			1,627	16,271	215,547
CT Technologies Holdings, LLC (CT Technologies Intermediate Holdings, Inc.)		Business Services			5,556	3,200,000	6,696,281
i2 Holdings Ltd.		Aerospace and Defense			457,322	454,030	1,293,476
Transportation 100 Holdco, L.L.C. (Greatwide Logistics Services, L.L.C)		Cargo Transport			106,299	1,779,455	2,391,463
TZ Holdings, L.P. (Trizetto Group, Inc.)		Insurance			2	6,467	1,337,451
UP Holdings Inc. (UP Acquisitions Sub Inc.)		Oil and Gas			91,608	916	1,656,350
VSS-AHC Holdings, Inc. (Advanstar Inc.) (Warrant)	11/06/2018	Other Media			85		
<b>Total Common Equity/Warrants/Partnership Interests</b>						8,462,302	13,590,568
<b>First Lien Secured Debt 50.1%</b>							
1-800 Contacts, Inc.	03/04/2015	Distribution	7.70%	P+295 <sup>(8)</sup>	13,929,825	11,941,660	13,720,877
Burlington Coat Factory Warehouse Corp.	05/28/2013	Retail Store	2.57%	L+225	2,837,374	2,835,299	2,578,464
Ceva Group PLC <sup>(5)</sup>	10/01/2016	Logistics	11.63%		7,500,000	7,284,525	7,284,525
Chester Downs and Marina, LLC	07/31/2016	Hotels, Motels, Inns and Gaming	12.38%	L+988 <sup>(8)</sup>	10,000,000	9,421,220	10,050,000
EnviroSolutions, Inc.	07/07/2012	Environmental Services	11.00% <sup>(6)</sup>	P+775 <sup>(8)</sup>	14,175,260	13,391,908	12,715,207
Hanley-Wood, L.L.C.	03/08/2014	Other Media	2.49%	L+225	8,842,500	8,842,500	6,225,120
Hughes Network Systems, L.L.C.	04/15/2014	Telecommunications	2.88%	L+250	5,000,000	5,000,000	4,562,500
Jacuzzi Brands Corp.	02/07/2014	Home and Office Furnishings, Housewares and Durable Consumer Products	2.53%	L+225	9,817,568	9,817,568	4,810,608
Levlad, L.L.C.	03/08/2014	Consumer Products	7.75%	L+475	4,434,548	4,434,548	1,064,292
Lyondell Chemical Co.	12/15/2009	Chemicals, Plastics and Rubber	13.00%	L+1,000 <sup>(8)</sup>	12,668,615	12,965,067	13,169,026
Lyondell Chemical Co. <sup>(9)</sup>	12/15/2009	Chemicals, Plastics and Rubber			6,331,385	6,458,897	6,581,474
Mattress Holding Corp.	01/18/2014	Home and Office Furnishings, Housewares and Durable Consumer Products	2.55%	L+225	3,910,200	3,910,200	3,022,585
Mitchell International, Inc.	03/28/2014	Business Services	2.31%	L+200	1,910,204	1,910,204	1,687,346
National Bedding Co., L.L.C.	02/28/2013	Home and Office Furnishings, Housewares and Durable Consumer	2.26%	L+200	6,825,000	6,829,243	6,142,500

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Products							
Penton Media, Inc.	02/01/2013	Other Media	2.73%	L+225	4,875,000	4,875,000	3,568,500
Philosophy, Inc.	03/16/2014	Consumer Products	2.25%	L+200	1,426,506	1,426,506	1,148,337
Questex Media Group, Inc.	05/04/2014	Other Media	5.25% <sup>(7)</sup>	L+200	4,886,667	4,886,667	2,912,600
Rexair, L.L.C.	06/30/2010	Retail	4.50%	L+425	6,695,795	5,507,847	5,189,241
Rexnord, L.L.C.	07/19/2013	Manufacturing/Basic Industry	2.50%	L+200	2,887,881	2,887,881	2,768,756
Site1, L.L.C.	01/30/2014	Business Services	5.95%	L+550	2,682,328	2,682,328	2,226,332
Sugarhouse HSP Gaming Prop.	09/23/2014	Hotels, Motels, Inns and Gaming	11.25%	L+825 <sup>(8)</sup>	20,000,000	19,203,528	19,600,000
U.S. Xpress Enterprises, Inc.	10/12/2014	Cargo Transportation	4.26%	L+400	14,966,254	10,315,732	10,887,950
World Color Press Inc.	07/21/2012	Printing	9.00%	P+500 <sup>(8)</sup>	3,500,000	3,177,842	3,491,250
Yonkers Racing Corp. <sup>(5)</sup>	07/15/2016	Hotels, Motels, Inns and Gaming	11.38%		5,000,000	4,857,698	5,200,000
Total First Lien Secured Debt						164,863,868	150,607,490
Investments in Non-Controlled, Non-Affiliated Portfolio Companies						479,909,805	453,644,335

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## PENNANTPARK INVESTMENT CORPORATION

## SCHEDULE OF INVESTMENT

SEPTEMBER 30, 2009

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index <sup>(4)</sup>	Par / Shares	Cost	Fair Value <sup>(3)</sup>
<b>Investments in Non-Controlled, Affiliated Portfolio Companies 5.4%</b> <sup>(1),(2)</sup>							
<b>Subordinated Debt/Corporate Notes 1.7%</b>							
Performance Holdings, Inc.	07/02/2014	Leisure, Amusement, Motion Pictures and Entertainment	14.25% <sup>(6)</sup>		\$ 5,077,822	\$ 4,878,081	\$ 4,988,960
<b>Second Lien Secured Debt 2.7%</b>							
Performance, Inc.	07/02/2013	Leisure, Amusement, Motion Pictures and Entertainment	6.24%	L+575	8,750,000	8,750,000	8,019,375
<b>Common Equity/Partnership Interest<sup>(7)</sup> 1.0%</b>							
NCP-Performance (Performance Holdings, Inc.)		Leisure, Amusement, Motion Pictures and Entertainment			37,500	3,750,000	3,107,403
<b>Investments in Non-Controlled, Affiliated Portfolio Companies</b>						17,378,081	16,115,738
<b>Total Investments 156.3%</b>						497,287,886	469,760,073
<b>Cash Equivalents 11.1%</b>					33,247,666	33,247,666	33,247,666
<b>Total Investments and Cash Equivalents 167.4%</b>						\$ 530,535,552	\$ 503,007,739
<b>Liabilities in Excess of Other Assets (67.4%)</b>							(202,427,471)
<b>Net Assets 100.0%</b>							\$ 300,580,268

(1) As used in this Schedule of Investments and in accordance with the 1940 Act, non-controlled means we own less than 25% of a portfolio company's voting securities.

(2) As used in this Schedule of Investments and in accordance with the 1940 Act, non-affiliated means we own less than 5% of a portfolio company's voting securities and affiliated means that we own 5% or more, but less than 25%, of a portfolio company's voting securities.

(3) Valued based on our accounting policy (See Note 2 to our financial statements).

(4) Represents floating rate instruments that accrue interest at a predetermined spread relative to an index, typically the applicable London Interbank Offer Rate (LIBOR or L ) or Prime Rate (Prime or P ).

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- (5) Security is exempt from registration under Rule 144A promulgated under the Securities Act of 1933. The security may be resold in transactions that are exempt from registration, normally to qualified institutional buyers.
- (6) Coupon is payable in cash and/or in-kind ( PIK ).
- (7) Non-income producing securities.
- (8) Coupon is subject to a LIBOR or Prime rate floor.
- (9) Represents the purchase of a security with delayed settlement. This security does not have a basis point spread above an index.

