

GLADSTONE INVESTMENT CORPORATION\DE  
Form 10-Q  
October 28, 2014

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

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

**OR**

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

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

**Commission file number: 814-00704**

**GLADSTONE INVESTMENT CORPORATION**  
**(Exact name of registrant as specified in its charter)**

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

**83-0423116**  
**(I.R.S. Employer**  
**Identification No.)**

**1521 WESTBRANCH DRIVE, SUITE 100**  
**MCLEAN, VIRGINIA**  
**(Address of principal executive office)**  
**(703) 287-5800**

**22102**  
**(Zip Code)**

**(Registrant's telephone number, including area code)**

**Not Applicable**

**(Former name, former address and former fiscal year, if changed from last report)**

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

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

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

Large accelerated filer  Accelerated filer

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. The number of shares of the issuer's Common Stock, \$0.001 par value per share, outstanding as of October 27, 2014, was 26,475,958.



**GLADSTONE INVESTMENT CORPORATION**

**TABLE OF CONTENTS**

<b>PART I. <u>FINANCIAL INFORMATION:</u></b>	
Item 1. <u>Financial Statements (Unaudited)</u>	
Condensed Consolidated Statements of Assets and Liabilities as of September 30 and March 31, 2014	2
<u>Condensed Consolidated Statements of Operations for the three and six months ended September 30, 2014 and 2013</u>	3
<u>Condensed Consolidated Statements of Changes in Net Assets for the six months ended September 30, 2014 and 2013</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the six months ended September 30, 2014 and 2013</u>	5
<u>Condensed Consolidated Schedules of Investments as of September 30 and March 31, 2014</u>	6
<u>Notes to Condensed Consolidated Financial Statements</u>	13
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	
<u>Overview</u>	30
<u>Results of Operations</u>	34
<u>Liquidity and Capital Resources</u>	42
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	50
Item 4. <u>Controls and Procedures</u>	50
<b>PART II. <u>OTHER INFORMATION:</u></b>	
Item 1. <u>Legal Proceedings</u>	51
Item 1A. <u>Risk Factors</u>	51
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	51
Item 3. <u>Defaults Upon Senior Securities</u>	51
Item 4. <u>Mine Safety Disclosures</u>	51
Item 5. <u>Other Information</u>	51
Item 6. <u>Exhibits</u>	51
<u>SIGNATURES</u>	52

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES**  
**(DOLLAR AMOUNTS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)**  
**(UNAUDITED)**

	September 30, 2014	March 31, 2014
<b>ASSETS</b>		
Investments at fair value		
Non-Control/Non-Affiliate investments (Cost of <b>\$181,693</b> and \$233,895, respectively)	\$ 172,970	\$ 205,440
Affiliate investments (Cost of <b>\$201,605</b> and \$120,010, respectively)	156,661	87,849
Control investments (Cost of <b>\$28,782</b> and \$29,632 respectively)	17,270	21,104
Total investments at fair value (Cost of <b>\$412,080</b> and \$383,537, respectively)	346,901	314,393
Cash	3,052	4,553
Restricted cash	3,450	5,314
Interest receivable	1,713	1,289
Due from custodian	1,177	1,704
Deferred financing costs	3,569	2,355
Other assets	1,312	1,086
Total assets	\$ 361,174	\$ 330,694
<b>LIABILITIES</b>		
Borrowings:		
Line of credit at fair value (Cost of <b>\$87,750</b> and \$61,250, respectively)	\$ 87,750	\$ 61,701
Secured borrowing	5,096	5,000
Total borrowings	92,846	66,701
Mandatorily redeemable preferred stock, \$0.001 par value, \$25 liquidation preference; 1,610,000 shares authorized, <b>1,600,000</b> shares issued and outstanding	40,000	40,000
Accounts payable and accrued expenses	1,055	665
Fees due to Adviser <sup>(A)</sup>	1,307	1,225
Fee due to Administrator <sup>(A)</sup>	209	224
Other liabilities	984	1,042
Total liabilities	136,401	109,857
Commitments and contingencies <sup>(B)</sup>		
<b>NET ASSETS</b>		
Common stock, \$0.001 par value per share, 100,000,000 shares authorized, <b>26,475,958</b> shares issued and outstanding	\$ 26	\$ 26
Capital in excess of par value	286,866	287,062

