INNOSPEC INC.
Form 10-Q
May 06, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2015

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 1-13879

INNOSPEC INC.

(Exact name of registrant as specified in its charter)

DELAWARE	**98-0181725**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
8310 South Valley Highway	
Suite 350	
Englewood	
Colorado	**80112**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (303) 792 5554

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

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

Large accelerated filer ¨	Accelerated filer x
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 x

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

Class	**Outstanding as of April 30, 2015**
Common Stock, par value $0.01	24,240,306

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CAUTIONARY STATEMENT RELATIVE TO FORWARD-LOOKING STATEMENTS

This Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical facts included or incorporated herein may constitute forward-looking statements. Such forward-looking statements include statements (covered by words like expects, estimates, anticipates, may, believes, feels or similar words or expressions), for example, which relat earnings, growth potential, operating performance, events or developments that we expect or anticipate will or may occur in the future. Although forward-looking statements are believed by management to be reasonable when made, they are subject to certain risks, uncertainties and assumptions, and our actual performance or results may differ materially from these forward-looking statements. Additional information regarding risks, uncertainties and assumptions relating to Innospec and affecting our business operations and prospects are described in Innospec s Annual Report on Form 10-K for the year ended December 31, 2014, and other reports filed with the U.S. Securities and Exchange Commission. You are urged to review our discussion of risks and uncertainties that could cause actual results to differ from forward-looking statements under the heading Risk Factors in such reports. Innospec undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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PART I FINANCIAL INFORMATION

Item 1 Financial Statements

INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(in millions, except share and per share data)	Three Months Ended March 31 2015	2014
Net sales	$ 269.2	$ 220.7
Cost of goods sold	(187.4)	(155.0)
Gross profit	81.8	65.7
Operating expenses:		
Selling, general and administrative	(48.7)	(42.0)
Research and development	(6.2)	(5.7)
Adjustment to fair value of contingent consideration	(3.5)	0.0
Total operating expenses	(58.4)	(47.7)
Operating income	23.4	18.0
Other net income	1.5	1.9
Interest expense, net	(1.0)	(0.9)
Income before income taxes	23.9	19.0
Income taxes	(6.0)	(2.1)
Net income	$ 17.9	$ 16.9
Earnings per share:		
Basic	$ 0.74	$ 0.69
Diluted	$ 0.72	$ 0.69
Weighted average shares outstanding (in thousands):		
Basic	24,301	24,362
Diluted	24,808	24,635

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended March 31	
(in millions)	**2015**	**2014**
Net income	$ 17.9	$ 16.9
Other comprehensive income/(loss):		
Changes in cumulative translation adjustment	(8.0)	(1.2)
Amortization of prior service credit, net of tax of $0.1, and $0.1, respectively	(0.2)	(0.3)
Amortization of actuarial net losses, net of tax of $(0.3), and $(0.3), respectively	1.0	1.1
Total other comprehensive loss	(7.2)	(0.4)
Total comprehensive income	$ 10.7	$ 16.5

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in millions, except share and per share data)	March 31, 2015 (Unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 46.5	$ 41.6
Short-term investments	5.2	4.7
Trade and other accounts receivable (less allowances of $3.7 and $3.9, respectively)	147.7	164.3
Inventories (less allowances of $9.8 and $10.2, respectively):		
Finished goods	114.4	127.0
Work in progress	2.0	1.2
Raw materials	59.6	56.7
Total inventories	176.0	184.9
Current portion of deferred tax assets	8.4	8.4
Prepaid expenses	6.6	8.3
Prepaid income taxes	1.0	2.0
Total current assets	391.4	414.2
Property, plant and equipment:		
Gross cost	185.7	187.0
Less accumulated depreciation	(105.7)	(106.2)
Net property, plant and equipment	80.0	80.8
Goodwill	275.9	276.1
Other intangible assets	178.6	181.1
Deferred finance costs	0.9	1.1
Deferred tax assets, net of current portion	0.7	0.7
Pension asset	48.9	45.2
Other non-current assets	0.4	0.7
Total assets	$ 976.8	$ 999.9

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS - (Continued)

(in millions, except share and per share data)	**March 31, 2015 (Unaudited)**	**December 31, 2014**
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 59.4	$ 87.6
Accrued liabilities	71.9	77.2
Current portion of long-term debt	0.2	0.4
Current portion of finance leases	0.6	0.5
Current portion of plant closure provisions	4.9	5.7
Current portion of accrued income taxes	4.8	5.6
Current portion of acquisition-related contingent consideration	47.3	45.7
Current portion of deferred income	0.2	0.2
Total current liabilities	189.3	222.9
Long-term debt, net of current portion	139.0	139.0
Finance leases, net of current portion	2.3	1.7
Plant closure provisions, net of current portion	29.4	28.4
Unrecognized tax benefits, net of current portion	6.3	6.2
Deferred tax liabilities, net of current portion	25.3	23.0
Pension liability	9.3	10.4
Acquisition-related contingent consideration	51.4	49.5
Deferred income, net of current portion	0.8	0.9
Other non-current liabilities	1.6	2.0
Total liabilities	454.7	484.0
Stockholders equity:		
Common stock, $0.01 par value, authorized 40,000,000 shares, issued 29,554,500 shares	0.3	0.3
Additional paid-in capital	308.9	308.8
Treasury stock (5,291,396 and 5,263,481 shares at cost, respectively)	(83.3)	(78.7)
Retained earnings	409.7	391.8
Accumulated other comprehensive loss	(113.5)	(106.3)
Total stockholders equity	522.1	515.9
Total liabilities and stockholders equity	$ 976.8	$ 999.9

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in millions)	**Three Months Ended March 31 2015**	**Three Months Ended March 31 2014**
Cash Flows from Operating Activities		
Net income	$ 17.9	$ 16.9
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8.5	7.4
Adjustment to fair value of contingent consideration	3.5	0.0
Deferred taxes	1.1	0.4
Excess tax benefit from stock-based payment arrangements	(0.7)	(0.2)
Cash contributions to defined benefit pension plans	(2.7)	(2.9)
Non-cash expense of defined benefit pension plans	0.2	1.0
Stock option compensation	0.9	0.6
Changes in assets and liabilities, net of effects of acquired and divested companies:		
Trade and other accounts receivable	14.1	14.2
Inventories	6.4	(1.1)
Prepaid expenses	1.5	1.5
Accounts payable and accrued liabilities	(33.1)	(21.4)
Accrued income taxes	0.2	8.0
Plant closure provisions	0.5	0.3
Unrecognized tax benefits	0.1	(4.0)
Other non-current assets and liabilities	(0.2)	0.2
Net cash provided by operating activities	18.2	20.9
Cash Flows from Investing Activities		
Capital expenditures	(3.4)	(2.3)
Internally developed software	(2.7)	(1.5)
Purchase of short-term investments	(1.8)	(1.2)
Sale of short-term investments	1.1	2.0
Net cash used in investing activities	(6.8)	(3.0)
Cash Flows from Financing Activities		
Repayments of revolving credit facility	0.0	(8.0)
Repayments of term loans	(0.2)	(0.3)
Excess tax benefit from stock-based payment arrangements	0.7	0.2
Issue of treasury stock	0.7	0.3
Repurchase of common stock	(6.3)	(0.2)
Net cash used in financing activities	(5.1)	(8.0)

Effect of foreign currency exchange rate changes on cash	(1.4)	0.0
Net change in cash and cash equivalents	4.9	9.9
Cash and cash equivalents at beginning of period	41.6	80.2
Cash and cash equivalents at end of period	$ 46.5	$ 90.1

Amortization of deferred finance costs of $0.2 million (2014 $0.2 million) are included in depreciation and amortization in the cash flow statement but in interest expense in the income statement.

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(Unaudited)

(in millions)	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders Equity
Balance at December 31, 2014	$ 0.3	$ 308.8	$ (78.7)	$ 391.8	$ (106.3)	$ 515.9
Net income				17.9		17.9
Changes in cumulative translation adjustment					(8.0)	(8.0)
Treasury stock re-issued		(1.5)	1.7			0.2
Treasury stock repurchased			(6.3)			(6.3)
Excess tax benefit from stock-based payment arrangements		0.7				0.7
Stock option compensation		0.9				0.9
Amortization of prior service credit, net of tax					(0.2)	(0.2)
Amortization of actuarial net losses, net of tax					1.0	1.0
Balance at March 31, 2015	$ 0.3	$ 308.9	$ (83.3)	$ 409.7	$ (113.5)	$ 522.1

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

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INNOSPEC INC. AND SUBSIDIARIES

NOTES TO THE UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X under the Securities Exchange Act of 1934. Accordingly, they do not include all the information and notes necessary for a comprehensive presentation of financial position, results of operations and cash flows.

It is our opinion, however, that all adjustments (consisting of normal, recurring adjustments, unless otherwise disclosed) have been made which are necessary for the financial statements to be fairly stated. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K filed on February 17, 2015.

The results for the interim period covered by this report are not necessarily indicative of the results to be expected for the full year.

We have reclassified certain prior period amounts to conform to the current period presentation.

When we use the terms the Corporation, Company, Registrant, we, us and our, we are referring to Innospec I its consolidated subsidiaries (Innospec) unless otherwise indicated or the context otherwise requires.

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NOTE 2 SEGMENTAL REPORTING

Innospec divides its business into three segments for management and reporting purposes: Fuel Specialties, Performance Chemicals and Octane Additives. The Fuel Specialties and Performance Chemicals segments operate in markets where we actively seek growth opportunities although their ultimate customers are different. As expected, the Octane Additives segment continues to decline as our one remaining customer transitions to unleaded fuel.

The Company evaluates the performance of its segments based on operating income. The following table analyzes sales and other financial information by the Company s reportable segments:

	Three Months Ended March 31	
(in millions)	**2015**	**2014**
Net sales:		
Fuel Specialties	$ 199.4	$ 164.2
Performance Chemicals	57.6	56.1
Octane Additives	12.2	0.4
	$ 269.2	$ 220.7
Gross profit:		
Fuel Specialties	$ 61.5	$ 52.0
Performance Chemicals	14.5	13.6
Octane Additives	5.8	0.1
	$ 81.8	$ 65.7
Operating income:		
Fuel Specialties	$ 23.5	$ 25.8
Performance Chemicals	6.4	6.5
Octane Additives	5.1	(1.2)
Pension charge	0.0	(0.8)
Corporate costs	(8.1)	(12.3)
Fair value of contingent consideration	(3.5)	0.0
Total operating income	$ 23.4	$ 18.0

Restructuring charges separately disclosed in prior periods have been reclassified to corporate costs. We have reclassified the prior period amounts to conform to the current period presentation.

The pension charge relates to the United Kingdom defined benefit pension plan which is closed to future service accrual. The charges related to our other much smaller pension arrangements in the U.S. and overseas are included in the segment and income statement captions consistent with the related employees costs.

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The following table presents a summary of the depreciation and amortization charges incurred by the Company s reportable segments:

(in millions)	Three Months Ended March 31 2015	2014
Depreciation:		
Fuel Specialties	$ 1.9	$ 1.2
Performance Chemicals	0.8	0.9
Octane Additives	0.1	0.1
Corporate	0.4	0.6
	$ 3.2	$ 2.8
Amortization:		
Fuel Specialties	$ 3.2	$ 2.2
Performance Chemicals	1.0	1.3
Corporate	0.9	0.9
	$ 5.1	$ 4.4

NOTE 3 EARNINGS PER SHARE

Basic earnings per share is based on the weighted average number of common shares outstanding during the period. Diluted earnings per share includes the effect of options that are dilutive and outstanding during the period. Per share amounts are computed as follows:

	Three Months Ended March 31 2015	2014
Numerator (in millions):		
Net income available to common stockholders	$ 17.9	$ 16.9
Denominator (in thousands):		
Weighted average common shares outstanding	24,301	24,362
Dilutive effect of stock options and awards	507	273
Denominator for diluted earnings per share	24,808	24,635
Net income per share, basic:	$ 0.74	$ 0.69
Net income per share, diluted:	$ 0.72	$ 0.69

In the three months ended March 31, 2015, the average number of anti-dilutive options excluded from the calculation of diluted earnings per share were 33,734 (three months ended March 31, 2014 - 8,049).

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NOTE 4 GOODWILL

The following table summarizes goodwill at the balance sheet dates:

(in millions)	March 31, 2015	December 31, 2014
Gross cost [1]	$ 512.4	$ 512.6
Accumulated impairment losses	(236.5)	(236.5)
Net book amount	$ 275.9	$ 276.1

[1] Gross cost for 2015 and 2014 is net of $298.5 million of historical accumulated amortization.
The movement in gross cost for the period is due to foreign currency translation.

NOTE 5 OTHER INTANGIBLE ASSETS

The following table summarizes the other intangible assets movement year on year:

(in millions)	Three Months Ended March 31 2015	2014
Gross cost at January 1	$ 247.6	$ 175.5
Capitalization of internally developed software	2.7	1.5
Exchange effect	(0.1)	0.0
Gross cost at March 31	250.2	177.0
Accumulated amortization at January 1	(66.5)	(48.7)
Amortization expense	(5.1)	(4.4)
Exchange effect	0.0	0.1
Accumulated amortization at March 31	(71.6)	(53.0)
Net book amount at March 31	$ 178.6	$ 124.0

Capitalization of internally developed software

We are continuing with the implementation of our new, company-wide, information system platform. At March 31, 2015, we had capitalized $30.5 million (2014 $20.1 million) in relation to this internally developed software.