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**PENNANTPARK INVESTMENT CORPORATION**

**NOTES TO FINANCIAL STATEMENTS**

**DECEMBER 31, 2009**

**(Unaudited)**

*Except where the context suggests otherwise, the terms we, us, our and PennantPark Investment refer to PennantPark Investment Corporation.*

**1. ORGANIZATION**

PennantPark Investment Corporation was organized as a Maryland corporation on January 11, 2007. PennantPark Investment's objective is to generate both current income and capital appreciation through debt and equity investments. PennantPark Investment invests primarily in U.S. middle-market companies in the form of mezzanine debt, senior secured loans and equity investments. Before the completion of its initial public offering on April 24, 2007, PennantPark Investment had limited operations other than the sale and issuance of 80,000 shares of common stock at a price of \$15.00 per share to PennantPark Investment Advisers, LLC (the Investment Adviser or PennantPark Investment Advisers), resulting in net proceeds of \$1.2 million.

On April 24, 2007 PennantPark Investment closed its initial public offering and sold 20,000,000 shares of common stock at a price of \$15.00 per share, resulting in net proceeds of \$279.6 million. Also, on April 24, 2007 PennantPark Investment closed a private placement to officers, directors, the Investment Adviser and managers of the Investment Adviser, pursuant to Regulation D promulgated under the Securities Act of 1933, and issued an additional 320,000 shares of common stock at a price of \$15.00 per share, resulting in net proceeds of \$4.8 million. On May 21, 2007, the underwriters of the initial public offering exercised their over-allotment option under the Underwriting Agreement and elected to purchase 625,000 shares of common stock at a price of \$15.00 per share, resulting in net proceeds of \$8.8 million.

On September 29, 2009 PennantPark Investment closed a secondary public offering and sold 4,300,000 shares of common stock at a price of \$8.00 per share, resulting in proceeds of \$32.5 million. On October 13, 2009, the underwriters of the secondary offering exercised their over-allotment option under the underwriting agreement and elected to purchase an additional 440,000 shares of common stock at a price of \$8.00 per share resulting in additional net proceeds of \$3.3 million.

**2. SIGNIFICANT ACCOUNTING POLICIES**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles ( GAAP ) requires management to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reported period. Actual results could differ from these estimates. Certain prior period amounts have been reclassified to conform to current period presentation. References to the Accounting Standards Codification, or ASC, serve as a single source of accounting literature and are not intended to change accounting literature.

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

The significant accounting policies consistently followed by PennantPark Investment are:

(a) Investment Valuations

Our board of directors generally uses market quotations to assess the value of our investments for which market quotations are readily available. We obtain these market values from independent pricing services or at the bid prices obtained from at least two broker/dealers if available, otherwise by a principal market maker or a primary market dealer. If the board of directors has a bona fide reason to believe any such market quote does not reflect the fair value of an investment, it may independently value such investments by using the valuation procedure that it uses with respect to assets for which market quotations are not readily available. Subordinated debt, first lien secured debt and other debt investments with maturities greater than 60 days generally are valued by an independent pricing service or at the bid prices from at least two

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broker/dealers (if available, otherwise by a principal market maker or a primary market dealer). Investments, of sufficient credit quality, purchased within 60 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates value. We expect that there will not be readily available market values for most, if not all, of the investments which are or will be in our portfolio, and we value such investments at fair value as determined in good faith by or under the direction of our board of directors using a documented valuation policy, described herein, and a consistently applied valuation process. With respect to investments for which there is no readily available market value, valuation methods include, but are not limited to, comparisons of financial ratios of the portfolio companies that issued such private securities to peer companies that are public. When an external event such as a purchase transaction, public offering or subsequent equity sale occurs, we consider the pricing indicated by the external event to corroborate or revise our valuation. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material. See Note 5 to the financial statements.

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

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

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**PENNANTPARK INVESTMENT CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**DECEMBER 31, 2009**

**(Unaudited)**

The factors that the board of directors may take into account in pricing our investments at fair value include, as relevant, the nature and realizable value of any collateral, the portfolio company's ability to make payments and its earnings and discounted cash flow, the markets in which the portfolio company does business, comparison to publicly traded securities and other relevant factors.

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

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

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

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

**(c) Income Taxes**

Since May 1, 2007, PennantPark Investment has complied with the requirements of Subchapter M of the Internal Revenue Code of 1986, as amended, (the Code) and expects to be subject to tax as a regulated investment company, or RIC. As a RIC, PennantPark Investment accounts for income taxes using the asset liability method prescribed by ASC 740, *Income Taxes*. Under this method, income taxes were provided for amounts currently payable and for amounts deferred as tax assets and liabilities based on differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. Based upon PennantPark Investment's qualification and election to be subject to tax as a RIC, we do not anticipate paying any material level of taxes in the future. Although we are subject to tax as a RIC, we have elected to retain a portion of our calendar year income and record an excise tax of \$0.1 million for the three months ended December 31, 2009. PennantPark Investment recognizes in its financial statements the effect of a tax position when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. We did not have any uncertain tax positions that met the recognition or measurement criteria of ASC 740-10-25 nor did we have any unrecognized tax benefits as of the periods presented herein. Although we file federal and state tax returns, our major tax jurisdiction is federal. Our inception-to-date federal tax years remain subject to examination by the Internal Revenue Service.

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



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

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

(e) New Accounting Pronouncements and Accounting Standards Updates

In April 2009, the FASB issued guidance on, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, or ASC 820-10-35-51A. ASC 820-10-35-51A amends ASC 820 to provide additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased and includes guidance on identifying circumstances that indicate a transaction is not orderly. It emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique used, the objective of a fair value measurement remains the same that the fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. The guidance in ASC 820-10-35-51A is effective for periods ending after June 15, 2009. PennantPark Investment adopted ASC 820-10-35-51A on June 30, 2009, and it did not have a material impact on our financial statements.

In May 2009, FASB issued guidance on, *Subsequent Events*, or ASC 855, which establishes general accounting standards for and disclosure of events that occur after the balance sheet date but before the financial statements are issued. The adoption of ASC 855 did not have a material impact on our financial statements.

In June 2009, FASB issued guidance on, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FASB 162*, or ASC 105-10, *Generally Accepted Accounting Principles*. ASC 105-10 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. On the effective date of ASC 105-10, the Accounting Standards Codification, or ASC, has superseded all then-existing GAAP for non-governmental entities and reporting standards, subject to certain grandfathered literature. The purpose of ASC is not to change accounting literature but rather to serve as a single source of authoritative accounting literature. The adoption of ASC 105-10 did not have a material impact on our financial statements.

In August 2009, the FASB released Accounting Standards Update No. 2009-05 (ASU 2009-05) as an update to ASC 820, *Measuring Liabilities at Fair Value*. ASU 2009-05 provides additional clarity in circumstances where a quoted price in an active market for the identical liability is not available. ASU 2009-05 clarifies that a liability is required to measure fair value by using one or more of the following techniques: (a) The quoted price of the identical liability when traded as an asset; (b) Quoted prices for similar liabilities or similar liabilities when traded as an asset; or (c) Another valuation technique that is consistent with principles of ASC 820. This update also clarifies that when estimating fair value of a liability, a reporting entity is not required to include a separate adjustment to an input relating to the

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)**

existence of a restriction that prevents the transfer of the liability. The update also states that both a quoted price in an active market for a liability at the measurement date and the quoted price for the same liability when traded as an asset in an active market when no adjustments are made to the quoted price are *Level 1* fair value measurements. We adopted ASU 2009-05 on September 30, 2009 and it did not have a material impact on our financial statements. See Note 5 to the financial statements.

**3. AGREEMENTS**

PennantPark Investment has entered into an Investment Management Agreement with the Investment Adviser, which was re-approved by our board of directors, including a majority of our directors who are not interested persons of PennantPark Investment in February 2010. Under this agreement the Investment Adviser, subject to the overall supervision of PennantPark Investment's board of directors, manages the day-to-day operations of and provides investment advisory services to, PennantPark Investment. For providing these services, the Investment Adviser receives a fee from PennantPark Investment, consisting of two components—a base management fee and an incentive fee (collectively, Management Fees).