Cumulative net unrealized depreciation of investments	(65,179)	(69,144)
Cumulative net unrealized depreciation of other	(74)	(525)
Net investment income in excess of distributions	3,344	3,616
Accumulated net realized loss	(210)	(198)
<b>Total net assets</b>	<b>224,773</b>	<b>220,837</b>
Total liabilities and net assets	\$ 361,174	\$ 330,694
<b>NET ASSET VALUE PER SHARE AT END OF PERIOD</b>	<b>\$ 8.49</b>	<b>\$ 8.34</b>

(A) Refer to Note 4 *Related Party Transactions* for additional information.

(B) Refer to Note 10 *Commitments and Contingencies* for additional information.

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(DOLLAR AMOUNTS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)**  
**(UNAUDITED)**

	Three Months Ended September 30		Six Months Ended September 30,	
	2014	2013	2014	2013
<b>INVESTMENT INCOME</b>				
Interest income				
Non-Control/Non-Affiliate investments	\$ 4,494	\$ 5,216	\$ 9,751	\$ 9,893
Affiliate investments	3,540	473	6,156	931
Control investments	535	2,017	1,065	4,063
Cash and cash equivalents	1		2	1
Total interest income	8,570	7,706	16,974	14,888
Other income				
Non-Control/Non-Affiliate investments	501	25	1,900	241
Affiliate investments		333	34	333
Control investments		3,295		3,295
Total other income	501	3,653	1,934	3,869
Total investment income	9,071	11,359	18,908	18,757
<b>EXPENSES</b>				
Base management fee <sup>(A)</sup>	1,744	1,561	3,410	3,110
Loan servicing fee <sup>(A)</sup>	1,158	1,116	2,293	2,141
Incentive fee <sup>(A)</sup>	1,051	1,557	2,266	1,722
Administration fee <sup>(A)</sup>	209	156	444	399
Interest expense on borrowings	720	597	1,458	1,074
Dividends on mandatorily redeemable preferred stock	712	712	1,425	1,425
Amortization of deferred financing fees	282	256	536	499
Professional fees	305	159	547	280
Other general and administrative expenses	450	467	747	832
Expenses before credits from Adviser	6,631	6,581	13,126	11,482
Credit of loan servicing fee <sup>(A)</sup>	(1,158)	(1,116)	(2,293)	(2,141)
Other credits to Adviser fees <sup>(A)</sup>	(606)	(334)	(988)	(845)
Total expenses net of credits to fees	4,867	5,131	9,845	8,496
<b>NET INVESTMENT INCOME</b>	<b>4,204</b>	<b>6,228</b>	<b>9,063</b>	<b>10,261</b>

<b>REALIZED AND UNREALIZED (LOSS) GAIN</b>					
Net realized (loss) gain:					
Control investments	(12)	24,804	(12)	24,804	
Total net realized (loss) gain	(12)	24,804	(12)	24,804	
Net unrealized (depreciation) appreciation:					
Non-Control/Non-Affiliate investments	9,454	1,258	9,899	(8,378)	
Affiliate investments	(4,283)	411	(2,941)	(3,022)	
Control investments	(6,666)	(17,353)	(2,993)	(15,690)	
Other		(409)	451	445	
Total net unrealized (depreciation) appreciation	(1,495)	(16,093)	4,416	(26,645)	
Net realized and unrealized (loss) gain	(1,507)	8,711	4,404	(1,841)	
<b>NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS</b>					
	\$ 2,697	\$ 14,939	\$ 13,467	\$ 8,420	
<b>BASIC AND DILUTED PER COMMON SHARE:</b>					
Net investment income	\$ 0.16	\$ 0.24	\$ 0.34	\$ 0.39	
Net increase in net assets resulting from operations	\$ 0.10	\$ 0.57	\$ 0.51	\$ 0.32	
Distributions	\$ 0.18	\$ 0.15	\$ 0.36	\$ 0.30	
<b>WEIGHTED AVERAGE SHARES OF COMMON STOCK OUTSTANDING:</b>					
Basic and diluted	26,475,958	26,475,958	26,475,958	26,475,958	

(A) Refer to Note 4 *Related Party Transactions* for additional information.