Amortization expense

	Three Months Ended March 31	
(in millions)	**2015**	**2014**
Product rights	$ (0.9)	$ (1.0)
Brand names	(0.3)	(0.1)
Technology	(0.9)	(0.6)
Customer relationships	(1.7)	(1.3)
Patents	0.0	(0.1)
Non-compete agreements	(0.2)	(0.2)
Marketing related	(0.2)	(0.2)
Internally developed software	(0.9)	(0.9)
Total	$ (5.1)	$ (4.4)

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NOTE 6 PENSION PLANS

The Company maintains a defined benefit pension plan (the Plan) covering a number of its current and former employees in the United Kingdom, although it does also have other much smaller pension arrangements in the U.S. and overseas. The Plan is closed to future service accrual but has a large number of deferred and current pensioners.

(in millions)	Three Months Ended March 31 2015	2014
Plan net pension credit/(charge):		
Service cost	$ (0.4)	$ (0.4)
Interest cost on projected benefit obligation	(7.0)	(8.7)
Expected return on plan assets	8.4	9.3
Amortization of prior service credit	0.3	0.4
Amortization of actuarial net losses	(1.3)	(1.4)
	$ 0.0	$ (0.8)

The amortization of prior service credit and actuarial net losses is a reclassification out of accumulated other comprehensive loss into selling, general and administrative expenses.

The Company also maintains an unfunded defined benefit pension plan covering a number of its current and former employees in Germany (the German plan). The German plan is closed to new entrants and has no assets. The net pension charge for the German plan was $0.2 million in the first quarter of 2015 ($0.2 million - 2014).

NOTE 7 INCOME TAXES

A roll-forward of unrecognized tax benefits and associated accrued interest and penalties is as follows:

(in millions)	Unrecognized Tax Benefits	Interest and Penalties	Total
Opening balance at January 1, 2015	$ 5.7	$ 0.5	$ 6.2
Additions for tax positions of prior periods	0.0	0.1	0.1
Closing balance at March 31, 2015	5.7	0.6	6.3
Current	0.0	0.0	0.0
Non-current	$ 5.7	$ 0.6	$ 6.3

All of the unrecognized tax benefits, interest and penalties, would impact our effective tax rate if recognized.

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We recognize accrued interest and penalties associated with uncertain tax positions as part of income taxes in our consolidated statements of income.

The Company or one of its subsidiaries files income tax returns with the U.S. federal government, and various state and foreign jurisdictions. One of the Company s U.S. subsidiaries received notification in March 2015 of a federal income tax examination by the IRS in respect of 2013. It is currently anticipated that adjustments, if any, arising out of this tax audit would not result in a material change to the Company s financial position as at March 31, 2015.

The Company and its U.S. subsidiaries remain open to examination by the IRS for years 2011 onwards. The Company s subsidiaries in foreign tax jurisdictions are open to examination including France (2013 onwards), Germany (2010 onwards), Switzerland (2013 onwards) and the United Kingdom (2013 onwards).

The Company is in a position to control whether or not to repatriate foreign earnings and we currently do not expect to make a repatriation in the foreseeable future. No taxes have been provided for on the unremitted earnings of our overseas subsidiaries as any tax basis differences relating to investments in these overseas subsidiaries are considered to be permanent in duration. The amount of unremitted earnings at December 31, 2014 was approximately $743 million. If these earnings are remitted, additional taxes could result after offsetting foreign income taxes paid although the calculation of the additional taxes is not practicable to compute at this time.

NOTE 8 LONG-TERM DEBT

Long-term debt consists of the following:

(in millions)	**March 31, 2015**	**December 31, 2014**
Revolving credit facility	$ 139.0	$ 139.0
Other long-term debt	0.2	0.4
	139.2	139.4
Less current portion	(0.2)	(0.4)
	$ 139.0	$ 139.0

NOTE 9 PLANT CLOSURE PROVISIONS

The liability for estimated closure costs of Innospec s manufacturing facilities includes costs for decontamination and environmental remediation activities (remediation). The principal site giving rise to remediation liabilities is the manufacturing site at Ellesmere Port in the United Kingdom. There are also remediation liabilities on a much smaller scale in respect of our other manufacturing sites in the U.S. and Europe.

Movements in the provisions are summarized as follows:

	Three Months Ended March 31

(in millions)	**2015**	**2014**
Total at January 1	$ 34.1	$ 32.4
Charge for the period	1.1	0.7
Utilized in the period	(0.5)	(0.4)
Exchange effect	(0.4)	0.0
Total at March 31	34.3	32.7
Due within one year	(4.9)	(5.4)
Due after one year	$ 29.4	$ 27.3

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Amounts due within one year refer to provisions where expenditure is expected to arise within one year of the balance sheet date.

NOTE 10 FAIR VALUE MEASUREMENTS

The following table presents the carrying amount and fair values of the Company s assets and liabilities measured on a recurring basis:

(in millions)	March 31, 2015 Carrying Amount	March 31, 2015 Fair Value	December 31, 2014 Carrying Amount	December 31, 2014 Fair Value
Assets				
Non-derivatives:				
Cash and cash equivalents	$ 46.5	$ 46.5	$ 41.6	$ 41.6
Short-term investments	5.2	5.2	4.7	4.7
Liabilities				
Non-derivatives:				
Long-term debt (including current portion)	$ 139.2	$ 139.2	$ 139.4	$ 139.4
Finance leases (including current portion)	2.9	2.9	2.2	2.2
Derivatives (Level 1 measurement):				
Other non-current liabilities:				
Foreign currency forward exchange contracts	1.5	1.5	1.8	1.8
Non-financial liabilities (Level 3 measurement):				
Acquisition-related contingent consideration	98.7	98.7	95.2	95.2
Stock equivalent units	5.2	5.2	7.2	7.2

The following methods and assumptions were used to estimate the fair values of financial instruments:

Cash and cash equivalents, and short-term investments: The carrying amount approximates fair value because of the short-term maturities of such instruments.

Long-term debt and finance leases: Long-term debt principally comprises the revolving credit facility, which was entered into in December 2011. Finance leases relate to certain fixed assets in our oilfield specialties business. The carrying amount of long-term debt and finance leases approximates to the fair value.

Derivatives: The fair value of derivatives relating to interest rate swaps, foreign currency forward exchange contracts and commodity swaps are derived from current settlement prices and comparable contracts using current assumptions. Foreign currency forward exchange contracts primarily relate to contracts entered into to hedge future known transactions or hedge balance sheet net cash positions. The movements in the carrying amounts and fair values of these contracts are largely due to changes in exchange rates against the U.S. dollar.

Acquisition-related contingent consideration: Contingent consideration payable in cash is discounted to its fair value. Where contingent consideration is dependent upon pre-determined financial targets, an estimate of the fair value of the likely consideration payable is made on a quarterly basis.

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Stock equivalent units: The fair values of stock equivalent units are calculated at each balance sheet date using either the Black-Scholes or Monte Carlo method.

NOTE 11 DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Company enters into various foreign currency forward exchange contracts to minimize currency exchange rate exposure from expected future cash flows. As at March 31, 2015 the contracts have maturity dates of up to eighteen months at the date of inception. These foreign currency forward exchange contracts have not been designated as hedging instruments, and their impact on the income statement for the first three months of 2015 was a gain of $1.9 million.

NOTE 12 COMMITMENTS AND CONTINGENCIES

Legal matters

While we are involved from time to time in claims and legal proceedings that result from, and are incidental to, the conduct of our business including business and commercial litigation, employee and product liability claims, there are no material pending legal proceedings to which the Company or any of its subsidiaries is a party, or of which any of their property is subject. It is possible, however, that an adverse resolution of an unexpectedly large number of such individual claims or proceedings could in the aggregate have a material adverse effect on the results of operations for a particular year or quarter.

Guarantees

The Company and certain of the Company s consolidated subsidiaries are contingently liable for certain obligations of affiliated companies primarily in the form of guarantees of debt and performance under contracts entered into as a normal business practice. This includes guarantees of non-U.S. excise taxes and customs duties. As at March 31, 2015, such guarantees which are not recognized as liabilities in the consolidated financial statements amounted to $3.7 million.

Under the terms of the guarantee arrangements, generally the Company would be required to perform should the affiliated company fail to fulfil its obligations under the arrangements. In some cases, the guarantee arrangements have recourse provisions that would enable the Company to recover any payments made under the terms of the guarantees from securities held of the guaranteed parties assets.

The Company and its affiliates have numerous long-term sales and purchase commitments in their various business activities, which are expected to be fulfilled with no adverse consequences material to the Company.

NOTE 13 STOCK-BASED COMPENSATION PLANS

The Company grants stock options and stock equivalent units (SEUs) from time to time as a long-term performance incentive. In certain cases the grants are subject to performance conditions such as the Company s stock price. Where performance conditions apply the Monte Carlo simulation model is used to determine the fair values. Otherwise the Black-Scholes model is used to determine the fair values.

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Stock option plans

The following table summarizes the transactions of the Company s stock option plans for the three months ended March 31, 2015:

	Number of Options	Weighted Average Exercise Price	Weighted Average Grant-Date Fair Value
Outstanding at December 31, 2014	728,640	$ 19.55	
Granted - at discount	54,717	$ 0.00	$ 36.18
- at market value	23,550	$ 43.95	$ 9.89
Exercised	(113,920)	$ 6.25	
Forfeited	(3,931)	$ 16.49	
Outstanding at March 31, 2015	689,056	$ 20.96	

At March 31, 2015, there were 115,793 stock options that were exercisable, of which 39,000 had performance conditions attached.

The stock option compensation cost for the first three months of 2015 was $0.9 million (2014 $0.6 million). The total intrinsic value of options exercised in the first three months of 2015 was $2.0 million (2014 $0.5 million).

The total compensation cost related to non-vested stock options not yet recognized at March 31, 2015 was $5.7 million and this cost is expected to be recognized over the weighted-average period of 2.34 years.

Stock equivalent units

The following table summarizes the transactions of the Company s SEUs for the three months ended March 31, 2015:

	Number of SEUs	Weighted Average Exercise Price	Weighted Average Grant-Date Fair Value
Outstanding at December 31, 2014	286,563	$ 3.41	
Granted - at discount	69,280	$ 0.00	$ 36.65
- at market value	6,336	$ 43.95	$ 9.89
Exercised	(81,695)	$ 2.31	
Forfeited	(1,495)	$ 29.56	
Outstanding at March 31, 2015	278,989	$ 3.67	

At March 31, 2015 there were 73,890 SEUs that are exercisable, of which 63,838 had performance conditions attached.

The charges for SEUs are spread over the life of the award subject to a revaluation to fair value each quarter. The revaluation may result in a charge or a credit to the income statement in the quarter dependent upon our share price and other performance criteria.

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The SEU compensation cost for the first three months of 2015 was $1.0 million (2014 - $0.6 million). The total intrinsic value of SEUs exercised in the first three months of 2015 was $1.9 million (2014 $3.0 million).

The weighted-average remaining vesting period of non-vested SEUs is 2.03 years.

Additional exceptional long-term incentive plan

A maximum of $3.0 million of our cash-settled long-term incentives is accounted for as share-based compensation and the fair value is calculated on a quarterly basis using a Monte Carlo model. The fair values at each of the balance sheet dates are summarized as follows:

(in millions)	2015	2014
Balance at January 1	$ 0.1	$ 0.0
Compensation charge for the period	0.1	0.1
Balance at March 31	$ 0.2	$ 0.1

The following assumptions were used in the Monte Carlo model at March 31:

	2015	2014
Dividend yield	1.19%	1.11%
Volatility of Innospec s share price	25.91%	36.04%
Risk free interest rate	0.89%	0.90%

NOTE 14   RECLASSIFICATIONS OUT OF ACCUMULATED OTHER COMPREHENSIVE LOSS

Reclassifications out of accumulated other comprehensive loss for the first three months of 2015 were:

(in millions) Details about AOCL Components	Amount Reclassified from AOCL	Affected Line Item in the Statement where Net Income is Presented
Defined benefit pension plan items:		
Amortization of prior service credit	$ (0.3)	See (1) below
Amortization of actuarial net losses	1.3	See (1) below
	1.0	Total before tax
	(0.2)	Income tax expense
	0.8	Net of tax
Total reclassifications	$ 0.8	Net of tax

(1) These items are included in the computation of net periodic pension cost. See Note 6 of the Notes to the Consolidated Financial Statements for additional information.