The base management fee is calculated at an annual rate of 2.00% on PennantPark Investment's gross assets (net of U.S. Treasury Bills and/or temporary draws on the credit facility, average adjusted gross assets, if any, see Note 10). Although the base management fee is 2.00% of our average adjusted gross assets, the Investment Adviser agreed to waive a portion of the base management fee such that the base management fee equaled 1.50% from the consummation of the initial public offering through September 30, 2007 and 1.75% from October 1, 2007 through March 31, 2008. The base management fee has been 2.00% since March 31, 2008 and is payable quarterly in arrears. The base management fee is calculated based on the average value of our average adjusted gross assets at the end of the two most recently completed calendar quarters, and appropriately adjusted for any share issuances or repurchases during the current calendar quarter. For the three months ended December 31, 2009 and 2008, the Investment Adviser earned a base management fee of \$2.5 million and \$1.8 million, respectively, from us.

The incentive fee has two parts, as follows:

One part is calculated and payable quarterly in arrears based on PennantPark Investment's Pre-Incentive Fee Net Investment Income for the immediately preceding calendar quarter. For this purpose, Pre-Incentive Fee Net Investment Income means interest income, distribution income and any other income, including any other fees other than fees for providing managerial assistance, such as commitment, origination, structuring, diligence and consulting fees or other fees received from portfolio companies accrued during the calendar quarter, minus PennantPark Investment's operating expenses for the quarter (including the base management fee, any expenses payable under the Administration Agreement, and any interest expense and distribution paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-Incentive Fee Net Investment Income includes, in the case of investments with deferred interest feature (such as original issue discount, debt instruments with PIK interest and zero coupon securities), accrued income not yet received in cash. Pre-Incentive Fee Net Investment Income does not include any realized capital gains, realized capital losses or unrealized capital appreciation or depreciation. Pre-Incentive Fee Net Investment Income, expressed as a rate of return on the value of PennantPark Investment's net assets at the end of the immediately preceding calendar quarter, is compared to the hurdle rate of 1.75% per quarter (7.00% annualized). PennantPark Investment pays the Investment Adviser an incentive fee with respect to PennantPark Investment's Pre-Incentive Fee Net Investment Income in each calendar quarter as follows: (1) no incentive fee in any calendar quarter in which PennantPark Investment's Pre-Incentive Fee Net Investment Income does not exceed the hurdle rate of 1.75%, (2) 100% of PennantPark Investment's Pre-Incentive Fee Net Investment Income with respect to that portion of such Pre-Incentive Fee Net Investment Income, if any, that exceeds the hurdle rate but is less than 2.1875% in any calendar quarter (8.75% annualized), and (3) 20% of the amount of PennantPark Investment's Pre-Incentive Fee Net Investment Income, if any, that exceeds 2.1875% in any calendar quarter. These calculations are pro rated for any period of less than three months and adjusted for any share issuances or repurchases during the current quarter.

The second part of the incentive fee is determined and payable in arrears as of the end of each calendar year (or upon termination of the Investment Management Agreement, as of the termination date), commencing on December 31, 2007, and equals 20.0% of PennantPark Investment's realized capital gains, if any, on a cumulative basis from inception through the end of each calendar year, computed net of all

realized capital losses and unrealized capital depreciation on a cumulative basis, less the aggregate amount of any previously paid capital gain incentive fees. However, the incentive fee determined as of December 31, 2007 was calculated for a period of shorter than twelve calendar months to take into account any realized capital gains computed net of all realized capital losses and unrealized capital depreciation from inception. For the three months ended December 31, 2009 and 2008, the Investment Adviser earned an incentive fee of \$1.8 million and \$1.4 million, respectively from us.

PennantPark Investment has also entered into an Administration Agreement with PennantPark Investment Administration, LLC (the Administrator or PennantPark Investment Administration ), which was re-approved by our board of directors including a majority of our directors who are not interested persons of PennantPark Investment in February 2010. Under our Administration Agreement, the Administrator performs, or oversees the performance of, our required administrative services, which include, among other things, being responsible for the financial records which we are required to maintain and preparing reports to our stockholders and reports filed with the SEC. In addition, the Administrator assists us in determining and publishing our net asset value, oversees the preparation and filing of our tax returns and the printing and dissemination of reports to our stockholders, and generally oversees the payment of our expenses and the performance of administrative and professional services rendered to us by others. Payments under our Administration Agreement are equal to an amount based upon our allocable portion of the Administrator's overhead in performing its obligations under our Administration Agreement, including rent and our allocable portion of the cost of compensation and related expenses of our Chief Compliance Officer and Chief Financial Officer and their respective staffs. Under our Administration Agreement, the Administrator provides on our behalf managerial assistance to those portfolio companies to which we are required to provide such assistance. To the extent that our Administrator outsources any of its functions, we pay the fees associated with such functions on a direct basis without profit to the Administrator. Reimbursement for certain of these costs is included in administrative services expenses in the statement of operations. For the three months ended December 31, 2009 and 2008, the Investment Adviser was reimbursed \$0.3 million and \$0.3 million, respectively, from us, including expenses it incurred on behalf of the Administrator, for services described above.

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)****4. INVESTMENTS**

Purchases of long-term investments including PIK for the three months ended December 31, 2009 and 2008 totaled \$51.6 million and \$1.7 million, respectively. Sales and repayments of long-term investments for the three months ended December 31, 2009 and 2008 totaled \$16.8 million and \$2.3 million, respectively.

Investments and cash equivalents consisted of the following:

	December 31, 2009		September 30, 2009	
	Cost	Fair Value	Cost	Fair Value
First lien	\$ 168,552,263	\$ 160,710,620	\$ 164,863,868	\$ 150,607,490
Second lien	152,481,888	147,136,016	152,321,496	134,401,542
Subordinated debt / corporate notes	174,807,171	176,796,186	158,139,903	157,119,017
Preferred equity	9,750,316	10,882,075	9,750,317	10,934,053
Common equity	11,196,363	17,616,429	12,212,302	16,697,971
Total Investments	516,788,001	513,141,326	497,287,886	469,760,073
Cash equivalents	7,051,165	7,051,165	33,247,666	33,247,666
Total Investments and cash equivalents	\$ 523,839,166	\$ 520,192,491	\$ 530,535,552	\$ 503,007,739

The table below describes investments by industry classification and enumerates the percentage, by market value, of the total portfolio assets (excluding cash equivalents) in such industries as of December 31, 2009 and September 30, 2009.

Industry Classification	December 31, 2009	September 30, 2009
Business Services	8%	7%
Chemicals, Plastic and Rubber	8	9
Hotels, Motels, Inns and Gaming	8	7
Aerospace and Defense	7	8
Healthcare, Education and Childcare	6	7
Consumer Products	5	5
Energy / Utilities	5	5
Insurance	5	5
Oil and Gas	5	6
Transportation	5	5
Buildings and Real Estate	4	3
Cargo Transport	4	3
Auto Sector	3	4
Distribution	3	3
Diversified / Conglomerate Manufacturing	3	
Financial Services	3	3

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Home and Office Furnishings, Housewares and Durable Consumer Products	3	3
Leisure, Amusement, Motion Picture and Entertainment	3	3
Other Media	3	3
Communication	2	
Education	2	2
Environmental Services	2	3
Logistics	2	2
Other	1	4
<b>Total</b>	<b>100%</b>	<b>100%</b>

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**PENNANTPARK INVESTMENT CORPORATION**

**NOTES TO FINANCIAL STATEMENTS (Continued)**

**DECEMBER 31, 2009**

**(Unaudited)**

**5. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Effective October 1, 2008, we adopted ASC 820, *Fair Value Measurements*, for cash and cash equivalents, investments and long-term credit facility. We realized no gain or loss as a result of the adoption of ASC 820. Fair value, as defined under ASC 820, is the price that we would receive upon selling an investment or pay to transfer a liability in an orderly transaction to a market participant in the principal or most advantageous market for the investment or liability. ASC 820 emphasizes that valuation techniques maximize the use of observable market inputs and minimize the use of unobservable inputs. Inputs refer broadly to the assumptions that market participants would use in pricing an asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on market data obtained from sources independent of PennantPark Investment. Unobservable inputs are inputs that reflect the assumptions market participants would use in pricing an asset or liability developed based on the best information available in the circumstances.