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*



**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS**

(IN THOUSANDS)

(UNAUDITED)

	<b>Six Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
<b>OPERATIONS:</b>		
Net investment income	\$ 9,063	\$ 10,261
Net realized (loss) gain of investments	(12)	24,804
Net unrealized appreciation (depreciation) of investments	3,965	(27,090)
Net unrealized appreciation of other	451	445
Net increase in net assets from operations	13,467	8,420
<b>DISTRIBUTIONS TO COMMON STOCKHOLDERS:</b>	<b>(9,531)</b>	<b>(7,943)</b>
Total increase in net assets	3,936	477
Net assets at beginning of period	220,837	240,963
Net assets at end of period	\$ 224,773	\$ 241,440

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(IN THOUSANDS)

(UNAUDITED)

	Six Months Ended September 30,	
	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net increase in net assets resulting from operations	\$ 13,467	\$ 8,420
Adjustments to reconcile net increase in net assets resulting from operations to net cash (used in) provided by operating activities:		
Purchase of investments	(29,287)	(55,990)
Principal repayments of investments	802	22,200
Increase in investment balance due to paid in kind interest	(58)	(30)
Net proceeds from the sale of investments	(12)	30,804
Net realized loss (gain) on investments	12	(24,804)
Net unrealized (appreciation) depreciation of investments	(3,965)	27,090
Net unrealized appreciation of other	(451)	(445)
Amortization of deferred financing costs	536	499
Decrease (increase) in restricted cash	1,864	(4,851)
Increase in interest receivable	(424)	(170)
Decrease in due from custodian	527	633
Increase in other assets	(226)	(293)
Increase (decrease) in accounts payable and accrued expenses	357	(24)
Increase (decrease) in fees due to Adviser <sup>(A)</sup>	82	(120)
Decrease in administration fee due to Administrator <sup>(A)</sup>	(15)	(65)
(Decrease) increase in other liabilities	(58)	592
Net cash (used in) provided by operating activities	(16,849)	3,446
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from short-term loans		48,014
Repayments on short-term loans		(84,025)
Proceeds from line of credit	36,800	71,500
Repayments on line of credit	(10,300)	(68,500)
Proceeds from secured borrowing	96	
Purchase of derivative		(75)
Payment of deferred financing costs	(1,717)	(1,088)
Distributions paid to common stockholders	(9,531)	(7,943)
Net cash provided by (used in) financing activities	15,348	(42,117)
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(1,501)</b>	<b>(38,671)</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<b>4,553</b>	<b>85,904</b>

<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<b>\$</b>	<b>3,052</b>	<b>\$</b>	<b>47,233</b>
---	-----------	--------------	-----------	---------------

(A) Refer to Note 4 *Related Party Transactions* for additional information.

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS**

**September 30, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

**(UNAUDITED)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value
<b>NON-CONTROL/NON-AFFILIATE INVESTMENTS<sup>(L)</sup>:</b>					
Auto Safety House, LLC	Automobile	Line of Credit , \$1,000 available (7.0%, Due 10/2018)	\$ 5,000	\$ 5,000	\$ 4,900
				5,000	4,900
B-Dry, LLC	Personal, Food and Miscellaneous Services	Line of Credit, \$0 available (6.5%, Due 5/2015)	750	750	544
		Senior Term Debt (13.5%, Due 5/2015)	6,433	6,443	4,703
		Senior Term Debt (13.5%, Due 5/2015)	2,840	2,840	2,066
		Common Stock Warrants (85 shares) <sup>(C)(F)</sup>		300	
				10,333	7,313
Cavert II Holding Corp.	Containers, Packaging, and Glass	Preferred Stock (18,446 shares) <sup>(C)(F)</sup>		1,845	3,140
				1,845	3,140
Country Club Enterprises, LLC	Automobile	Senior Subordinated Term Debt (18.6%, Due 5/2017)	4,000	4,000	4,000
		Preferred Stock (7,079,792 shares) <sup>(C)(F)</sup>		7,725	2,888
		Guaranty (\$2,000) <sup>(D)</sup>			
		Guaranty (\$716) <sup>(D)</sup>			
				11,725	6,888
Drew Foam Company, Inc.	Chemicals, Plastics, and Rubber	Senior Term Debt (13.5%, Due 8/2017)	10,913	10,913	10,913
		Preferred Stock (34,045 shares) <sup>(C)(F)</sup>		3,375	1,769
		Common Stock (5,372 shares) <sup>(C)(F)</sup>		63	
				14,351	12,682

Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

Frontier Packaging, Inc.	Containers, Packaging, and Glass	Senior Term Debt (12.0%, Due 12/2017)	12,500	12,500	12,500
		Preferred Stock (1,373 shares) <sup>(C)(F)</sup>		1,373	1,591
		Common Stock (152 shares) <sup>(C)(F)</sup>		152	1,102
				14,025	15,193
Funko, LLC <sup>(K)</sup>	Personal and Non-Durable Consumer Products (Manufacturing Only)	Senior Subordinated Term Debt (12.0% and 1.5% PIK, Due 5/2019)	7,646	7,646	7,817
		Preferred Stock (1,305 shares) <sup>(C)(F)</sup>		1,305	5,691
				8,951	13,508
Ginsey Home Solutions, Inc.	Home and Office Furnishings, Housewares, and Durable Consumer Products	Senior Subordinate Term Debt (13.5%, Due 1/2018) <sup>(H)</sup>	13,300	13,300	13,300
		Preferred Stock (18,898 shares) <sup>(C)(F)</sup>		9,583	1,660
		Common Stock (63,747 shares) <sup>(C)(F)</sup>		8	
				22,891	14,960
Jackrabbit, Inc.	Farming and Agriculture	Senior Term Debt (13.5%, Due 4/2018)	11,000	11,000	11,000
		Preferred Stock (3,556 shares) <sup>(C)(F)</sup>		3,556	3,986
		Common Stock (548 shares) <sup>(C)(F)</sup>		94	4,341
				14,650	19,327
Mathey Investments, Inc.	Machinery (Nonagriculture, Nonconstruction, Nonelectronic)	Senior Term Debt (10.0%, Due 3/2016)	1,375	1,375	1,375
		Senior Term Debt (12.0%, Due 3/2016)	3,727	3,727	3,727
		Senior Term Debt (12.5%, Due 3/2016) <sup>(E)(I)</sup>	3,500	3,500	3,500
		Common Stock (29,102 shares) <sup>(C)(F)</sup>		777	7,204
				9,379	15,806
Mitchell Rubber Products, Inc.	Chemicals, Plastics, and Rubber	Subordinated Term Debt (13.0%, Due 10/2016) <sup>(I)</sup>	13,560	13,560	12,543
			1,500	1,500	1,388

		Subordinated Term Debt (13.0%, Due 12/2015) <sup>(1)</sup>			
		Preferred Stock (27,900 shares) <sup>(C)(F)</sup>		2,790	
		Common Stock (27,900 shares) <sup>(C)(F)</sup>		28	
				17,878	13,931
Precision Southeast, Inc.	Diversified/Conglomerate Manufacturing	Senior Term Debt (14.0%, Due 12/2015)	5,617	5,617	5,617
		Preferred Stock (19,091 shares) <sup>(C)(F)</sup>		1,909	108
		Common Stock (90,909 shares) <sup>(C)(F)</sup>		91	
				7,617	5,725