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Changes in accumulated other comprehensive loss for the first three months of 2015, net of tax, were:

(in millions)	Defined Benefit Pension Plan Items	Cumulative Translation Adjustments	Total
Balance at December 31, 2014	$ (57.3)	$ (49.0)	$ (106.3)
Other comprehensive income/(loss) before reclassifications	0.0	(8.0)	(8.0)
Amounts reclassified from AOCL	0.8	0.0	0.8
Total other comprehensive income/(loss)	0.8	(8.0)	(7.2)
Balance at March 31, 2015	$ (56.5)	$ (57.0)	$ (113.5)

NOTE 15 RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In April 2015, the FASB issued ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs* (ASU 2015-03), which requires debt issuance costs related to a recognized debt liability to be presented on the balance sheet as a direct deduction from the debt liability, similar to the presentation of debt discounts. The ASU is effective for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The Company is evaluating the effect that ASU 2015-03 will have on its consolidated financial statements and related disclosures.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. ASU 2014-09 is effective for annual periods, and interim periods within those years, beginning after December 15, 2016. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

NOTE 16 RELATED PARTY TRANSACTIONS

Mr. Robert I. Paller has been a non-executive director of the Company since November 1, 2009. The Company has retained and continues to retain Smith, Gambrell & Russell, LLP (SGR), a law firm with which Mr. Paller holds a position. In the first three months of 2015 the Company incurred fees from SGR of $0.2 million (2014 $0.1 million). As at March 31, 2015, the amount due to SGR from the Company was $0.1 million (December 31, 2014 - $0.1 million).

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Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations for the Three Months Ended March 31, 2015

This discussion should be read in conjunction with our unaudited interim consolidated financial statements and the notes thereto.

CRITICAL ACCOUNTING ESTIMATES

The policies and estimates that the Company considers the most critical in terms of complexity and subjectivity of assessment are those related to contingencies, environmental liabilities, pensions, deferred tax and uncertain income tax positions, business combinations, goodwill, property, plant and equipment and other intangible assets (net of amortization). These policies have been discussed in the Company s 2014 Annual Report on Form 10-K.

RESULTS OF OPERATIONS

The following table provides operating income by reporting segment:

	Three Months Ended March 31	
(in millions)	**2015**	**2014**
Net sales:		
Fuel Specialties	$ 199.4	$ 164.2
Performance Chemicals	57.6	56.1
Octane Additives	12.2	0.4
	$ 269.2	$ 220.7
Gross profit:		
Fuel Specialties	$ 61.5	$ 52.0
Performance Chemicals	14.5	13.6
Octane Additives	5.8	0.1
	$ 81.8	$ 65.7
Operating income:		
Fuel Specialties	$ 23.5	$ 25.8
Performance Chemicals	6.4	6.5
Octane Additives	5.1	(1.2)
Pension charge	0.0	(0.8)
Corporate costs	(8.1)	(12.3)
Fair value of contingent consideration	(3.5)	0.0
Total operating income	$ 23.4	$ 18.0

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(in millions, except ratios)	Three Months Ended March 31 2015	2014	Change	
Net sales:				
Fuel Specialties	$ 199.4	$ 164.2	$ 35.2	+21%
Performance Chemicals	57.6	56.1	1.5	+3%
Octane Additives	12.2	0.4	11.8	n/a
	$ 269.2	$ 220.7	$ 48.5	+22%
Gross profit:				
Fuel Specialties	$ 61.5	$ 52.0	$ 9.5	+18%
Performance Chemicals	14.5	13.6	0.9	+7%
Octane Additives	5.8	0.1	5.7	n/a
	$ 81.8	$ 65.7	$ 16.1	+25%
Gross margin (%):				
Fuel Specialties	*30.8*	*31.7*	*-0.9*	
Performance Chemicals	*25.2*	*24.2*	*+1.0*	
Octane Additives	*47.5*	*25.0*	*+22.5*	
Aggregate	*30.4*	*29.8*	*+0.6*	
Operating expenses:				
Fuel Specialties	$ (38.0)	$ (26.2)	$ (11.8)	+45%
Performance Chemicals	(8.1)	(7.1)	(1.0)	+14%
Octane Additives	(0.7)	(1.3)	0.6	n/a
Pension charge	0.0	(0.8)	0.8	-100%
Corporate costs	(8.1)	(12.3)	4.2	-34%
	$ (54.9)	$ (47.7)	$ (7.2)	+15%

Fuel Specialties

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

Change (%)	Three Months Ended March 31, 2015 Americas	EMEA	ASPAC	AvTel	Total
Volume	+7	+2	+27	-53	+4
Acquisitions	+48	0	0	0	+24
Price and product mix	+1	+4	-14	+9	0
Exchange rates	0	-18	-2	0	-7
	+56	-12	+11	-44	+21

Americas saw an increase in volumes as a result of higher demand, while benefiting from a slightly improved price and product mix. Acquisitions in the Americas, relating to Independence Oilfield Chemicals LLC, generated additional sales compared to the prior year. EMEA volumes increased from the prior year together with an improved price and product mix as a result of higher sales of higher margin products. Volumes were higher in ASPAC together with an adverse price and product mix related to one-off cost of goods sold variances. AvTel volumes were lower due to the timing of shipments to customers as opposed to any change in the long-term outlook for that market, while the price and product mix benefited from a

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favorable customer mix. EMEA and ASPAC were adversely impacted by exchange rate movements year over year, driven primarily by a weakening of the European Union euro and the British pound sterling against the U.S. dollar.

Gross margin: the year on year decrease of 0.9 percentage points primarily reflected the lower margins currently achieved from our oilfield specialties businesses.

Operating expenses: the year on year increase of 45%, or $11.8 million, was due to $10.1 million of additional costs for the Independence business; together with a $1.9 million increase in selling expenses related to higher sales volumes in the Americas; and a $0.2 million decrease in other expenses.

Performance Chemicals

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

	Three Months Ended March 31, 2015			
Change (%)	**Americas**	**EMEA**	**ASPAC**	**Total**
Volume	+12	+31	-11	+16
Price and product mix	-1	-9	-6	-5
Exchange rates	-1	-19	-3	-8
	+10	+3	-20	+3

Volumes in the Americas and EMEA were higher, primarily due to increased Personal Care volumes. ASPAC volumes were lower across all our markets. Weaker pricing drove an adverse price and product mix for all our regions. A weakening of the European Union euro and the British pound sterling against the U.S. dollar resulted in an adverse exchange variance for all our regions.

Gross margin: the year on year increase of 1.0 percentage points, primarily driven by a greater proportion of sales from our higher margin Personal Care business.

Operating expenses: the year on year increase of 14%, or $1.0 million, was driven by higher research and development costs, additional headcount to support our Personal Care growth and the phasing of expenditure year over year.

Octane Additives

Net sales: the year on year increase of $11.8 million was primarily due to the timing of shipments with our one remaining customer.

Gross margin: the year on year increase of 22.5 percentage points is primarily a reflection of the higher sales in 2015.

Operating expenses: the year on year decrease of $0.6 million was due to the efficient management of the cost base.

Other Income Statement Captions

Pension charge: is non-cash, and was $0.0 million in 2015 compared to a $0.8 million net charge in 2014, primarily driven by a lower interest cost on the projected benefit obligation.

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Corporate costs: the year on year decrease of 34%, or $4.2 million, related to $3.1 million lower legal, professional and other expenses; $1.4 million lower insurance claims; partly offset by $0.3 million higher personnel-related compensation, primarily due to higher accruals for share-based compensation.

Other net income/(expense): other net income of $1.5 million primarily related to net gains of $1.9 million on foreign currency forward exchange contracts. In 2014, other net income of $1.9 million primarily related to gains of $1.5 million on translation of net assets denominated in non-functional currencies in our European businesses.

Interest expense, net: was $1.0 million in 2015 and $0.9 million in 2014.

Income taxes: the effective tax rate was 25.1% and 11.1% for the first three months of 2015 and 2014, respectively. The adjusted effective tax rate, once adjusted for income tax provisions was 24.7% in 2015 compared with 22.6% in 2014. The 2.1% increase in the adjusted effective tax rate was primarily due to the first quarter of 2015 benefiting to a lesser extent from the positive impact of taxable profits in different geographical locations as compared to the first quarter of 2014. The Company believes that this adjusted effective tax rate, a non-GAAP financial measure, provides useful information to investors and may assist them in evaluating the Company s underlying performance and identifying operating trends. In addition, management uses this non-GAAP financial measure internally to evaluate the performance of the Company s operations and for planning and forecasting in subsequent periods.

	Three Months Ended March 31	
(in millions)	**2015**	**2014**
Income before income taxes	$ 23.9	$ 19.0
Income taxes	$ 6.0	$ 2.1
Adjustment of income tax positions	(0.1)	2.2
	$ 5.9	$ 4.3
GAAP effective tax rate	25.1%	11.1%
Adjusted effective tax rate	24.7%	22.6%

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LIQUIDITY AND FINANCIAL CONDITION

Working Capital

The Company believes that adjusted working capital, a non-GAAP financial measure, (defined by the Company as trade and other accounts receivable, inventories, prepaid expenses, accounts payable and accrued liabilities rather than total current assets less total current liabilities) provides useful information to investors in evaluating the Company s underlying performance and identifying operating trends. Management uses this non-GAAP financial measure internally to allocate resources and evaluate the performance of the Company s operations. Items excluded from the adjusted working capital calculation are listed in the table below and represent factors which do not fluctuate in line with the day to day working capital needs of the business.

(in millions)	March 31, 2015	December 31, 2014
Total current assets	$ 391.4	$ 414.2
Total current liabilities	(189.3)	(222.9)
Working capital	202.1	191.3
Less cash and cash equivalents	(46.5)	(41.6)
Less short-term investments	(5.2)	(4.7)
Less current portion of deferred tax assets	(8.4)	(8.4)
Less prepaid income taxes	(1.0)	(2.0)
Add back current portion of accrued income taxes	4.8	5.6
Add back current portion of long-term debt	0.2	0.4
Add back current portion of finance leases	0.6	0.5
Add back current portion of plant closure provisions	4.9	5.7
Add back current portion of acquisition-related contingent consideration	47.3	45.7
Add back current portion of deferred income	0.2	0.2
Adjusted working capital	$ 199.0	$ 192.7

In 2015 our adjusted working capital increased by $6.3 million, driven primarily by the timing of shipments in our Octane Additives business just prior to the quarter end which led to an increase in trade accounts receivable for that segment.

We had a $16.6 million decrease in trade and other accounts receivable in 2015, which is primarily related to the collection of receivables in our Fuel Specialties segment following high sales in the fourth quarter of 2014, partly offset by higher receivables in our Octane Additives segment. Days sales outstanding in our Fuel Specialties segment decreased from 52 days to 42 days (44 days March 31, 2014) and remained unchanged at 48 days (52 days March 31, 2014) in our Performance Chemicals segment.

We had an $8.9 million decrease in inventories in 2015, which is primarily related to lower inventories in our Fuel Specialties segment following high sales in the fourth quarter of 2014 and lower inventories in our Performance Chemicals segment due to lower production levels and lower cost raw materials. Days sales in inventory in our Fuel Specialties segment increased from 76 days to 80 days (79 days March 31, 2014) and decreased in our Performance

Chemicals segment from 99 days to 80 (83 days March 31, 2014) days.

Prepaid expenses decreased $1.7 million in the first quarter of 2015 ($1.4 million 2014) from $8.3 million to $6.6 million, primarily related to the normal expensing of prepaid costs.

We had a $33.5 million decrease in accounts payable and accrued liabilities in 2015, as our payables unwind following the higher sales in the fourth quarter of 2014, together with payments for personnel-related compensation in the first quarter of 2015. Creditor days in our Fuel Specialties segment decreased from 40 days to 28 days (30 days March 31, 2014) and in our Performance Chemicals segment decreased from 31 days to 27 days (26 days March 31, 2014).

Operating Cash Flows

We generated cash from operating activities of $18.2 million in 2015 compared to $20.9 million in 2014. Year over year cash from operating activities has been adversely impacted by additional working capital requirements, primarily related to the timing of shipments in our Octane Additives segment and significant changes in our income tax cash flows.

Cash

At March 31, 2015 and December 31, 2014 we had cash and cash equivalents of $46.5 million and $41.6 million, respectively, of which $35.2 million and $30.1 million, respectively, were held by non-U.S. subsidiaries principally in the United Kingdom. The Company is in a position to control whether or not to repatriate foreign earnings. We currently do not expect to make a repatriation in the foreseeable future and hence have not provided for future income taxes on the cash held by overseas subsidiaries. If circumstances were to change that would cause these earnings to be repatriated, an additional U.S. tax liability could be incurred, and we continue to monitor this position.

Short-term investments

At March 31, 2015 and December 31, 2014, the Company had short-term investments of $5.2 million and $4.7 million, respectively.

Debt

At March 31, 2015, the Company had $139.0 million of debt outstanding under the revolving credit facility, $0.2 million of debt financing within our Independence business and $2.9 million of obligations under finance leases relating to certain fixed assets within our Independence business.

The Company has a revolving credit facility that provides for borrowing of up to $200.0 million which expires on December 14, 2016 and may be drawn down in full in the U.S..

Item 3 Quantitative and Qualitative Disclosures about Market Risk

The Company uses floating rate debt to finance its global operations. The Company is subject to business risks inherent in non-U.S. activities, including political and economic uncertainty, import and export limitations, and market risk related to changes in interest rates and foreign currency exchange rates. The political and economic risks are mitigated by the stability of the major countries in which the Company s largest operations are located. Credit limits, ongoing credit evaluation and account monitoring procedures are used to minimize bad debt risk. Collateral is not generally required.