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

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

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

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

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

The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data is available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes accompanied by disclaimer would result in classification as *Level 3* information, assuming no additional corroborating evidence was available.

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

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



**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)**

At December 31, 2009 and September 30, 2009, our cash and cash equivalents, investments and our long-term credit facility were categorized as follows in the fair value hierarchy for ASC 820 purposes:

**At December 31, 2009**

Description	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable inputs (Level 2)	Significant Unobservable inputs (Level 3)
Loan and debt investments	\$ 484,642,822	\$	\$	\$ 484,642,822
Equity investments	28,498,504			28,498,504
<b>Total Investments</b>	<b>513,141,326</b>			<b>513,141,326</b>
Cash Equivalents	7,051,165	7,051,165		
<b>Total Investments and cash equivalents</b>	<b>520,192,491</b>	<b>7,051,165</b>		<b>513,141,326</b>
Long-Term Credit Facility	\$ (201,914,294)	\$	\$	\$ (201,914,294)

**At September 30, 2009**

Description	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable inputs (Level 2)	Significant Unobservable inputs (Level 3)
Loan and debt investments	\$ 442,128,049	\$	\$	\$ 442,128,049
Equity investments	27,632,024			27,632,024
<b>Total Investments</b>	<b>469,760,073</b>			<b>469,760,073</b>
Cash Equivalents	33,247,666	33,247,666		
<b>Total Investments and cash equivalents</b>	<b>503,007,739</b>	<b>33,247,666</b>		<b>469,760,073</b>
Long-Term Credit Facility	\$ (168,475,380)	\$	\$	\$ (168,475,380)

The following tables show a reconciliation of the beginning and ending balances for fair valued investments measured using significant unobservable inputs (*Level 3*) for the three months ended December 31, 2009 and 2008:

**Period Ended December 31, 2009**



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Description	Loan and debt investments	Equity investments	Totals
Beginning Balance, September 30, 2009	\$ 442,128,049	\$ 27,632,024	\$ 469,760,073
Realized gains (losses)	(13,598,702)	(3,005,163)	(16,603,865)
Unrealized appreciation / (depreciation)	21,998,720	1,882,418	23,881,138
Purchases, PIK and net discount accretion	52,229,864	683,058	52,912,922
Sales / repayments	(16,808,942)		(16,808,942)
Non-cash exchanges	(1,306,167)	1,306,167	
Transfers in and /or out of <i>Level 3</i>			
Ending Balance, December 31, 2009	\$ 484,642,822	\$ 28,498,504	\$ 513,141,326

Net change in unrealized appreciation (depreciation) for the year reported within the net change in unrealized appreciation on investments in our Statement of Operations attributable to our <i>Level 3</i> assets still held at the reporting date	\$ 5,856,098	\$ (1,122,745)	\$ 4,733,353
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**Period Ended December 31, 2008**

Description	Loan and debt investments	Equity investments	Totals
Beginning Balance, September 30, 2008	\$ 349,260,104	\$ 22,887,716	\$ 372,147,820
Realized gains (losses)	(887,070)		(887,070)
Unrealized appreciation / (depreciation)	(39,885,419)	(2,470,858)	(42,356,277)
Purchases, PIK and net discount accretion	1,870,146	318,896	2,189,042
Sales / repayments	(2,280,140)		(2,280,140)
Transfers in and /or out of <i>Level 3</i>			
Ending Balance, December 31, 2008	\$ 308,077,621	\$ 20,735,754	\$ 328,813,375

Net change in unrealized depreciation for the year reported within the net change in unrealized depreciation on investments in our Statement of Operations attributable to our <i>Level 3</i> assets still held at the reporting date	\$ (40,255,417)	\$ (2,470,858)	\$ (42,726,275)
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**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)**

The following tables show a reconciliation of the beginning and ending balances for fair valued liabilities measured using significant unobservable inputs (*Level 3*) for the three months ended December 31, 2009 and 2008:

**Period Ended December 31, 2009\***

	<b>Carrying / Fair Value</b>
<b>Long-Term Credit Facility</b>	
Beginning balance, September 30, 2009 (Cost \$218,100,000)	\$ 168,475,380
Total unrealized appreciation included in earnings	5,838,914
Borrowings	47,300,000
Repayments	(19,700,000)
Transfers in and/or out of <i>Level 3</i>	
Ending Balance, December 31, 2009 (Cost \$245,700,000)	\$ 201,914,294

\* There was no temporary draw as of December 31, 2009.

**Period Ended December 31, 2008\***

	<b>Carrying / Fair Value</b>
<b>Long-Term Credit Facility</b>	
Beginning balance, September 30, 2008 (Cost \$162,000,000)	\$ 162,000,000
Cumulative effect of adoption of fair value option	(41,796,000)
Total unrealized appreciation included in earnings	(5,718,694)
Borrowings	4,400,000
Repayments	(9,000,000)
Transfers in and/or out of <i>Level 3</i>	
Ending Balance, December 31, 2008 (Cost \$157,400,000)	\$ 109,885,306

\* There was no temporary draw as of December 31, 2008.

The carrying value of our financial instruments approximates fair value. Effective October 1, 2008, we adopted ASC 825-10, which provides companies with an option to report selected financial assets and liabilities at fair value, and made an irrevocable election to apply ASC 825-10 to our long-term credit facility. PennantPark Investment elected to use the fair value option for the credit facility to align the measurement attributes of both our assets and liabilities while mitigating volatility in earnings from using different measurement attributes. ASC 825-10 establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities and to more easily understand the effect of a company's choice to use fair value on its earnings. ASC 825-10 also requires entities to display the fair value of the selected assets and liabilities on the face of the balance sheet and changes in fair

value of the credit facility are recorded in the statement of operations. We elected not to apply ASC 825-10 to any other financial assets or liabilities. For the three month periods ended December 31, 2009 and 2008, our credit facility had a net change in unrealized (appreciation) depreciation of \$(5.8) million and \$5.7 million, respectively. On December 31, 2009 and September 30, 2009, net unrealized appreciation on our long-term credit facility totaled \$43.8 million and \$49.6 million, respectively, which included the cumulative effect of adoption of ASC 825-10 on our credit facility of \$41.8 million. PennantPark Investment uses a nationally recognized independent valuation service to measure the fair value of its credit facility in a manner consistent with the valuation process that the board of directors uses to value investments.

## **6. CASH EQUIVALENTS**

Cash equivalents represents cash pending investment in longer-term portfolio holdings, PennantPark Investment may invest temporarily in U.S. Treasury Bills (of varying maturities), repurchase agreements, money markets or repo-like treasury securities. These temporary investments with maturities of 90 days or less are deemed cash equivalents and are included in the Schedule of Investments. At the end of each fiscal quarter, PennantPark Investment could take proactive steps to preserve investment flexibility for the next quarter, which is dependent upon the composition of its total assets at quarter end. PennantPark Investment may accomplish this in several ways, including purchasing U.S. Treasury Bills and closing out its positions on a net cash basis after quarter-end, temporarily drawing down on its credit facility, or utilizing repurchase agreements or other balance sheet transactions as are deemed appropriate for this purpose. These amounts are excluded from adjusted gross assets for purposes of computing management fee. U.S. Treasury Bills with maturities greater than 60 days from the time of purchase are marked-to-market consistent with PennantPark Investment's valuation policy.