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)**

**September 30, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

**(UNAUDITED)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value
Quench Holdings Corp.	Home and Office Furnishings, Housewares, and Durable Consumer Products	Common Stock (4,770,392 shares) <sup>(C)(F)</sup>		\$ 3,397	\$ 4,753
				3,397	4,753
SBS, Industries, LLC	Machinery (Nonagriculture, Nonconstruction, Nonelectronic)	Senior Term Debt (14.0%, Due 8/2016)	11,355	11,355	11,355
				1,994	2,527
				221	381
			13,570	14,263	
Schylling Investments, LLC	Leisure, Amusement, Motion Pictures, Entertainment	Senior Term Debt (13.0%, Due 8/2017)	13,081	13,081	13,081
				4,000	
			17,081	13,081	
Star Seed, Inc.	Farming and Agriculture	Senior Term Debt (12.5%, Due 4/2018)	7,500	7,500	7,500
				1,499	
				1	
			9,000	7,500	
<b>Total Non-Control/Non-Affiliate Investments (represents 49.9% of total investments at fair value)</b>				<b>\$ 181,693</b>	<b>\$ 172,970</b>

**AFFILIATE INVESTMENTS<sup>(M)</sup>:**

Acme Cryogenics, Inc.	Chemicals, Plastics, and Rubber	Senior Subordinated Term Debt (11.5%, Due 3/2015) <sup>(I)</sup>	\$ 14,500	\$ 14,500	\$ 14,500
		Preferred Stock (965,982 shares) <sup>(C)(F)</sup>		7,956	12,639
		Common Stock (549,908 shares) <sup>(C)(F)</sup>		1,197	
		Common Stock Warrants (465,639 shares) <sup>(C)(F)</sup>		25	
			23,678	27,139	
Alloy Die Casting Corp. <sup>(K)</sup>	Diversified/Conglomerate Manufacturing	Senior Term Debt (13.5%, Due 10/2018)	12,215	12,215	12,200
		Preferred Stock (4,064 shares) <sup>(C)(F)</sup>		4,064	2,619
		Common Stock (630 shares) <sup>(C)(F)</sup>		41	
			16,320	14,819	
Behrens Manufacturing, LLC <sup>(K)</sup>	Diversified/Conglomerate Manufacturing	Senior Term Debt (13.0%, Due 12/2018)	9,975	9,975	9,975
		Preferred Stock (2,923 shares) <sup>(C)(F)</sup>		2,922	2,684
			12,897	12,659	
Cambridge Sound Management, LLC	Home and office Furnishings, Housewares and Durable Consumer Products	Line of Credit, \$325 available (13.0%, Due 9/2015) <sup>(J)</sup>	675	675	675
		Senior Term Debt (13.0%, Due 9/2019) <sup>(J)</sup>	15,000	15,000	15,000
		Preferred Stock (4,500 shares) <sup>(C)(F)(J)</sup>		4,500	4,500
			20,175	20,175	
Channel Technologies Group, LLC	Diversified/Conglomerate Manufacturing	Preferred Stock (2,279 shares) <sup>(C)(F)</sup>		2,864	2,110
		Common Stock (2,279,020 shares) <sup>(C)(F)</sup>			
			2,864	2,110	
Danco Acquisition Corp.	Diversified/Conglomerate Manufacturing	Line of Credit, \$550 available (4.0%, Due 8/2015)	4,000	4,000	300
		Senior Term Debt (4.0%, Due 8/2015)	2,575	2,575	193
		Senior Term Debt (4.0%, Due 8/2015)	8,795	8,795	660



Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

		Due 8/2015)			
		Senior Term Debt (5.0%, Due 8/2015) <sup>(E)</sup>	1,150	1,150	86
		Preferred Stock (25 shares) <sup>(C)(F)</sup>		2,500	
		Common Stock (1,241 shares) <sup>(C)(F)</sup>		3	
				19,023	1,239
Edge Adhesives Holdings, Inc. <sup>(K)</sup>	Diversified/Conglomerate Manufacturing	Line of Credit, \$345 available (10.5%, Due 8/2015)	1,155	1,155	1,152
		Senior Term Debt (12.5%, Due 2/2019)	9,300	9,300	9,312
		Senior Term Debt (13.75%, Due 11/2014) <sup>(J)</sup>	877	877	877
		Senior Subordinated Term Debt (13.75%, Due 2/2019)	2,400	2,400	2,406
		Preferred Stock (3,474 shares) <sup>(C)(F)</sup>		3,474	4,327
				17,206	18,074
Head Country Food Products, Inc.	Beverage, Food and Tobacco	Senior Term Debt (12.5%, Due 2/2019)	9,050	9,050	9,050
		Preferred Stock (4,000 shares) <sup>(C)(F)</sup>		4,000	1,757
				13,050	10,807