From time to time, the Company uses derivatives, including interest rate swaps, commodity swaps and foreign currency forward exchange contracts, in the normal course of business to manage market risks. The derivatives used in hedging activities are considered risk management tools and are not used for

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trading purposes. In addition, the Company enters into derivative instruments with a diversified group of major financial institutions in order to manage the exposure to non-performance of such instruments. The Company s objective in managing the exposure to changes in interest rates is to limit the impact of such changes on earnings and cash flows and to lower overall borrowing costs. The Company s objective in managing the exposure to changes in foreign currency exchange rates is to reduce volatility on earnings and cash flows associated with such changes.

The Company offers fixed prices for some long-term sales contracts. As manufacturing and raw material costs are subject to variability the Company, from time to time, uses commodity swaps to hedge the cost of some raw materials thus reducing volatility on earnings and cash flows. The derivatives are considered risk management tools and are not used for trading purposes. The Company s objective is to manage its exposure to fluctuating costs of raw materials.

The Company s exposure to market risk has been discussed in the Company s 2014 Annual Report on Form 10-K and there have been no significant changes since that time.

Item 4 Controls and Procedures
Evaluation of Disclosure Controls and Procedures

Based on an evaluation carried out as of the end of the period covered by this report, under the supervision and with the participation of our management, our Chief Executive Officer and our Chief Financial Officer concluded that the Company s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934) were effective as of March 31, 2015.

Changes in Internal Control over Financial Reporting

The Company is continuously seeking to improve the efficiency and effectiveness of its operations and of its internal control over financial reporting. This is intended to result in refinements to processes throughout the Company.

Remediation of Existing Material Weaknesses:

The following material weakness that existed as of December 31, 2014 and reported in the Company s 2014 Form 10-K filed on February 17, 2015, was remediated as of March 31, 2015:

Treatment of Intercompany Loans Denominated in Currencies Other Than the Entity s Functional Currency:

The Company previously reported that it lacked effective internal control over financial reporting procedures to ensure the proper application of ASC 830, Foreign Currency Matters, (ASC 830), related to the treatment of foreign currency gains or losses on intercompany loan balances denominated in currencies other than the entity s functional currency. The Company previously reported it did not maintain effective internal control over the calculation of intercompany foreign exchange gains or losses and lacked an effective control to assess and document at inception whether or not intercompany loan balances are long-term in nature. The ineffectiveness of the internal control environment with respect to the treatment of foreign currency gains or losses on intercompany loan balances has not resulted in an adjustment to any financial statements.

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The Company has designed and implemented new internal control over financial reporting procedures to address this material weakness in the quarter. The Company has completed the remediation plan including the following:

- Implemented and evidenced a monthly review of all loan balances to ensure the designation and documentation of certain intercompany loans is correct to ensure the proper application of ASC 830; and

- Implemented additional control procedures to ensure the calculation of foreign exchange gains and losses on intercompany loans included in other comprehensive income is correct.

The Company has tested the operating effectiveness of the internal control over financial reporting steps described above, which are performed on a monthly basis, and concluded that, as of March 31, 2015, this previously reported material weakness has been remediated.

Except as otherwise discussed herein, there were no changes to our internal control over financial reporting, which were identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Securities Exchange Act of 1934, that occurred during the first quarter of 2015 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II OTHER INFORMATION

Item 1 Legal Proceedings

Legal matters

While we are involved from time to time in claims and legal proceedings that result from, and are incidental to, the conduct of our business including business and commercial litigation, employee and product liability claims, there are no material pending legal proceedings to which the Company or any of its subsidiaries is a party, or of which any of their property is subject. It is possible, however, that an adverse resolution of an unexpectedly large number of such individual claims or proceedings could in the aggregate have a material adverse effect on results of operations for a particular year or quarter.

Item 1A Risk Factors

Information regarding risk factors appears in Item 1A of the Company s 2014 Annual Report on Form 10-K and, in management s view, there have been no material changes in the risk factors facing the Company since that time.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds

There were no unregistered sales of equity securities, nor any purchases of equity securities by the issuer in the quarter ended March 31, 2015.

Item 3 Defaults Upon Senior Securities

None.

Item 4 Mine Safety Disclosures

Not applicable.

Item 5 Other Information

None.

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Item 6 Exhibits

31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
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.
101	XBRL Instance Document and Related Items.

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SIGNATURES

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

		INNOSPEC INC. **Registrant**
Date: May 6, 2015	By	/s/ PATRICK S. WILLIAMS **Patrick S. Williams** **President and Chief Executive Officer**
Date: May 6, 2015	By	/s/ IAN P. CLEMINSON **Ian P. Cleminson** **Executive Vice President and Chief Financial Officer**

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September 25, 2007

September 28, 2007 $0.22

June 22, 2007

June 29, 2007 $0.14

Total

$0.36*

* $0.00107 per share is a tax return of capital

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In January 2010, a Form 1099-DIV will be sent to stockholders which, will state the amount and composition of distributions and provide information with respect to appropriate tax treatment of our distributions.

We maintain an opt out dividend reinvestment plan for our common stockholders. As a result, if we declare a dividend or other distribution, then stockholders cash distributions 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 distributions.

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 when applicable to us as a business development company under the 1940 Act and 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 our RIC status. We cannot assure stockholders that they will receive any dividends and distributions or dividends and distributions at a particular level.

Sale of Unregistered Securities

We did not engage in any sales of unregistered securities during the fiscal year ended September 30, 2009.

Stock Performance Graph

This graph compares the return on our common stock with that of the Standard & Poor s 500 Stock Index and the Russell 2000 Financial Services Index, for the period from April 24, 2007 (initial public offering) through September 30, 2009. The graph assumes that, on April 24, 2007, a person invested $100 in each of our common stock, the S&P 500 Index, and the Russell 2000 Financial Services Index. The graph measures total stockholder return, which takes into account both changes in stock price and dividends. It assumes that dividends paid are invested in like securities.

The graph and other information furnished under this Part II Item 5 of this Form 10-K shall not be deemed to be soliciting material or to be filed with the SEC or subject to Regulation 14A or 14C, or to the liabilities of Section 18 of the 1934 Act. The stock price performance included in the above graph is not necessarily indicative of future stock price performance.

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Item 6. Selected Financial Data

The Statement of operations, Per share data and Balance sheet data as of and for the fiscal years ended September 30, 2009, 2008 and as of and for the period from January 11, 2007 (inception) through September 30, 2007 are derived from our financial statements which have been audited by KPMG LLP, our independent registered public accounting firm. This selected financial data should be read in conjunction with our financial statements and related notes thereto and Management s Discussion and Analysis of Financial Condition and Results of Operations and included elsewhere in this Report.

(Dollar amounts in thousands, except per share data)	Year ended September 30, 2009	Year ended September 30, 2008	For the period from January 11, 2007 (inception) through September 30, 2007
Statement of operations data:			
Total investment income	$ 45,119	$ 39,811	$ 13,107
Net expenses before base management fee waiver	22,400	21,676	6,444
Net expenses after base management fee waiver(1)	22,400	21,255	5,803
Net investment income	22,719	18,556	7,304
Net realized and unrealized gain (loss)	13,083	(59,259)	(24,004)
Net increase/(decrease) in net assets resulting from operations	35,802	(40,703)	(16,699)
Per share data:			
Net asset value (at period end)	11.85	10.00	12.83
Net investment income(2)	1.08	0.88	0.35
Net realized and unrealized gain (loss)(2)	0.62	(2.81)	(1.15)
Net increase/(decrease) in net assets resulting from operations(2)	1.70	(1.93)	(0.80)
Distributions declared(2),(6)	(0.96)	(0.90)	(0.36)
Balance sheet data (at period end):			
Total assets	512,381	419,811	555,008
Total investment portfolio	469,760	372,148	291,017
Borrowings outstanding	175,475(5)	202,000	10,000
Payable for investments and unfunded investments	25,821		273,339
Total net asset value	300,580	210,728	270,393
Other data:			
Total return(3)	30.39%	(38.58)%	(8.29)%
Number of portfolio companies (at period end)	42(4)	37(4)	38(4)
Yield on debt portfolio (at period end)	11.4%(4)	11.1%(4)	10.1%(4)

(1) The base management fee waiver was in effect from Inception through March 31, 2008.

(2) Net investment income and net realized and change in unrealized losses per share data are calculated based on the weighted average shares outstanding for the respective periods.

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

(4) Unaudited.

(5) At fair value.

(6) Determined based on taxable income calculated in accordance with income tax regulations which may differ from amounted determined under accounting principles generally accepted in the United States of America.

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Item 7. 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;
- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- the impact of a protracted decline in the liquidity of credit markets on our business;
- the impact of investments that we expect to make;
- the impact of fluctuations in interest rates on our business;
- our contractual arrangements and relationships with third parties;
- the valuation of our investments in portfolio companies, particularly those having no liquid trading market;
- the ability of our prospective portfolio companies to achieve their objectives;
- our expected financings and investments;
- the adequacy of our cash resources and working capital;
- the timing of cash flows, if any, from the operations of our prospective portfolio companies; and
- the ability of the Investment Adviser to locate suitable investments for us and to monitor and administer our investments.

We use words such as anticipates, believes, expects, intends, seeks and similar expressions to identify forward-looking statements. 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, reports on Form 10-Q and current reports on Form 8-K.

The following analysis of our financial condition and results of operations should be read in conjunction with our 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 subordinate 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 a rating 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

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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.

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;

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 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.

As of September 30, 2008, our portfolio totaled $372.1 million and consisted of $166.2 million of subordinated debt, $104.2 million of second lien secured debt, $78.8 million of senior secured loans, and $22.9 million of preferred and common equity investments. Our core assets totaled $305.5 million and consisted of investments in nineteen different companies with an average investment size of $16.1 million per company and a weighted average yield of 12.5% on debt investments. Our non-core senior secured loan portfolio totaled $66.6 million and consisted of nineteen different companies (including one company also in our core portfolio) with an average investment size of $3.5 million, and a weighted average yield of 5.2%. Our debt portfolio consisted of 45% fixed-rate and 55% variable-rate investments. Overall, the portfolio had an unrealized depreciation of $72.0 million. Our overall portfolio consisted of thirty-seven companies with an average investment size of $10.1 million and a weighted average yield on debt investments of 11.1%, and was invested 45% in subordinated debt, 28% in second lien secured debt, 21% in senior secured loans and 6% in preferred and common equity investments.

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For the fiscal year ended September 30, 2009, we purchased $112.7 million of investments in eleven new and six existing portfolio companies with an overall weighted average yield of 14.5% on debt investments. This compares to purchasing $206.8 million in fourteen new and two existing portfolio companies with an overall average yield of 13.8% on debt investments and compares to purchasing $414.0 million in eight new and five existing portfolio companies with an overall average yield of 13.0% on debt investments for the fiscal year ended September 30, 2008 and for the period April 24, 2007 (initial public offering) to September 30, 2007, respectively.

CRITICAL ACCOUNTING POLICIES

The discussion of our financial condition and results of operation is based upon our financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles, or 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 an independent pricing service or at the bid prices, if available, obtained from at least two broker/dealers 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, together with 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 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 are readily available but believed not to reflect the fair value of an investment, our board of directors undertakes a multi-step valuation process each quarter, as described below:

1. Our quarterly valuation process begins with each portfolio company or investment being initially valued by the investment professionals of the Investment Adviser responsible for the portfolio investment;

2. Preliminary valuation conclusions are then documented and discussed with the management of our Investment Adviser;

3. Our board of directors also engages independent valuation firms to conduct independent appraisals of our investments for which market quotations are not readily available or are readily available but deemed not reflective of the fair value of an investment. The independent valuation firm reviews management s preliminary valuations in light of its own independent assessment and also in light of any market quotations obtained from an independent pricing service, broker, dealer or market maker;

4. The audit committee of our board of directors reviews the preliminary valuations of the Investment Adviser and that of the independent valuation firms and responds and supplements the valuation recommendations of the independent valuation firms to reflect any comments; and

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

In September 2006, Financial Accounting Standards Board (the FASB) issued Statements on Financial Accounts Standards (SFAS) 157, *Fair Value Measurements*, 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. With adoption of the Accounting Standards Codification in September of 2009, or ASC and as more fully described in Note 2 of the financial statements, references to authoritative accounting literature now refer to the ASC. Adoption of ASC 820 (formerly known as SFAS 157) 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. The adoption of ASC 820 did not affect our financial position or results of operations.

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 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.

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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*.

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.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB 115*. This statement permits an entity to choose to measure many financial instruments and certain other items at fair value. ASC 825-10 (formerly known as SFAS 159) 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 long-term 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 our 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. 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 have been recorded in the statement of operations. We have not elected to apply ASC825-10 to any other financial assets or liabilities. For the fiscal year ended September 30, 2009, $7.8 million was recorded as a change in unrealized appreciation on the credit facility in the statement of operations. See Note 5 to the financial statements.

In April 2009, the FASB issued FASB Staff Position No. 157-4, 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* (FSP No. 157-4). ASC 820-10-35-51A (formerly known as FSP No. 157-4) made amendments to ASC 820 to provide additional guidance for estimating fair value in accordance with ASC 820 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. See Note 5 to the 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 on the ex-dividend date to the extent that we expect to collect such amounts.