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)****7. REPURCHASE AGREEMENTS**

PennantPark Investment may enter into repurchase agreements as part of its investment program. In these transactions, PennantPark Investment's custodian takes possession of collateral pledged by the counterparty. The collateral is marked-to-market daily to ensure that the value, plus accrued interest, is at least equal to the repurchase price. In the event of default of the obligor to repurchase, PennantPark Investment will have the right to liquidate the collateral and apply the proceeds in satisfaction of the obligation. Under certain circumstances, in the event of default or bankruptcy by the counterparty to the agreement, realization and/or retention of the collateral or proceeds may be subject to legal proceedings. There were no repurchase agreements outstanding on December 31, 2009 or September 30, 2009.

**8. CHANGE IN NET ASSETS FROM OPERATIONS PER COMMON SHARE**

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

Class and Year	Three months ended	Three months ended
	December 31, 2009	December 31, 2008
Numerator for net increase (decrease) in net assets resulting from operations	\$ 8,676,247	\$ (31,756,724)
Denominator for basic and diluted weighted average shares	25,751,381	21,068,772
Basic and diluted net increase (decrease) in net assets per share resulting from operations	\$ 0.34	\$ (1.51)

**9. FINANCIAL HIGHLIGHTS**

PennantPark Investment's net assets and net asset value per share on December 31, 2009 and 2008 were \$306.1 million and \$215.7 million, respectively, and \$11.86 and \$10.24, respectively. Below are the financial highlights for the three months ended December 31, 2009 and 2008.

	Three months ended December 31, 2009	Three months ended December 31, 2008
<b>Per Share Data:</b>		
Net asset value, beginning of period	\$ 11.85	\$ 10.00
Cumulative effect of adoption of fair value option <sup>(1)</sup>		1.99
Adjusted net asset value, beginning of period	11.85	11.99
Net investment income <sup>(2)</sup>	0.28	0.27
Net change in realized and unrealized gain/(loss) <sup>(2)</sup>	0.06	(1.78)
Net increase (decrease) in net assets resulting from operations <sup>(2)</sup>	0.34	(1.51)
Dividends to stockholders <sup>(3)</sup>	(0.25)	(0.24)
Dilutive effect of common stock issuance below net asset value	(0.08)	

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Net asset value, end of period	\$	11.86	\$	10.24
Per share market value, end of period	\$	8.92	\$	3.61
Total return <sup>*(4)</sup>		12.95%		(48.44)%
Shares outstanding at end of period		25,808,772		21,068,772

**Table of Contents****PENNANTPARK INVESTMENT CORPORATION****NOTES TO FINANCIAL STATEMENTS (Continued)****DECEMBER 31, 2009****(Unaudited)**

	<b>Three months ended December 31, 2009</b>	<b>Three months ended December 31, 2008</b>
<b>Ratios ** / Supplemental Data:</b>		
Ratio of operating expenses to average net assets	7.17%	8.55%
Ratio of credit facility related expenses to average net assets	1.06%	3.51%
Ratio of total expenses to average net assets	8.23%	12.06%
Ratio of net investment income to average net assets	9.37%	11.03%
Net assets at end of period	\$ 306,148,322	\$ 215,711,031
Weighted average debt outstanding	\$ 224,010,870	\$ 164,316,304
Weighted average debt per share	\$ 8.70	\$ 7.80
Portfolio turnover ratio	13.71%	0.48%

\* Not annualized for periods less than one year.

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

- (1) On October 1, 2008, PennantPark Investment adopted ASC 825 and made an irrevocable election to apply the fair value option to our long-term credit facility. Upon our adoption Net Asset Value increased \$41.8 million, or \$1.99 per share, due to the fair value adjustment related to our credit facility.
- (2) Net investment income, net change in realized and unrealized loss and net increase (decrease) in net assets resulting from operations per share data are calculated based on the weighted average shares outstanding for the respective periods.
- (3) Dividends and distributions are determined based on taxable income calculated in accordance with income tax regulations, which may differ from amounts determined under accounting principles generally accepted in the United States of America.
- (4) Total return is based on the change in market price per share during the period and takes into account dividends and distributions, if any, reinvested in accordance with our dividend reinvestment plan.

**10. CREDIT FACILITY**

On June 25, 2007, we entered into a senior secured revolving credit agreement, or our credit facility, among us, various lenders and SunTrust Bank, as administrative agent for the lenders. SunTrust Robinson Humphrey Capital Markets acted as the joint lead arranger and book-runner, and JPMorgan Chase (Chase Lincoln First Commercial successor interest of Bear Stearns Corporate Lending Inc.) acted as joint lead arranger and syndication agent. As of December 31, 2009 and September 30, 2009, there were \$245.7 million and \$225.1 million (including a \$7.0 million temporary draw) in outstanding borrowings under the credit facility, respectively, with a weighted average interest rate at the time of 1.23% and 1.31%, respectively, exclusive of the fee on undrawn commitment of 0.20%.

Under the credit facility, the lenders agreed to extend credit to PennantPark Investment in an initial aggregate principal or face amount not exceeding \$300.0 million at any one time outstanding. The credit facility is a five-year revolving facility (with a stated maturity date of June 25, 2012) and is secured by substantially all of the assets in PennantPark Investment's portfolio. Pricing is set at 100 basis points over LIBOR.

The credit facility contains customary affirmative and negative covenants, including the maintenance of a minimum stockholders' equity, the maintenance of a ratio not less than 200% of total assets (less total liabilities other than indebtedness) to total indebtedness and restrictions on certain payments and issuance of debt. For a complete list of such covenants, see our report on Form 8-K, filed June 28, 2007.

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

**11. COMMITMENTS AND CONTINGENCIES**

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

**12. SUBSEQUENT EVENTS**

PennantPark Investment has evaluated subsequent events and has no material events to report subsequent to the measurement date of these financial statements through the date of issuance on February 3, 2010.

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**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders

PennantPark Investment Corporation

We have reviewed the accompanying statement of assets and liabilities of PennantPark Investment Corporation (the Company), including the schedules of investments, as of December 31, 2009, and the statements of operations, changes in net assets, and cash flows for the three month periods ended December 31, 2009 and 2008. These interim financial statements are the responsibility of the Company's management.

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

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

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the statement of assets and liabilities of PennantPark Investment Corporation, including the schedule of investments, as of September 30, 2009; and in our report dated November 18, 2009, we expressed an unqualified opinion on that financial statement and schedule.

New York, New York  
February 3, 2010



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

This Report, including the Management's Discussion and Analysis of Financial Condition and Results of Operations, contains statements that constitute forward-looking statements, which relate to future events or our future performance or financial condition. These forward-looking statements are not historical facts, but rather are based on current expectations, estimates and projections about our industry, our beliefs and our assumptions. The forward-looking statements contained in this report involve risks and uncertainties, including statements as to:

our future operating results;

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

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

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

the impact of investments that we expect to make;

the impact of fluctuations in interest rates on our business;

our contractual arrangements and relationships with third parties;

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

our expected financings and investments;

the adequacy of our financing arrangements and working capital;

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

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

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

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

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on Form 10-Q and current reports on Form 8-K.

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

### Overview

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

Our investment activities are managed by PennantPark Investment Advisers. Under our Investment Management Agreement, we have agreed to pay our Investment Adviser an annual base management fee based on our average adjusted gross total assets as well as an incentive fee based on our investment performance. We have also entered into an Administration Agreement with PennantPark Investment Administration. Under our Administration Agreement, we have agreed to reimburse the Administrator for our allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under our Administration Agreement, including rent and our allocable portion of the costs of compensation and related expenses of our chief compliance officer, chief financial officer and their respective staffs. Our board of directors, a majority of whom are independent of us and PennantPark Investment Advisers, supervise our activities.

Our investment objectives are to generate both current income and capital appreciation through debt and equity investments primarily in U.S. middle-market private companies in the form of mezzanine debt, senior secured loans and equity investments. We consider our core assets, by value and investment focus, to consist of subordinated debt, second lien secured debt, certain senior secured investments and, to a lesser extent, equity investments. The companies in which we invest are typically highly leveraged, often as a result of leveraged buy-outs or other recapitalization transactions, and, in most cases, are not rated by national rating agencies. If such companies were rated, we believe that they would typically receive ratings below investment grade (between BB and CCC under the Standard & Poor's system) from the national rating agencies.

We expect that our investments in mezzanine debt, senior secured loans and other investments will range between \$10 million and \$50 million each. We expect this investment size to vary proportionately with the size of our capital base.

We are currently operating in a severely constrained credit market. Our investment activity depends on many factors, including the amount of debt and equity capital available to middle-market companies, the level of merger and acquisition activity for such companies, the general economic environment and the competitive environment for the types of investments we make. We have used, and will continue to use, the proceeds of our public offerings of securities and of our credit facility in accordance with our investment objectives. The turmoil in the credit markets is adversely affecting each of these factors and has resulted in broad-based reduction in the demand for, and valuation of, high-risk debt instruments. These conditions may present us with attractive investment opportunities, as we believe that there are many middle-market companies that need senior secured and mezzanine debt financing. However, these market conditions are also adversely affecting our portfolio valuations and increase the risk of default among our portfolio companies, which could negatively impact our performance.

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### **Revenues**

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

### **Expenses**

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

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

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

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

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

transfer agent and custodial fees;

fees and expenses associated with marketing efforts;

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

federal, state and local taxes;

independent directors' fees and expenses;

brokerage commissions;

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

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

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

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

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

### **PORTFOLIO AND INVESTMENT ACTIVITY**

As of December 31, 2009, our portfolio totaled \$513.1 million and consisted of \$176.8 million of subordinated debt, \$147.1 million of second lien secured debt, \$160.7 million of senior secured loans, and \$28.5 million of preferred and common equity investments. Our core assets totaled \$478.2 million and consisted of investments in thirty-five different companies with an average investment size of \$13.7 million per company and a weighted average yield of 12.2% on debt investments. Our non-core senior secured loan portfolio totaled \$34.9 million and consisted of nine different companies with an average investment size of \$3.9 million, and a weighted average yield of 2.7% on debt investments. Our debt portfolio consisted of 61% fixed-rate (including 18% with a LIBOR floor) and 39% in variable-rate investments. Overall, the portfolio had net unrealized depreciation of \$3.6 million as of December 31, 2009. Our overall portfolio consisted of forty-four companies with an average investment size of \$11.7 million and a weighted average yield on debt investments of 11.3%, and was invested 35% in subordinated debt, 29% in second lien secured debt, 31% in senior secured loans and 5% in preferred and common equity investments.

For the three months ended December 31, 2009, we invested \$50.5 million in six new and two existing portfolio companies with a weighted average yield on debt investments of 12.8%. Sales and repayments of long-term investments for the three months ended December 31, 2009 totaled \$16.8 million.

As of September 30, 2009, our portfolio totaled \$469.8 million and consisted of \$157.1 million of subordinated debt, \$134.4 million of second lien secured debt, \$150.6 million of senior secured loans and \$27.7 million of preferred and common equity investments. Our core assets totaled \$427.1 million and consisted of investments in thirty different companies with an average investment size of \$14.2 million per company and a weighted average yield of 12.5% on debt investments. Our non-core senior secured loan portfolio totaled \$42.7 million and consisted of thirteen different companies (including one company also in our core portfolio) with an average investment size of \$3.3 million and a weighted average yield of 3.1%. Our debt portfolio consisted of 53% fixed-rate and 47% variable-rate investments. Overall, the portfolio had an unrealized depreciation of \$27.5 million. Our overall portfolio consisted of forty-two companies with an average investment size of \$11.2 million and a weighted average yield on debt investments of 11.4%, and was invested 33% in subordinated debt, 29% in second lien secured debt, 32% in senior secured loans and 6% in preferred and common equity investments.

For the three months ended December 31, 2008, we invested approximately \$0.8 million in two existing portfolio companies. Sales and repayments of long term investments for the three months ended December 31, 2008 totaled \$2.3 million.

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### **CRITICAL ACCOUNTING POLICIES**

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

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

As a business development company, we generally invest in illiquid securities including debt and equity investments of middle-market companies. All of our investments are recorded using broker/dealers quotes or at fair value as determined in good faith by our board of directors. Our board of directors generally uses market quotations to assess the value of our investments for which market quotations are readily available. We obtain these market values from independent pricing services or at the bid prices obtained from at least two broker/dealers, if available, or by a principal market maker or a primary market dealer. If the board of directors has a bona fide reason to believe any such market quote does not reflect the fair value of an investment, it may independently value such investments by using the valuation procedure that it uses with respect to assets for which market quotations are not readily available. Debt and equity investments that are not publicly traded or whose market prices are not readily available are valued at fair value as determined in good faith by or under the direction of our board of directors. Such determination of fair values involves subjective judgments and estimates. Investments, of sufficient credit quality, purchased within 60 days of maturity are valued at cost plus accreted discount, or minus amortized premium, which approximates value. With respect to unquoted securities, our board of directors, in consultation with Investment Adviser and our independent third party valuation firms, values each investment considering, among other measures, discounted cash flow models, comparisons of financial ratios of peer companies that are public and other factors.

When an external event such as a purchase transaction, public offering or subsequent equity sale occurs in connection with one of our portfolio companies, our board of directors uses the pricing indicated by the external event to corroborate and/or assist us in our valuation of our investment in such portfolio company. Because there are not always readily available markets for most of the investments in our portfolio, we value certain of our portfolio investments at fair value as determined in good faith by our board of directors using a documented valuation policy and a consistently applied valuation process. Due to the inherent uncertainty of determining the fair value of investments that do not have a readily available market value, the fair value of our investments may differ significantly from the values that would have been used had a readily available market value existed for such investments, and the differences could be material.

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

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

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The board of directors discusses these valuations and determines the fair value of each investment in our portfolio in good faith based on the input of our Investment Adviser, the respective independent valuation firms and the audit committee.

In September 2006, the Financial Accounting Standards Board, or FASB, issued guidance related to *Fair Value Measurements*, or ASC 820, which clarifies the definition of fair value and requires companies to expand their disclosure about the use of fair value to measure assets and liabilities in interim and annual periods subsequent to initial recognition. Adoption of ASC 820 requires the use of the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We adopted this statement on October 1, 2008. This adoption did not affect the PennantPark Investment's financial position or its results of operations.

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

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

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

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

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. All of our investments (other than cash and cash equivalents) and long-term credit facility are classified as *Level 3*.

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The inputs into the determination of fair value may require significant management judgment or estimation. Even if observable market data are available, such information may be the result of consensus pricing information or broker quotes which include a disclaimer that the broker would not be held to such a price in an actual transaction. The non-binding nature of consensus pricing and/or quotes accompanied by disclaimer would result in classification as Level 3 information, assuming no additional corroborating evidence.

In February 2007, the FASB issued guidance on, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB 115*, or ASC 825-10. This statement permits an entity to choose to measure many financial instruments and certain other items at fair value. This statement applies to all reporting entities, and contains financial statement presentation and disclosure requirements for assets and liabilities reported at fair value as a consequence of the election. This statement is effective for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We adopted ASC 825-10 on October 1, 2008 and have made an irrevocable election to apply the fair value option to our credit facility liability. The fair value option was elected for our credit facility to align the measurement attributes of both the assets and liabilities while mitigating volatility in earnings from using different measurement attributes. Upon adoption, our Net Asset Value increased by \$41.8 million, or \$1.99 per share, due to the fair value adjustment related to our credit facility. For the three month periods ended December 31, 2009 and 2008, our long-term credit facility had a net change in unrealized (appreciation) depreciation of \$(5.8) million and \$5.7 million, respectively. On December 31, 2009 and September 30, 2009, net unrealized appreciation on our long-term credit facility totaled \$43.8 million and \$49.6 million, respectively, which included the cumulative effect of adoption of ASC 825-10 on our credit facility of \$41.8 million. We have used a nationally recognized independent valuation service to measure the fair value of our credit facility in a manner consistent with the valuation process that our board of directors uses to value our investments. After adoption, subsequent changes in the fair value of our credit facility will be recorded in the Statement of Operations. We have not elected to apply ASC 825-10 to any other financial assets or liabilities.