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

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

Payment-in-Kind Interest

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

Federal Income Taxes

We operate so as to qualify to maintain our election to be taxed as a RIC under Subchapter M of the Code and intend to continue to do so. 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.

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.

RESULTS OF OPERATIONS

The overall leveraged finance market has continued to experience pressure which has resulted in depreciation on some of our existing assets and improved risk/reward environment for new investments. We did not experience compromised liquidity during the turmoil in the global credit markets because of our ability to sell our senior secured loans and availability under our credit facility and our ability to access the capital markets to sell common stock.

Set forth below are our results of operations for the fiscal years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) to September 2007.

Investment Income

Investment income for the fiscal year ended September 30, 2009, was $45.1 million, and was primarily attributable to $24.1 million from subordinated debt investments, $12.2 million from second lien secured debt investments, and $6.0 million from senior secured loan investments for the same period. The remaining investment income was primarily attributed to interest income from net accretion of discount and amortization of premium. The increase in investment income from fiscal year 2008 to 2009 was due to the growth in our overall portfolio.

Investment income for the fiscal year ended September 30, 2008, was $39.8 million, and was primarily attributable to $16.2 from senior secured loan investments, $14.7 million from second lien secured debt investments, and $7.2 million from subordinated debt investments for the same period. The remaining investment income was primarily attributed to interest income from short-term investments and to net accretion of discount and amortization of premium. The increase in investment income from fiscal year 2007 to 2008 was due to the growth of our portfolio and the transition of the portfolio from temporary to long-term investments.

Investment income for the period from January 11, 2007 (inception) through September 30, 2007 was $13.1 million and was primarily attributed to senior secured loan investments.

Expenses

Expenses for the fiscal year ended September 30, 2009, totaled $22.4 million. Base management fee for the same period totaled $7.7 million, performance-based incentive fee totaled $5.7 million, credit facility related expense totaled $4.6 million and general and administrative expenses totaled $4.4 million. The increases in expenses from fiscal year 2008 to 2009 were primarily due to the growth of our portfolio and offset by the reduced borrowing costs under our credit facility.

Net expenses for the fiscal year ended September 30, 2008, totaled $21.2 million. Net base management fee for the same period totaled $6.7 million, performance-based incentive fee totaled $3.8 million, credit facility related expense totaled $6.3 million and general and administrative expenses totaled $4.4 million. The increases in expenses from fiscal year 2007 to 2008 were due to the growth of our portfolio and the incurrence of additional borrowing costs under our credit facility.

Net expenses for the period from January 11, 2007 (inception) through September 30, 2007 were $5.8 million. Of these totals, $1.8 million was attributable to credit facility related expenses, and $2.1 million to general and administrative expenses (including approximately $0.3 million non-recurring, primarily legal and corporate tax expenses). Net base management fee for both periods totaled $1.9 million. PennantPark Investment Advisers did not receive a management or incentive fee for its service performed on our behalf prior to completion of our initial public offering on April 24, 2007.

Net Investment Income

Net investment income totaled $22.7 million or $1.08 per share and $18.6 million or $0.88 per share, respectively, for the fiscal years ended September 30, 2009 and 2008, and $7.3 million or $0.35 per share for the period from January 11, 2007 (inception) through September 30, 2007.

Net Realized Loss

Sales and repayments of long-term investments for the fiscal years ended September 30, 2009 and 2008, totaled $28.0 million and $70.1 million, respectively, and net realized losses totaled $39.2 and $11.2 million, respectively. Sales and repayments of long-term investments for the period from January 11, 2007 (inception) through September 30, 2007 totaled $99.6 million and net realized losses totaled approximately $0.1 million.

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Net Unrealized Appreciation (Depreciation) on Investments, Cash Equivalents and Credit Facility

Net unrealized appreciation (depreciation) on investments and cash equivalents totaled $44.5 million, $(48.1) million and $(23.9) million for the fiscal years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007, respectively. Net unrealized appreciation on the credit facility totaled $7.8 million for the fiscal year ended September 30, 2009.

Net Increase/Decrease in Net Assets Resulting From Operations

Net increase in net assets resulting from operations totaled $35.8 million, or $1.70 per share, for the fiscal year ended September 30, 2009, primarily due to the overall increases in market values for investments held in our portfolio and the decrease in the fair value of our credit facility, offset by realized losses. Net decrease in net assets resulting from operations totaled $40.7 million, or $1.93 per share, for the fiscal year ended September 30, 2008, primarily due to the overall decline in market values for investments held in our portfolio. Net decrease in net assets resulting from operations totaled $16.7 million, or $0.80 per share for the period from January 11, 2007 (inception) through September 30, 2007.

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 successor interest of Bear Stearns Corporate Lending Inc.) acted as joint lead arranger and syndication agent. As of September 30, 2009, PennantPark Investment had outstanding borrowings of $225.1 million (including a $7.0 million temporary draw) with a fair value of $175.5 million, with a weighted average interest rate at the time of 1.31% 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.

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, debt capital, 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. 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 $42.4 million for the fiscal year ended September 30, 2009, and our financing activities provided net cash proceeds of $35.4 million for the same period, primarily from both proceeds on a follow-on public offering and net borrowings on our credit facility.

Our operating activities used cash of $390.7 million for the fiscal year ended September 30, 2008, and our financing activities provided cash proceeds of $173.0 million for the same period, primarily from net borrowings under our credit facility.

Our operating activities used cash of $37.9 million for the period from January 11, 2007 (inception) through September 30, 2007 and our financing activities provided cash proceeds of $295.8 million for the same period, primarily from the issuance of our common stock.

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[1]	$ 225.1[2]		$ 225.1		

(1) As of September 30, 2009, PennantPark Investment had $74.9 million of unused borrowing capacity under our credit facility, subject to maintenance of the applicable total assets to debt ratio of 200%, maintenance of a blended percentage of the values of our portfolio companies, and restrictions on certain payments and issuance of debt.

(2) Including a $7.0 million temporary draw.

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We have entered into certain contracts under which we have material future commitments. Under our Investment Management Agreement, which was renewed in February 2009, 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 2009, 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.

During the fiscal years ended September 30, 2009, 2008, and for the period from January 11, 2007 (inception) through September 30, 2007, we paid to stockholders distributions of $0.96, $0.90 and $0.36 per share, respectively, for total distributions of $20.2 million, $19.0 million and $7.6 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.

In January 2009, 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, 2009 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 when applicable to us as a business development company under the 1940 Act and 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

On September 16, 2009, our board of directors approved an issuance of shares of common stock at a price below our current net asset value per share and at a price per share that approximates the market value of our shares traded on the NASDAQ Global Select Market, less an underwriting discount, at the time of sale. Our board of directors unanimously believed that such issuance was in our best interest and in the best interests of our stockholders.

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On September 29, 2009, PennantPark Investment closed its follow-on public offering and sold 4,300,000 shares of common stock at a price of $8.00 per share, resulting in proceeds, net of underwriting fees and expenses, of $32.5 million. On October 13, 2009, the underwriters of our public 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 proceeds, net of underwriting fees, of $3.3 million.

Item 7A. Quantitative And Qualitative Disclosures About Market Risk

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

Assuming that the balance sheet as of September 30, 2009 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 periods covered by this Report, we did not engage in interest rate hedging activities.

Item 8. Financial Statements and Supplementary Data

Management s Report on Internal Control over Financial Reporting

The management of PennantPark Investment Corporation, except where the context suggests otherwise, the terms we, us, our and PennantPark Investment refer to PennantPark Investment Corporation, is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control system is a process designed to provide reasonable assurance to our management and board of directors regarding the preparation and fair presentation of published financial statements.

PennantPark Investment s internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets; provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of management and the directors of PennantPark Investment; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of PennantPark Investment s internal control over financial reporting as of September 30, 2009. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control Integrated Framework*. Based on the assessment management believes that, as of September 30, 2009, our internal control over financial reporting is effective based on those criteria.

PennantPark Investment s independent registered public accounting firm that audited the financial statements has issued an audit report on the effectiveness of our internal control over financial reporting as of September 30, 2009. This report appears on page 43.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

PennantPark Investment Corporation:

We have audited the accompanying statements of assets and liabilities of PennantPark Investment Corporation (the Company) as of September 30, 2009 and 2008, including the schedules of investments, and the related statements of operations, changes in net assets, and cash flows for the years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PennantPark Investment Corporation as of September 30, 2009 and 2008, and the results of its operations and its cash flows for the years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), PennantPark Investment Corporation s internal control over financial reporting as of September 30, 2009, based on criteria established in *Internal Control Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated November 18, 2009 expressed an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

/s/ KPMG LLP

New York, New York

November 18, 2009

Report of Independent Registered Public Accounting Firm

On Internal Control Over Financial Reporting

The Board of Directors and Stockholders

PennantPark Investment Corporation:

We have audited PennantPark Investment Corporation s (the Company) internal control over financial reporting as of September 30, 2009, based on criteria established in *Internal Control Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Management of the Company is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included on page 40 of the Annual Report on Form 10-K, and Item 9A., Controls and Procedures Management s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, PennantPark Investment Corporation maintained, in all material respects, effective internal control over financial reporting as of September 30, 2009, based on criteria established in *Internal Control Integrated Framework,* issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the statements of assets and liabilities of PennantPark Investment Corporation as of September 30, 2009 and 2008, including the schedules of investments, and the related statements of operations, changes in net assets, and cash flows for the years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007, and our report dated November 18, 2009 expressed an unqualified opinion on those financial statements.

/s/ KPMG LLP

New York, New York

November 18, 2009

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PENNANTPARK INVESTMENT CORPORATION

STATEMENTS OF ASSETS AND LIABILITIES

	September 30, 2009	September 30, 2008
Assets		
Investments at fair value		
Non-controlled, non-affiliated investments, at fair value (cost $479,909,805 and $427,481,745, respectively)	$ 453,644,335	$ 354,261,950
Non-controlled, affiliated investments, at fair value (cost $17,378,081 and $16,692,261, respectively)	16,115,738	17,885,870
Total of Investments, at fair value (cost $497,287,886 and $444,174,006, respectively)	469,760,073	372,147,820
Cash equivalents (See Note 8)	33,247,666	40,249,201
Interest receivable	5,539,056	6,046,199
Receivables for investments sold	2,726,007	
Prepaid expenses and other assets	1,108,567	1,367,479
Total assets	512,381,369	419,810,699
Liabilities		
Distributions payable	5,056,505	5,056,505
Payable for investments purchased	19,489,525	
Unfunded investments	6,331,385	
Credit facility payable (fair value: $175,475,380 and $160,204,000, respectively, and cost: $225,100,000 and $202,000,000, respectively), (See Notes 5 and 11)	175,475,380	202,000,000
Interest payable on credit facility	72,788	725,317
Management fees payable (See Note 3)	2,220,110	85,896
Performance-based incentive fee payable (See Note 3)	1,508,164	123,033
Accrued other expenses	1,647,244	1,091,688
Total liabilities	211,801,101	209,082,439
Net Assets		
Common stock, par value $0.001 per share, 100,000,000 shares authorized and 25,368,772 and 21,068,772 shares issued and outstanding, respectively	25,369	21,069
Paid-in capital in excess of par	327,062,304	294,586,604
Undistributed (distributions in excess of) net investment income	1,890,235	(602,660)
Accumulated net realized loss on investments and cash equivalents	(50,494,447)	(11,250,567)
Net unrealized depreciation on investments and cash equivalents	(27,527,813)	(72,026,186)
Cumulative effect of adoption of fair value option on credit facility (See Note 5)	41,796,000	
Net unrealized depreciation on credit facility	7,828,620	
Total net assets	$ 300,580,268	$ 210,728,260
Total liabilities and net assets	$ 512,381,369	$ 419,810,699
Net asset value per share	$ 11.85	$ 10.00

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PENNANTPARK INVESTMENT CORPORATION

STATEMENTS OF OPERATIONS

	Year ended September 30, 2009	Year ended September 30, 2008	Period from January 11, 2007 (inception) through September 30, 2007
Investment income:			
From non-controlled, non-affiliated investments:			
Interest	$ 43,555,240	$ 38,149,813	$ 12,013,028
Dividends			879,537
Other	212,304	255,944	4,995
From non-controlled, affiliated investments:			
Interest	1,351,227	1,405,205	209,781
Total investment income	45,118,771	39,810,962	13,107,341
Expenses:			
Base management fee (See Note 3)	7,715,615	7,136,580	2,565,085
Performance-based incentive fee (See Note 3)	5,683,388	3,791,900	
Interest and other credit facility expenses	4,628,564	6,308,933	1,835,816
Administrative services expenses (See Note 3)	2,319,759	2,301,973	778,587
Other general and administrative expenses	2,052,530	2,136,303	1,158,750
Expenses before base management fee waiver	22,399,856	21,675,689	6,338,238
Base management fee waiver		(420,731)	(641,273)
Income tax expense			105,880
Net expenses	22,399,856	21,254,958	5,802,845
Net investment income	22,718,915	18,556,004	7,304,496
Realized and unrealized gain (loss) on investments, cash equivalents and credit facility:			
Net realized loss on non-controlled, non-affiliated investments and cash equivalents	(39,243,879)	(11,154,735)	(81,769)
Net change in unrealized appreciation (depreciation) on:			
Non-controlled, non-affiliated investments and cash equivalents	46,954,325	(49,052,812)	(24,166,983)
Non-controlled, affiliated investments	(2,455,952)	948,604	245,005
Credit facility (See Note 5)	7,828,620		
Net change in unrealized appreciation (depreciation)	52,326,993	(48,104,208)	(23,921,978)
Net realized and unrealized gain (loss) from investments, cash equivalents and credit facility	13,083,114	(59,258,943)	(24,003,747)
Net increase (decrease) in net assets resulting from operations	$ 35,802,029	$ (40,702,939)	$ (16,699,251)
Net increase (decrease) in net assets resulting from operations per common share (See Note 6)	$ 1.70	$ (1.93)	$ (0.80)