In April 2009, the FASB issued guidance on, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, or ASC 820-10-35-51A. ASC 820-10-35-51A amends ASC 820 to provide additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased and includes guidance on identifying circumstances that indicate a transaction is not orderly. It emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique used, the objective of a fair value measurement remains the same that the fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. The guidance in ASC 820-10-35-51A is effective for periods ending after June 15, 2009. We adopted ASC 820-10-35-51A on June 30, 2009, and it did not have a material impact on our financial statements.

In August 2009, the FASB released Accounting Standards Update No. 2009-05 (ASU 2009-05) as an update to ASC 820, *Measuring Liabilities at Fair Value*. ASU 2009-05 provides additional clarity in circumstances where a quoted price in an active market for the identical liability is not available. ASU 2009-05 clarifies that a liability is required to measure fair value by using one or more of the following techniques: (a) The quoted price of the identical liability when traded as an asset; (b) Quoted prices for similar liabilities or similar liabilities when traded as an asset; or (c) Another valuation technique that is consistent with principles of ASC 820. This update clarifies that when estimating fair value of a liability, a reporting entity is not required to include a separate adjustment to an input relating to the existence of a restriction that prevents the transfer of the liability. The update also states that both a quoted price in an active market for a liability at the measurement date and the quoted price for the same liability when traded as an asset in an active market when no adjustments are made to the quoted price are *Level 1* fair value measurements. We adopted ASU 2009-05 on September 30, 2009, and it did not have a material impact on our financial statements. See Note 5 to the financial statements.

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

## **Revenue Recognition**

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

the extent that we expect to collect such amounts.

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

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

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

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

#### **Federal Income Taxes**

We operate so as to qualify to maintain our elections to be taxed as a RIC under Subchapter M of the Code and intend to continue to do so. Accordingly, 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 are required to distribute at least 90% of our investment company taxable income as defined by the Code. If we do not distribute at least 98% of our annual taxable income (excluding net long-term capital gains retained or deemed to be distributed) in the year earned, we generally will be required to pay an excise tax on amounts carried over and distributed to shareholders in the next year equal to 4% of the amount by which 98% of our annual taxable income available for distribution exceeds the distributions from such income for the current year.



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

## **RESULTS OF OPERATIONS**

Set forth below are the results of operations for the three months ended December 31, 2009 and 2008.

### **Investment Income**

Investment income for the three month period ended December 31, 2009, was \$13.6 million, and was primarily attributable to \$5.4 million from subordinated debt investments, \$3.2 million from second lien secured debt investments and \$3.5 million from senior secured loan investments. The remaining investment income was primarily attributed to net accretion of discount and amortization of premium and other income. The increase in investment income compared with the same period in the prior year is due to the growth of our portfolio and the transition of the portfolio from temporary to long-term core investments.

Investment income for the three month period ended December 31, 2008, was \$12.1 million, and was primarily attributable to \$2.5 million from subordinated debt investments, \$3.9 million from second lien secured debt investments and \$5.0 million from senior secured loan investments. The remaining investment income was primarily attributed to interest income from short-term investments and to net accretion of discount and amortization of premium.

### **Expenses**

Expenses for the three month period ended December 31, 2009, totaled \$6.4 million. Base management fee for the same period totaled \$2.5 million, performance-based incentive fee totaled \$1.8 million, credit facility related expense totaled \$0.8 million, general and administrative expenses totaled \$1.1 million and an excise tax of \$0.1 million.

Expenses for the three month period ended December 31, 2008, totaled \$6.3 million. Base management fee for the same period totaled \$1.8 million, performance-based incentive fee totaled \$1.4 million, credit facility related expense totaled \$1.8 million and general and administrative expenses totaled \$1.2 million.

### **Net Investment Income**

Net investment income totaled \$7.2 million, or \$0.28 per share, for the three month period ended December 31, 2009, and \$5.8 million, or \$0.27 per share, for the three month period ended December 31, 2008.

### **Net Realized Loss**

Sales and repayments of long-term investments for the three month period ended December 31, 2009 totaled \$16.8 million and realized losses totaled \$16.6 million due to sales of senior secured loans and restructurings on investments offset by repayments on other investments. Sales and repayments of long-term investments totaled \$2.3 million, and net realized losses totaled \$0.9 million for the three month period ended December 31, 2008.

### **Net Unrealized Appreciation (Depreciation) on Investments and (Appreciation) Depreciation Credit Facility**

For the three month periods ended December 31, 2009 and 2008, our investments had a net change in unrealized appreciation (depreciation) of \$23.9 million and \$(42.4) million, respectively. On December 31, 2009 and September 30, 2009, net unrealized depreciation on investments totaled \$3.6 million and \$27.5 million, respectively.

For the three month periods ended December 31, 2009 and 2008, our long-term credit facility had a net change in unrealized (appreciation) depreciation of \$(5.8) million and \$5.7 million, respectively. On December 31, 2009 and September 30, 2009, net unrealized appreciation on our long-term credit facility totaled \$43.8 million and \$49.6 million, respectively, which included the cumulative effect of adoption of ASC 825-10 on our credit facility of \$41.8 million.

### **Net Increase (Decrease) in Net Assets from Operations**

Net increase in net assets resulting from operations totaled \$8.7 million, or \$0.34 per share, for the three month period ended December 31, 2009, primarily due to the overall increase in fair values for investments held in our portfolio offset to some extent by the increase in fair value of our credit facility and realized losses. Net decrease in net assets resulting from operations totaled \$(31.8) million, or \$(1.51) per share, for the three month period ended December 31, 2008.

### **LIQUIDITY AND CAPITAL RESOURCES**

On June 25, 2007, PennantPark Investment entered into a senior secured revolving credit agreement, or our credit facility, among us, various lenders and SunTrust Bank, as administrative agent for the lenders. SunTrust Robinson Humphrey Capital Markets acted as the joint lead arranger and JPMorgan Chase (Chase Lincoln First Commercial, as successor in interest to Bear Stearns Corporate Lending Inc.) acted as joint lead arranger and syndication agent. As of December 31, 2009, PennantPark Investment had outstanding borrowings of \$245.7 million with a fair value of \$201.9 million, with a weighted average interest rate at the time of 1.23% exclusive of the fee on undrawn commitment of 0.20%.

Under the credit facility, the lenders agreed to extend us credit in an initial aggregate principal or face amount not exceeding \$300.0 million at any one time outstanding. The credit facility is a five-year revolving facility (with a stated maturity date of June 25, 2012) and is secured by substantially all of our investment portfolio assets. Pricing of borrowings under our credit facility is set at 100 basis points over LIBOR.

The credit facility contains affirmative and restrictive covenants, including: (a) periodic financial reporting requirements, (b) maintenance of a minimum shareholders' equity of the greater of (i) 40% of the total assets of PennantPark Investment and its subsidiaries as of the last day of any fiscal quarter and (ii) the sum of (A) \$120,000,000 plus (B) 25% of the net proceeds from the sale of equity interests in PennantPark Investment and its subsidiaries after the closing date of the credit facility, (c) maintenance of a ratio of total assets (less total liabilities other than indebtedness) to total indebtedness, in each case of PennantPark Investment, of not less than 2.0:1.0, (d) maintenance of minimum liquidity standards, (e) limitations on the incurrence of additional indebtedness, (f) limitations on liens, (g) limitations on fundamental corporate changes, (h) limitations on investments (other than PennantPark Investment's portfolio investments and certain other ordinary course investments), (i) limitations on payments and distributions (other than distributions to PennantPark Investment's shareholders as contemplated to maintain RIC status), (j) limitations on transactions with affiliates, (k) limitations on engaging in business not contemplated by PennantPark Investment's investment objectives, and (l) limitations on the creation or existence of agreements that prohibit liens on properties of PennantPark Investment and its subsidiaries. In addition to the asset coverage ratio described in clause (c) of the preceding sentence, borrowings under our credit facility (and the incurrence of certain other permitted debt) will be subject to compliance with a borrowing base that will apply different advance rates to different types of assets in PennantPark Investment's portfolio.

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PennantPark Investment has and may continue to raise additional equity or debt capital through a registered offering off a shelf registration or may securitize a portion of its investments among other considerations. In addition, any future additional debt capital we incur, to the extent it is available under stressed credit market conditions, may be issued at a higher cost and on less favorable terms and conditions than our current credit facility. We continuously monitor conditions in the credit markets and seek opportunities to enhance our debt structure considering our credit facility matures in June 2012. Furthermore, our credit facility availability depends on (i) our asset coverage, which generally requires that the valuation of our total assets less liabilities other than indebtedness be at least equal to 200% of our indebtedness, (ii) our maintenance of a blended percentage of the values of our portfolio companies, and (iii) restrictions on certain payments and issuance of debt. The primary use of existing funds and any funds raised in the future is expected to be for repayment of indebtedness, investments in portfolio companies, cash distributions to our shareholders or for other general corporate purposes.

PennantPark Investment's liquidity and capital resources are also generated and available from cash flows from operations, investment sales and repayments, and income earned. On August 25, 2009, our stockholders approved a proposal that authorizes 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 12-month period. On September 29, 2009, we sold shares of our common stock below the then current net asset value per share of common stock. Any decision 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 is subject to the determination by our board of directors that such issuance and sale is in our and our stockholders' best interests. Any sale or other issuance of shares of our common stock at a price below net asset value per share has resulted and will continue to result in an immediate dilution to your interest in our common stock and a reduction of our net asset value per share.

Our operating activities used cash of \$45.1 million for the three months ended December 31, 2009, and our financing activities provided net cash proceeds of \$18.9 million for the same period, primarily from proceeds on issuance of common stock and net borrowings on our credit facility.

Our operating activities generated cash of 10.0 million for the three months ended December 31, 2008, and our financing activities used cash of \$49.7 million for the same period, primarily from net repayments under our credit facility.

**Contractual Obligations**

A summary of our significant contractual payment obligations for the repayment of outstanding borrowing under the multi-currency \$300.0 million, five-year, revolving credit facility maturing in June 2012 is as follows:

	Payments due by period (millions)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Senior secured revolving credit facility <sup>(1)</sup>	\$ 245.7		\$ 245.7		

(1) On December 31, 2009, \$54.3 million remained unused under our senior secured revolving credit facility, subject to maintenance of at least 200% of our total assets less liabilities other than indebtedness to our total outstanding indebtedness, maintenance of a blended percentage of the values of our portfolio companies, and restrictions on certain payments and issuance of debt.

We have entered into certain contracts under which we have material future commitments. Under our Investment Management Agreement, which was renewed in February 2010, PennantPark Investment Advisers serves as our investment adviser in accordance with the terms of that Investment Management Agreement. Payments under our Investment Management Agreement in each reporting period is equal to (1) a management fee equal to a percentage of the value of our gross assets and (2) an incentive fee based on our performance. See Note 3 to the financial statements.

Under our Administration Agreement, which was renewed in February 2010, PennantPark Investment Administration furnishes us with office facilities and administrative services necessary to conduct our day-to-day operations. If requested to provide managerial assistance to our portfolio companies, PennantPark Investment Administration will be paid an additional amount based on the services provided, which amount will not in any case exceed the amount we receive from the portfolio companies for such services. Payment under our Administration Agreement is based upon our allocable portion of the Administrator's overhead in performing its obligations under our Administration Agreement, including rent, technology systems, insurance and our allocable portion of the costs of our chief compliance officer, chief financial officer and their respective staff. See Note 3 to the financial statements.

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

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

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

#### **Distributions**

In order to qualify as a RIC and to not be subject to corporate-level tax on income, we are required, under Subchapter M of the Code, to distribute at least 90% of the sum of our ordinary income and realized net short-term capital gains, if any to our stockholders on an annual basis. Although not required for us to maintain our RIC tax status, we also must distribute at least 98% of our income (both ordinary income and net capital gains) in order to preclude the imposition of an entity level excise tax. For the three months ended December 31, 2009, we have elected to retain a portion of our calendar year income and record an excise tax of \$0.1 million.

During the three months ended December 31, 2009 and 2008, we declared distributions of \$0.25 and \$0.24 per share, respectively, for total distributions of \$6.5 million and \$5.1 million, respectively. We monitor available net investment income to determine if a tax return of capital may occur for the fiscal year. To the extent our taxable earnings fall below the total amount of our distributions for any given fiscal year, a portion of those distributions may be deemed to be a tax return of capital to our common stockholders. Tax characteristics of all distributions will be reported to stockholders on Form 1099-DIV after the end of the calendar year.

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

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

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

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In January 2010, the Internal Revenue Service issued a revenue procedure that temporarily allows a RIC to distribute its own stock as a dividend for the purpose of fulfilling its distribution requirements. Pursuant to this revenue procedure, a RIC may treat a distribution of its own stock as a dividend if (1) the stock is publicly traded on an established securities market, (2) the distribution is declared with respect to a taxable year ending on or before December 31, 2011 and (3) each shareholder may elect to receive his or her entire distribution in either cash or stock of the RIC subject to a limitation on the aggregate amount of cash to be distributed to all shareholders, which must be at least 10% of the aggregate declared distribution. If too many shareholders elect to receive cash, each shareholder electing to receive cash will receive a pro rata amount of cash (with the balance of the distribution paid in stock). In no event will any shareholder electing to receive cash receive less than 10% of his or her entire distribution in cash.

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

## **Recent Developments**

None.

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

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

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

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

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

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

As of the period covered by this report, we, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective in timely alerting management, including the Chief Executive Officer and Chief Financial Officer, of material information about us required to be included in periodic SEC filings. However, in evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. There have been no changes in our internal controls over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.



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**PART II OTHER INFORMATION**

**Item 1. Legal Proceedings**

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

**Item 1A. Risk Factors**

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I Item 1A. Risk Factors in our Annual Report on Form 10-K for the fiscal year ended September 30, 2009, which could materially affect our business, financial condition and/or operating results. The risks described in our Annual Report on Form 10-K are not the only risks facing our PennantPark Investment. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition and/or operating results.

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

None.

**Item 3. Defaults Upon Senior Securities**

None.

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

None.

**Item 5. Other Information**

None.

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**Item 6. Exhibits**

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

- 3.1 Articles of Incorporation (Incorporated by reference to Exhibit 99(a) to the Registrant's Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2/A (File No. 333-140092), filed on April 5, 2007).
- 3.2 Amended and Restated By-Laws of the Registrant (Incorporated by reference to Exhibit 3.2 to the Registrant's Annual Report on Form 10-K (File No. 814-00736), filed on December 13, 2007).
- 4.1 Form of Share Certificate (Incorporated by reference to Exhibit 99(d)(1) to the Registrant's Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
- 11 Computation of Per Share Earnings (included in the notes to the unaudited financial statements contained in this Report).
- 31.1 \* Certification of Chief Executive Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
- 31.2 \* Certification of Chief Financial Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
- 32.1 \* Certification of Chief Executive Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
- 32.2 \* Certification of Chief Financial Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
- 99.1 Privacy Policy of the Registrant (Incorporated by reference to Exhibit 99.1 to the Registrant's Annual Report on Form 10-K (File No. 814-00736), filed on November 18, 2009).

\* Filed herewith.



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**SIGNATURES**

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

PENNANTPARK INVESTMENT CORPORATION

Date: February 3, 2010

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

Date: February 3, 2010

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

**(Principal Accounting and Financial Officer)**