Net investment income per common share	$	1.08	$	0.88	$	0.35

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PENNANTPARK INVESTMENT CORPORATION

STATEMENTS OF CHANGES IN NET ASSETS

	Year ended September 30, 2009	Year ended September 30, 2008	Period from January 11, 2007 (inception) through September 30, 2007
Net increase (decrease) in net assets from operations:			
Net investment income	$ 22,718,915	$ 18,556,004	$ 7,304,496
Net realized loss on investments and cash equivalents	(39,243,879)	(11,154,735)	(81,769)
Net change in unrealized (appreciation) depreciation on investments and cash equivalents	44,498,373	(48,104,208)	(23,921,978)
Net change in unrealized depreciation on credit facility	7,828,620		
Net increase (decrease) in net assets resulting from operations	35,802,029	(40,702,939)	(16,699,251)
Dividends and distributions to stockholders:			
Dividends from net investment income	(20,226,021)	(18,961,895)	(7,545,458)
Return of capital			(28,356)
Total dividends and distributions	(20,226,021)	(18,961,895)	(7,573,814)
Capital share transactions:			
Issuance of shares of common stock	34,400,000		315,375,000
Offering costs related to public share offerings	(1,920,000)		(21,309,375)
Reinvestment of dividends			600,534
Net increase in net assets resulting from capital share transactions	32,480,000		294,666,159
Total increase (decrease) in net assets	48,056,008	(59,664,834)	270,393,094
Net Assets:			
Beginning of period	210,728,260	270,393,094	
Cumulative effect of adoption of fair value option (See Note 5)	41,796,000		
Adjusted beginning of period balance	252,524,260		
End of period	$ 300,580,268	$ 210,728,260	$ 270,393,094
Undistributed (distributions in excess of) net investment income, at period end	$ 1,890,235	$ (602,660)	$ (196,769)
Capital Share Activity:			
Shares issued from subscriptions	4,300,000		21,025,000
Shares issued from reinvestment of dividend			43,772
Total increase in capital shares	4,300,000		21,068,772

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PENNANTPARK INVESTMENT CORPORATION

STATEMENTS OF CASH FLOWS

	Year ended September 30, 2009	Year ended September 30, 2008	Period from January 11, 2007 (inception) through September 30, 2007
Cash flows from operating activities:			
Net increase (decrease) in net assets resulting from operations	$ 35,802,029	$ (40,702,939)	$ (16,699,251)
Adjustments to reconcile net increase (decrease) in net assets resulting from operations to net cash used for operating activities:			
Net change in net unrealized (appreciation) depreciation on investments and cash equivalents	(44,498,373)	48,104,208	23,921,978
Net change in unrealized (depreciation) on credit facility	(7,828,620)		
Net realized loss on investments and cash equivalents	39,243,879	11,154,735	81,769
Net accretion of discount and amortization of premium	(2,890,687)	(1,285,365)	(15,875)
Purchase of investments	(112,693,490)	(206,790,979)	(413,972,173)
Payment-in-kind interest	(4,729,590)	(2,434,562)	(668,268)
Proceeds from disposition of investments	27,956,008	70,120,751	99,635,961
Decrease (increase) in interest receivable	507,143	(1,528,349)	(4,517,850)
Decrease (increase) in prepaid expenses and other assets	258,912	146,104	(252,287)
Increase in distributions payable to stockholders		5,056,505	
(Decrease) increase in payables for cash equivalents purchased		(252,759,931)	252,759,931
Increase (decrease) in payables for investments purchased	19,489,525	(16,583,921)	16,583,921
Increase (decrease) in unfunded investments	6,331,385	(3,989,948)	3,989,948
(Decrease) increase in interest payable on credit facility	(652,529)	554,328	170,989
(Increase) in receivables for investments sold	(2,726,007)		
Increase in management fee payable	2,134,214	(288,585)	374,481
Increase in performance-based incentive fee payable	1,385,131	123,033	
Increase in accrued other expenses	555,556	356,376	735,312
Net cash used for operating activities	(42,355,514)	(390,748,539)	(37,871,414)
Cash flows from financing activities:			
Proceeds from issuance of common stock	34,400,000		315,375,000
Offering costs	(1,920,000)		(21,309,375)
Capitalized borrowing costs			(1,261,296)
Dividends and distributions to stockholders	(20,226,021)	(18,961,895)	(6,973,280)
Borrowings under credit facility (See Note 11)	169,600,000	461,040,000	271,913,786
Repayments under credit facility (See Note 11)	(146,500,000)	(269,040,000)	(261,913,786)
Net cash provided by financing activities	35,353,979	173,038,105	295,831,049
Net (decrease) increase in cash equivalents	(7,001,535)	(217,710,434)	257,959,635
Cash equivalents, beginning of period	40,249,201	257,959,635	
Cash equivalents, end of period	$ 33,247,666	$ 40,249,201	$ 257,959,635
Supplemental disclosure of cash flow information and non-cash activity:			
Interest paid	$ 5,014,055	$ 4,982,247	$ 1,598,055
Income taxes paid			150,000
Non-cash financing activities consist of the reinvestment of dividends totaling			600,534

Cumulative effect of adoption of fair value option on credit facility	41,796,000

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PENNANTPARK INVESTMENT CORPORATION

SCHEDULE OF INVESTMENTS

SEPTEMBER 30, 2009

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index (4)	Par/ Shares	Cost	Fair Value(3)
Investments in Non-Controlled, Non-Affiliated Portfolio Companies 150.9%(1),(2)							
Subordinated Debt/Corporate Notes 50.6%							
Affinion Group Holdings, Inc.	03/01/2012	Consumer Products	8.27%(6)	L+750	$ 23,572,133	$ 22,930,475	$ 21,497,875
Consolidated Foundries, Inc.	04/17/2015	Aerospace and Defense	14.25%(6)		8,109,468	7,952,769	8,190,563
CT Technologies Intermediate Holdings, Inc.	03/22/2014	Business Services	14.00%(6)		20,311,603	19,875,880	20,463,940
Digicel Limited (5)	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%(6)		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%(6)		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%(6)		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
Total Subordinated Debt/Corporate Notes						153,261,822	152,130,057
Second Lien Secured Debt 42.1%							
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%(6)	L+700(8)	2,309,343	2,309,344	2,309,344
Questex Media Group, Inc.	11/04/2014	Other Media	6.91%(7)	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.(5)	05/15/2015	Transportation	8.19%	L+775	10,000,000	9,941,121	7,100,000
Saint Acquisition Corp.(5)	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%(6)	L+575	21,500,000	18,855,728	19,414,500
Specialized Technology Resources, Inc.	12/15/2014	Chemical, Plastics and Rubber	7.25%(6)	L+700	22,500,000	22,488,166	22,500,000
TransFirst Holdings, Inc.	06/15/2015	Financial Services	7.04%(6)	L+675	16,792,105	16,247,489	15,264,023
Total Second Lien Secured Debt						143,571,496	126,382,167
Preferred Equity/Partnership Interests(7) 3.6%							
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
		Insurance			686	685,820	685,820

TZ Holdings, L.P., Series A (Trizetto Group, Inc.)					
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	2,499,067	3,094,252
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 INVESTMENTS (Continued)

SEPTEMBER 30, 2009

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index [4]	Par / Shares	Cost	Fair Value[3]
Common Equity/Warrants/Partnership Interests [7] 4.5%							
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		
Total Common Equity/Warrants/Partnership Interests						8,462,302	13,590,568
First Lien Secured Debt 50.1%							
1-800 Contacts, Inc.	03/04/2015	Distribution	7.70%	P+295[8]	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[5]	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[8]	10,000,000	9,421,220	10,050,000
EnviroSolutions, Inc.	07/07/2012	Environmental Services	11.00%[6]	P+775[8]	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[8]	12,668,615	12,965,067	13,169,026
Lyondell Chemical Co. [9]	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

		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%(7)	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
Sitel, 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(8)	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(8)	3,500,000	3,177,842	3,491,250
Yonkers Racing Corp. (5)	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 INVESTMENTS (Continued)

SEPTEMBER 30, 2009

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

(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

SCHEDULE OF INVESTMENTS

SEPTEMBER 30, 2008

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index [4]	Par	Cost	Value[3]
Investments in Non-Controlled, Non-Affiliated Portfolio Companies 168.1%[1), (2)]							
Subordinated Debt/Corporate Notes 76.8%							
Advanstar, Inc.	11/30/2015	Other Media	10.76%[6]	L+700	$ 16,268,634	$ 16,268,634	$ 12,567,520
Affinion Group Holdings, Inc.	03/01/2012	Consumer Products	9.37%[6]	L+625	22,500,000	21,587,384	18,562,500
Consolidated Foundries, Inc.	04/17/2015	Aerospace and Defense	14.25%[6]		8,000,000	7,831,761	8,000,000
CT Technologies Intermediate Holdings, Inc.	03/19/2014	Business Services	14.00%[6]		20,000,000	19,502,246	20,000,000
i2 Holdings Ltd.	06/06/2014	Aerospace and Defense	14.75%[6]		22,041,438	21,649,325	22,041,438
IDQ Holdings, Inc.	05/20/2012	Auto Sector	13.75%		20,000,000	19,555,782	20,000,000
Learning Care Group, Inc.	12/28/2015	Education	13.50%[6]		10,067,361	9,922,722	10,067,361
Realogy Corp.	04/15/2015	Buildings and Real Estate	12.38%		28,000,000	26,337,698	9,520,000
Trizetto Group, Inc.	10/01/2016	Insurance	13.50%[6]		20,000,000	19,811,785	20,000,000
UP Acquisitions Sub Inc.	02/08/2015	Oil and Gas	13.50%		21,000,000	20,428,146	21,000,000
Total Subordinated Debt/Corporate Notes					187,877,433	182,895,483	161,758,819
Second Lien Secured Debt 45.5%							
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	9.81%	L+700	12,000,000	11,682,795	11,160,000
Brand Energy and Infrastructure Services, Inc.	02/07/2015	Energy/Utilities	8.81%	L+600	13,600,000	13,068,290	12,342,000
Generics International (U.S.), Inc.	04/30/2015	Healthcare, Education and Childcare	11.26%	L+750	12,000,000	11,947,073	10,080,000
Questex Media Group, Inc.	11/04/2014	Other Media	9.31%	L+650	10,000,000	10,000,000	8,700,000
Saint Acquisition Corp.[5]	05/15/2015	Transportation	10.55%	L+775	10,000,000	9,951,058	3,100,000
Saint Acquisition Corp.[5]	05/15/2017	Transportation	12.50%		19,000,000	16,565,952	6,270,000
Sheridan Holdings, Inc.	06/15/2015	Healthcare, Education and Childcare	8.54%[6]	L+575	12,500,000	11,838,114	10,500,000
Specialized Technology Resources, Inc.	12/15/2014	Chemical, Plastics and Rubber	10.70%[6]	L+700	22,500,000	22,485,895	19,800,000
TransFirst Holdings, Inc.	06/15/2015	Financial Services	9.77%[6]	L+600	16,500,000	15,866,044	13,942,500
Total Second Lien Secured Debt					128,100,000	123,405,221	95,894,500
					Shares		
Preferred Equity 4.4%							
CFHC Holdings, Inc., Class A (Consolidated Foundries, Inc.)		Aerospace and Defense	12.00%[6]		842	841,927	841,927
i2 Holdings Ltd.		Aerospace and Defense	12.00%[6]		3,960,000	3,960,000	3,960,000
TZ Holdings, L.P., Series A (Trizetto Group, Inc.)		Insurance	[7]		686	685,820	685,820

TZ Holdings, L.P., Series B (Trizetto Group, Inc.)	Insurance	6.50%[(6)]	1,312	1,312,006	1,312,006
UP Holdings Inc., Class A-1 (UP Acquisitions Sub Inc.)	Oil and Gas	8.00%[(6)]	91,608	2,499,066	2,499,066
Total Preferred Equity			4,054,448	9,298,819	9,298,819

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PENNANTPARK INVESTMENT CORPORATION

SCHEDULE OF INVESTMENTS (Continued)

SEPTEMBER 30, 2008

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index (4)	Shares	Cost	Value(3)
Common Equity/Partnership Interest (7) 4.0%							
AHC Mezzanine (Advanstar Inc.)		Other Media			3,000	$ 3,000,000	$ 998,883
CFHC Holdings, Inc., (Consolidated Foundries, Inc.)		Aerospace and Defense			1,627	16,271	149,557
CT Technologies Holdings, LLC (CT Technologies Intermediate Holdings, Inc.)		Business Services			5,556	3,200,000	3,200,000
i2 Holdings Ltd.		Aerospace and Defense			440,000	440,000	1,545,062
TZ Holdings, L.P. (Trizetto Group, Inc.)		Insurance			2	2,173	2,173
UP Holdings Inc. (UP Acquisitions Sub Inc.)		Oil and Gas			91,608	916	2,569,208
Total Common Equity/Partnership Interest					541,793	6,659,360	8,464,883
					Par		
First Lien Secured Debt 37.4%							
Burlington Coat Factory Warehouse Corp.	05/28/2013	Retail Store	5.06%	L+225	$ 7,896,473	7,889,120	5,401,187
Cohr Holdings, Inc.	01/31/2013	Healthcare, Education and Childcare	5.35%	L+250	2,955,000	2,955,000	1,484,888
EnviroSolutions, Inc.	08/07/2012	Environmental Services	12.04%(6)	L+825	14,014,177	12,965,204	12,192,334
EnviroSolutions, Inc.	08/07/2012	Environmental Services	12.25%	P+725	2,293	2,121	1,995
Gatehouse Media Operating, Inc.	08/28/2014	Media	4.81%	L+200	7,000,000	7,000,000	3,336,690
General Nutrition Centers, Inc.	09/16/2013	Retail Store	5.57%	L+225	3,410,095	3,411,892	2,821,854
Greatwide Logistics Services, Inc.	12/19/2013	Cargo Transport	(7)		6,912,500	6,912,500	5,149,813
Hanley-Wood, L.L.C.	03/08/2014	Other Media	4.83%	L+225	8,932,500	8,932,500	6,327,185
Hughes Network Systems, L.L.C.	04/15/2014	Telecommunications	5.31%	L+250	5,000,000	5,000,000	4,275,000
Jacuzzi Brands Corp.	02/07/2014	Home and Office Furnishings, Housewares and Durable Consumer Products	5.35%	L+225	9,890,541	9,890,541	6,156,861
Levlad, L.L.C.	03/08/2014	Consumer Products	5.46%	L+225	4,564,563	4,564,563	2,639,837
Longview Power, L.L.C.	02/28/2014	Utilities	5.54%	L+225	3,000,000	3,000,000	2,630,001
Mattress Holding Corp.	01/18/2014	Home and Office Furnishings, Housewares and Durable Consumer Products	5.96%	L+225	3,950,100	3,950,100	2,567,565
Mitchell International, Inc.	03/28/2014	Business Services	5.81%	L+200	3,940,000	3,940,000	3,723,300
National Bedding Co., L.L.C.	02/28/2013	Home and Office Furnishings, Housewares and Durable Consumer Products	4.62%	L+200	6,895,000	6,900,583	5,274,675
Penton Media, Inc.	02/01/2013	Other Media	5.07%	L+225	4,925,000	4,925,000	3,558,313
Philosophy, Inc.	03/16/2014	Consumer Products	5.71%	L+200	1,474,667	1,474,667	1,194,480
Questex Media Group, Inc.	05/04/2014	Other Media	5.81%	L+300	4,924,167	4,924,167	4,825,683
Reader s Digest Association, Inc.	03/02/2014	Printing and Publishing	4.71%	L+200	985,000	985,000	699,350
Rexnord , L.L.C.	07/19/2013	Manufacturing/Basic Industry	5.76%	L+200	2,917,576	2,917,576	2,625,819

Sitel, L.L.C.	01/30/2014	Business Services	5.30%	L+250	2,592,017	2,592,017	1,892,172
Sitel, L.L.C.	01/30/2014	Business Services	6.50%	P+150	90,311	90,311	65,927
Total First Lien Secured Debt					106,271,980	105,222,862	78,844,929
Investments in Non-Controlled, Non-Affiliated Portfolio Companies						427,481,745	354,261,950

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PENNANTPARK INVESTMENT CORPORATION

SCHEDULE OF INVESTMENTS (Continued)

SEPTEMBER 30, 2008

Issuer Name	Maturity	Industry	Current Coupon	Basis Point Spread Above Index [4]	Par	Cost	Value[3]
Investments in Non-Controlled, Affiliated Portfolio Companies 8.5%[1],[2]							
Subordinated Debt/Corporate Notes 2.1%							
Performance Holdings, Inc.	07/02/2014	Leisure, Amusement, Motion Pictures, Entertainment	14.25%[6]		$ 4,414,356	$ 4,192,261	$ 4,414,356
Second Lien Secured Debt 4.0%							
Performance, Inc.	07/02/2013	Leisure, Amusement Motion Pictures, Entertainment	8.55%	L+575	8,750,000	8,750,000	8,347,500
					Shares		
Common Equity/Partnership Interest[7] 2.4%							
NCP-Performance (Performance Holdings, Inc.)		Leisure, Amusement, Motion Pictures, Entertainment			37,500	3,750,000	5,124,014
Investments in Non-Controlled, Affiliated Portfolio Companies						16,692,261	17,885,870
Total Investments 176.6%						$ 444,174,006	$ 372,147,820
					Par		
Cash Equivalents 19.1%							
Money Market Mutual Funds					$ 40,249,201	40,249,201	40,249,201
Total Cash Equivalents					40,249,201	40,249,201	40,249,201

Total Investments and Cash Equivalents 195.7%	$ 484,423,207	$ 412,397,021
Liabilities in Excess of Other Assets (95.7%)		$ (201,668,761)
Net Assets 100.0%		$ 210,728,260

(1) As used in this Schedule of Investments and in accordance with the Investment Company Act of 1940 (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 more than 5% 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) 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 payable in cash and/or payment-in-kind (PIK).
(7) Non-income producing.

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PENNANTPARK INVESTMENT CORPORATION

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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, and the purchase of first lien secured debt.

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 net proceeds of $3.3 million.

The consolidated financial statements, for the period from January 11, 2007 (inception) through September 30, 2007, include the accounts of PennantPark Investment and its wholly owned special purpose subsidiary, Pennant SPV Company, LLC (Pennant SPV) a Delaware corporation. On April 24, 2007, Pennant SPV transferred all of its assets to PennantPark Investment.

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.

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 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 are readily available but are deemed by our board of directors not reflective of the fair value of the investment, 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;

PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

(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.

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 (formerly known as FASB Statement No. 109), 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 corporate-level taxes in the future. 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 (formerly known as FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes) nor did we have any unrecognized tax benefits as of September 30, 2007, 2008 or 2009. Although we file federal and state tax returns, our major tax jurisdiction is federal. Our 2007 to 2009 federal tax years remain subject to examination by the Internal Revenue Service. See Note 7 to the financial statements.

(d) Dividends, Distributions, and Capital Transactions

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

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

(e) New Accounting Pronouncements and Accounting Standards Updates

In September 2006, FASB issued SFAS 157, *Fair Value Measurements*, 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. With adoption of the Accounting Standards Codification in September 2009, or ASC, references to authoritative accounting literature refer to the relevant section of the ASC. Adoption of ASC 820 (formerly known as SFAS 157) 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 have adopted ASC 820 on October 1, 2008. The adoption of ASC 820 did not affect our financial position or results of operations. See Note 2 and Note 5 to the financial statements.

In February 2007, FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB 115*. ASC 825 (formerly known as SFAS 159) permits an entity to choose to measure many financial instruments and certain other items at fair value. ASC 825 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 have adopted ASC 825 on October 1, 2008 and have made an irrevocable election to apply the fair value option to our long-term 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.

PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

Upon our adoption of ASC 825 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. We have used a nationally recognized independent valuations firm 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 have been recorded in the statement of operations. We have not elected to apply the fair value option to any other financial assets or liabilities. See Note 5 to the financial statements.

In April 2009, the FASB issued FASB Staff Position No. 157-4, 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* (FSP No. 157-4). ASC 820-10-35-51A (formerly known as FSP No. 157-4) made amendments to ASC 820 to provide additional guidance for estimating fair value in accordance with ASC 820 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 May 2009, FASB issued SFAS 165, or ASC 855, *Subsequent Events*, 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 SFAS 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB 162*, SFAS 168 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, will supersede all then-existing GAAP for non-governmental entities and reporting standards, subject to certain grandfathered literature. The purpose of ASC is not 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 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 2009. 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 adjusted gross assets , if any, see Note 11). Although the base management fee is 2.00% of 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 equals 2.00% since March 31, 2008 and is payable quarterly in arrears. The base management fee is calculated based on the average value of 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 fiscal years ended September 30, 2009 and 2008, the Investment Adviser received a net base management fee of $7.7 million and $6.7 million, respectively, from us. For the period from April 24, 2007 (initial public offering) through September 30, 2007, the Investment Adviser received a net base management fee of approximately $1.9 million 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 fiscal years ended September 30, 2009 and 2008, the Investment Adviser received an incentive fee of $5.7 million and $3.8 million, respectively from us. For the period from April 24, 2007 (initial public offering) through September 30, 2007, the Investment Adviser did not receive an incentive fee from us.

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PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

PennantPark Investment has also entered into an Administration Agreement with PennantPark Investment Administration, LLC (the Administrator or PennantPark Investment Administration), which was reapproved by our board of directors including a majority of our directors who are not interested persons of PennantPark Investment in February 2009. Under this agreement PennantPark Investment Administration provides administrative services for PennantPark Investment. For providing these services, facilities and personnel, PennantPark Investment reimburses the Administrator for PennantPark Investment s allocable portion of overhead and other expenses incurred by the Administrator in performing its obligations under the Administration Agreement, including rent, technology systems, insurance and PennantPark Investment s allocable portion of the costs of the compensation and related expenses for its chief compliance officer, chief financial officer and their respective staffs. The Administrator also provides on PennantPark Investment s behalf managerial assistance to portfolio companies to which PennantPark Investment is required to provide such assistance. Reimbursement for certain of these costs is included in administrative services expenses in the statement of operations. For the fiscal years ended September 30, 2009 and 2008, the Investment Adviser was reimbursed $1.7 million and $2.0 million, respectively, from us, including expenses it incurred on behalf of the Administrator, for services described above. For the period from April 24, 2007 (initial public offering) through September 30, 2007, the Investment Adviser was reimbursed approximately $0.5 million from us for services described above.

4. INVESTMENTS

Purchases of long-term investments including PIK for the fiscal years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007 totaled $117.4 million, $209.2 million and $414.6 million, respectively. Sales and repayments of long-term investments for the fiscal years ended September 30, 2009, 2008 and for the period from January 11, 2007 (inception) through September 30, 2007 totaled $28.0 million, $70.1 million and $99.6 million, respectively.

Investments and cash equivalents consisted of the following:

	September 30, 2009		September 30, 2008	
	Cost	Fair Value	Cost	Fair Value
First lien	$ 164,863,868	$ 150,607,490	$ 105,222,862	$ 78,844,929
Second lien	152,321,496	134,401,542	132,155,221	104,242,000
Subordinated debt / corporate notes	158,139,903	157,119,017	187,087,744	166,173,175
Preferred equity	9,750,317	10,934,053	9,298,819	9,298,819
Common equity	12,212,302	16,697,971	10,409,360	13,588,897
Cash equivalents	33,247,666	33,247,666	40,249,201	40,249,201
Total	$ 530,535,552	$ 503,007,739	$ 484,423,207	$ 412,397,021

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 September 30, 2009 and September 30, 2008.

Industry Classification	September 30, 2009	September 30, 2008
Chemicals, Plastic and Rubber	9%	5%
Aerospace and Defense	8	10
Business Services	7	8
Healthcare, Education and Childcare	7	6
Hotels, Motels, Inns and Gaming	7	

Oil and Gas	6	7
Consumer Products	5	6
Energy / Utilities	5	6
Insurance	5	6
Transportation	5	2
Auto Sector	4	5
Buildings and Real Estate	3	3
Cargo Transport	3	1
Distribution	3	
Environmental Services	3	3
Financial Services	3	4
Home and Office Furnishings, Housewares, and Durable Consumer Products	3	4
Leisure, Amusement, Motion Picture, Entertainment	3	5
Other Media	3	10
Education	2	3
Logistics	2	
Retail	1	2
Other	3	4
Total	100%	100%

PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

5. FAIR VALUE OF FINANCIAL INSTRUMENTS

Effective October 1, 2008, we adopted ASC 820 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.

In April 2009, the FASB issued FASB Staff Position No. 157-4, 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* (FSP No. 157-4). ASC 820-10-35-51A (formerly known as FSP No. 157-4) made amendments to ASC 820 to provide additional guidance for estimating fair value in accordance with ASC 820 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.

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.

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PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

At 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:

		Fair Value Measurements Using		
Description	**Fair Value**	**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
Total Investments	469,760,073			469,760,073
Cash Equivalents	33,247,666	33,247,666		
Total Investments, Cash Equivalents	503,007,739	33,247,666		469,760,073
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*):

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)	(39,243,879)		(39,243,879)
Unrealized appreciation / (depreciation)	42,008,505	2,489,868	44,498,373
Purchases, PIK, and net discount accretion	118,059,327	2,254,440	120,313,767
Sales / repayments	(27,956,008)		(27,956,008)
Transfers in and /or out of *Level 3*			
Ending Balance, September 30, 2009	$ 442,128,049	$ 27,632,024	$ 469,760,073
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 *Level 3* assets still held at the reporting date	$ 30,141,081	$ 2,489,868	$ 32,630,949

The following tables show a reconciliation of the beginning and ending balances for fair valued liabilities measured using significant unobservable inputs (*Level 3*):

	Long-Term Credit Facility
Beginning balance, September 30, 2008	$ 162,000,000
Cumulative effect of adoption of fair value option	(41,796,000)
Total unrealized appreciation included in earnings	(7,828,620)
Borrowings	108,200,000
Repayments	(52,100,000)
Transfers in and/or out of *Level 3*	
Ending Balance, September 30, 2009	$ 168,475,380

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PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

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 our fiscal year ended September 30, 2009, $7.8 million was recorded as the change in unrealized appreciation on the credit facility in the statement of operations. PennantPark Investment has used 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.

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 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.

The following table presents information about the eligible instrument for which PennantPark Investment elected the fair value option under ASC 825 as of September 30, 2009 and for which a transition adjustment was recorded as of October 1, 2008:

	September 30, 2009		Cost on October 1, 2008 before adoption of ASC 825	Transition Adjustment to Retained Earnings	Carrying Value/ Fair Value on October 1, 2008 after adoption of ASC 825
	Cost	Carrying/ Fair Value			
Revolving Credit Facility					
Long-term	$ 218,100,000	$ 168,475,380	$ 162,000,000	$ 41,796,000	$ 120,204,000
Temporary draw(1)	7,000,000	7,000,000	40,000,000		40,000,000
Total	$ 225,100,000	$ 175,475,380	$ 202,000,000	$ 41,796,000	$ 160,204,000

(1) Temporary draw may include credit facility borrowings at the end of each quarter to maximize investment flexibility. See Note 11 to the financial statements.

6. 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	Year ended September 30, 2009	Year ended September 30, 2008	Period from January 11, 2007 (inception) through September 30, 2007
Numerator for net increase (decrease) in net assets resulting from operations	$ 35,802,029	$ (40,702,939)	$ (16,699,251)
Denominator for basic and diluted weighted average shares	21,092,334**	21,068,772	20,936,149*
Basic and diluted net increase (decrease) in net assets per share resulting from operations	$ 1.70	$ (1.93)	$ (0.80)

* Since completion of IPO on April 24, 2007

** Denominator for diluted weighted average shares is 21,094,745. See Note 13 to the financial statements.

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PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

7. TAXES AND DISTRIBUTIONS

Dividends from net investment income and distributions from net realized capital gains are determined in accordance with U.S. federal tax regulations, which may differ from amounts determined in accordance with GAAP. These book/tax differences are either temporary or permanent in nature. To the extent these differences are permanent, they are reclassified to undistributed net investment income, accumulated net realized loss or paid-in-capital, as appropriate in the period that the differences arise. The following differences were reclassified for tax purposes for the year ended September 30, 2009:

Decrease in paid-in capital	$ (1,536)
Decrease in accumulated net realized loss	$ (87,991)
Increase in undistributed net investment income	$ 89,527

As of September 30, 2009, the cost of investments for federal income tax purposes was $497.3 million resulting in a gross unrealized appreciation and depreciation of $19.4 million and $46.9 million, respectively. The following reconciles net increase in net assets resulting from operations to taxable income for the year ended September 30, 2009:

Net increase in net assets resulting from operations	$ 35,802,029
Net realized loss on investments	39,243,879
Net unrealized appreciation on investments transactions	(44,498,373)
Net unrealized depreciation on credit facility	(7,828,620)
Other taxable income	841,335
Other deductible expenses	(13,808)
Taxable income before deductions for distributions	$ 23,546,442

As of September 30, 2009, the components of accumulated losses on tax basis and reconciliation to accumulated losses on a book basis were as follows:

Undistributed ordinary income	$ 7,618,230
Undistributed long-term net capital gains	
Total undistributed net earnings	7,618,230
Capital loss carry forward*	(11,250,565)
Post-October capital losses	(39,331,872)
Dividend payable and other temporary differences	(5,638,469)
Net unrealized appreciation of investments and credit facility	22,096,807
Total accumulated losses	$ (26,505,869)

* As of September 30, 2009, the Fund had a capital loss carryforward of $11.2 million. If not utilized against future capital gains, $0.2 million of this capital loss carryforward will expire in 2016 and $11.0 million will expire in 2017.

The tax character of dividends declared during the fiscal year ended September 30, 2009 was solely from ordinary income and totaled $20.2 million or $0.96 per share.

8. 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.

9. 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 September 30, 2009 or 2008.

PENNANTPARK INVESTMENT CORPORATION

NOTES TO FINANCIAL STATEMENTS (Continued)

SEPTEMBER 30, 2009

10. FINANCIAL HIGHLIGHTS

On September 30, 2009 and 2008, PennantPark Investment s total net assets and net asset value per share were $300.6 million and $210.7 million, respectively, and $11.85 and $10.00, respectively. On September 30, 2007, PennantPark Investment s total net assets and net asset value per share were $270.4 million and $12.83, respectively. Below please find the financial highlights for the periods ending September 30, 2009, 2008 and 2007.

	Year ended September 30, 2009	Year ended September 30, 2008	Period from January 11, 2007 (inception) through September 30, 2007
Per Share Data:			
Net asset value, beginning of period	$ 10.00	$ 12.83	$
Cumulative effect of adoption of fair value option(1)	1.99		
Adjusted net asset value, beginning of period	11.99	12.83	
Net investment income(2)	1.08	0.88	0.35
Net change in realized and unrealized loss(2)	0.62	(2.81)	(1.15)
Net increase (decrease) in net assets resulting from operations	1.70	(1.93)	(0.80)
Dividends and distributions to stockholders(3)	(0.96)	(0.90)	(0.36)
Initial issuance of common stock			15.00
Dilutive effect of common stock issuance below net asset value	(0.79)		
Offering costs related to public offerings	(0.09)		(1.01)
Net asset value, end of period	$ 11.85	$ 10.00	$ 12.83
Per share market value, end of period	$ 8.11	$ 7.41	$ 13.40
Total return(4)	30.39%	(38.58)%	(8.29)%*(7)
Shares outstanding at end of period	25,368,772	21,068,772	21,068,772
Ratio/Supplemental Data:			
Ratio of operating expenses to average net assets(5)	7.42%	6.30%	3.76%(7)
Ratio of credit facility related expenses to average net assets	1.93%	2.66%	1.50%(7)
Total expenses to average net assets(6)	9.35%	8.96%	5.26%(7)
Ratio of net investment income to average net assets	9.49%	7.82%	5.96%(7)
Net assets at end of period	$ 300,580,268	$ 210,728,260	$ 270,393,094
Average debt outstanding	$ 182,490,685	$ 119,472,732	$ 817,610 (7)
Average debt per share	$ 8.65	$ 5.67	$ 0.04 (7)
Portfolio turnover ratio	7.47%	20.10%	62.20%

* Not annualized

(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 and net change in realized and unrealized loss per share data are calculated based on the weighted average shares outstanding for the respective period.

(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.

(5) The ratio of operating expenses to average net assets before adoption of ASC 825 for the fiscal year ended September 30, 2009 was 9.32%. The ratio of operating expenses to average net assets before management fee waiver was 6.47% and 4.28% for the fiscal year ended September 30, 2008 and for the period from April 24, 2007 (initial public offering) through September 30, 2007, respectively.

(6) The ratio of total expenses to average net assets before adoption of ASC 825 for the fiscal year ended September 30, 2009 was 11.75%. the ratio of total expenses before management fee waiver to average net assets was 9.13% and 5.78% for the fiscal year ended September 30, 2008 and for the period from April 24, 2007 (initial public offering) through September 30, 2007, respectively.

(7) Since initial public offering on April 24, 2007.

11. 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 September 30, 2009, there was $225.1 million in outstanding borrowings under the credit facility (including a $7.0 million temporary draw), with a weighted average interest rate at the time of 1.31% 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 is approximately 271% including temporary draw as of September 30, 2009 or 278% excluding such draws, 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.

12. 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.

13. SUBSEQUENT EVENTS

Subsequent events after the Statement of Assets and Liabilities date have been evaluated through the November 18, 2009.

On October 13, 2009, the underwriters of the follow-on public offering of common stock exercised their over-allotment option under the underwriting agreement and elected to purchase an additional 440,000 shares of common stock from us at a price of $8.00 per share, resulting in proceeds, net of underwriting fees, of $3.3 million.

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Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

Item 9A. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

As of September 30, 2009, we, including our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) of the 1934 Act). Based on that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective and provided reasonable assurance that information required to be disclosed in our periodic SEC filings is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. However, in evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of such possible controls and procedures.

(b) Management s Report on Internal Control Over Financial Reporting

Management s Report on Internal Control Over Financial Reporting, which appears on page 40 of this Form 10-K, is incorporated by reference herein.

(c) Changes in Internal Controls Over Financial Reporting.

There have been no material changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our most recently completed fiscal quarter, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None

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PART III

We will file a definitive Proxy Statement for our 2010 Annual Meeting of Stockholders with the SEC, pursuant to Regulation 14A, not later than 120 days after the end of our fiscal year. Accordingly, certain information required by Part III has been omitted under General Instruction G(3) to Form 10-K. Only those sections of our definitive Proxy Statement that specifically address the items set forth herein are incorporated by reference.

Item 10. Directors, Executive Officers and Corporate Governance

The information required by Item 10 is hereby incorporated by reference from our definitive Proxy Statement relating to our 2010 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days following the end of our fiscal year.

Item 11. Executive Compensation

The information required by Item 11 is hereby incorporated by reference from our definitive Proxy Statement relating to our 2010 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days following the end of our fiscal year.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information required by Item 12 is hereby incorporated by reference from our definitive Proxy Statement relating to our 2010 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days following the end of our fiscal year.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by Item 13 is hereby incorporated by reference from our definitive Proxy Statement relating to our 2010 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days following the end of our fiscal year.

Item 14. Principal Accountant Fees and Services

The information required by Item 14 is hereby incorporated by reference from our definitive Proxy Statement relating to our 2010 Annual Meeting of Stockholders, to be filed with the Securities and Exchange Commission within 120 days following the end of our fiscal year.

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PART IV

Item 15. Exhibits and Financial Statement Schedules

The following documents are filed as part of this Annual Report:

(1) Financial Statements Refer to Item 8 starting on page 40.

(2) Financial Statement Schedules None.

(3) Exhibits

3.1	Articles of Incorporation (Incorporated by reference to the Registrant s Pre-Effective Amendment No.1 to the Registration Statement on Form N-2/A (File No. 333-140092), filed on March 5, 2007).
3.2	Amended and Restated Bylaws of the Registrant (Incorporated by reference to Exhibit 3.2 to 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).
10.1	Form of Investment Management Agreement between the Registrant and PennantPark Investment Advisers, LLC (Incorporated by reference to Exhibit 99(g) to the Registrant s Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
10.2	Form of Custodian Agreement between the Registrant and PFPC Trust Company (Incorporated by reference to Exhibit 99(j)(1) to the Registrant s Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
10.3	Form of Administration Agreement between the Registrant and various lenders (Incorporated by reference to Exhibit 99(k)(1) to the Registrant s Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
10.4	Dividend Reinvestment Plan (Incorporated by reference to Exhibit 99(e) to the Registrant s Registration Statement on Form N-2 (File No. 333-150033), filed on April 2, 2008).
10.5	Senior Secured Revolving Credit Agreement between Registrant and various lenders (Incorporated by reference to the Report on Form 8-K. Exhibit 99.2 (File No. 814-00736), filed on June 28, 2007).
11	Computation of Per Share Earnings (included in the notes to the audited financial statements contained in this Report).
14.1*	Joint Code of Ethics of the Registrant.
31.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
31.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14 of the Securities Exchange Act of 1934, as amended.
32.1*	Certification of Chief Executive Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer pursuant to section 906 of The Sarbanes-Oxley Act of 2002.
99.1	Privacy Policy of the Registrant (Incorporated by reference to Exhibit 99.1 to the Registrant s Annual Report on Form 10-K (File No. 814-00736), filed on December 13, 2007).

* Filed herewith

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SIGNATURES

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

By:	/s/ ARTHUR H. PENN
Name:	**Arthur H. Penn**
Title:	**Chief Executive Officer and Chairman of the Board**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ ARTHUR H. PENN	Chairman of the Board of Directors and Chief Executive Officer	November 18, 2009
Arthur H. Penn	(Principal Executive Officer)	
/s/ AVIV EFRAT	Chief Financial Officer and Treasurer	November 18, 2009
Aviv Efrat	(Principal Financial and Accounting Officer)	
/s/ ADAM K. BERNSTEIN	Director	November 18, 2009
Adam K. Bernstein		
/s/ JEFFREY FLUG	Director	November 18, 2009
Jeffrey Flug		
/s/ MARSHALL BROZOST	Director	November 18, 2009
Marshall Brozost		
/s/ SAMUEL L. KATZ	Director	November 18, 2009
Samuel L. Katz		