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)**

**September 30, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

**(UNAUDITED)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value	
Meridian Rack & Pinion, Inc. <sup>(K)</sup>	Automobile	Senior Term Debt (13.5%, Due 12/2018)	\$ 9,660	\$ 9,660	\$ 9,648	
		Preferred Stock (3,381 shares) <sup>(C)(F)</sup>		3,381	3,613	
				13,041	13,261	
NDLI Inc.	Cargo Transport	Line of Credit, \$0 available (10.5%, Due 1/2015)	1,225	1,225	968	
		Senior Term Debt (11.0%, Due 1/2015)	7,227	7,227	5,709	
		Senior Term Debt (10.5%, Due 1/2015)	3,650	3,650	2,847	
		Senior Term Debt (10.5%, Due 1/2015) <sup>(E)</sup>	3,650	3,650	2,865	
		Preferred Stock (3,600 shares) <sup>(C)(F)</sup>			3,600	
		Common Stock (545 shares) <sup>(C)(F)</sup>				
				19,352	12,389	
SOG Specialty K&T, LLC	Leisure, Amusement, Motion Pictures, Entertainment	Senior Term Debt (13.3%, Due 10/2017)	6,200	6,200	6,200	
		Senior Term Debt (14.8%, Due 10/2017)	12,199	12,199	12,199	
		Preferred Stock (9,749 shares) <sup>(C)(F)</sup>		9,749	5,590	
				28,148	23,989	
Tread Corp.	Oil and Gas	Line of Credit, \$496 available (12.5%, Due 2/2015) <sup>(G)(I)</sup>	2,754	2,754		
		Senior Subordinated Term Debt (12.5%, Due 2/2015) <sup>(G)(I)</sup>	5,000	5,000		
		Senior Subordinated Term Debt	2,750	2,750		

		(12.5%, Due 2/2015) <sup>(G)(I)</sup>			
		Senior Subordinated Term Debt			
		(12.5%, Due 2/2015) <sup>(G)(I)</sup>	1,000	1,000	
		Senior Subordinated Term Debt			
		(12.5%, Due on Demand) <sup>(G)(I)</sup>	510	510	
		Preferred Stock (3,332,765			
		shares) <sup>(C)(F)</sup>		3,333	
		Common Stock (7,716,320			
		shares) <sup>(C)(F)</sup>		501	
		Common Stock Warrants			
		(2,372,727 shares) <sup>(C)(F)</sup>		3	
				15,851	
		<b>Total Affiliate Investments (represents 45.1% of total investments at fair value)</b>		<b>\$ 201,605</b>	<b>\$ 156,661</b>
<b>CONTROL INVESTMENTS<sup>(N)</sup>:</b>					
Galaxy Tool Holding Corp.	Aerospace and Defense	Senior Subordinated Term Debt			
		(13.5%, Due 8/2017)	\$ 15,520	\$ 15,520	\$ 15,520
		Preferred Stock (6,039,387			
		shares) <sup>(C)(F)</sup>		11,464	
		Common Stock (88,843			
		shares) <sup>(C)(F)</sup>		48	
				27,032	15,520
Tread Real Estate Corp.	Buildings and Real Estate	Common Stock (1,000			
		shares) <sup>(C)(F)(J)</sup>		1,750	1,750
				1,750	1,750
		<b>Total Control Investments (represents 5.0% of total investments at fair value)</b>		<b>\$ 28,782</b>	<b>\$ 17,270</b>
		<b>TOTAL INVESTMENTS</b>		<b>\$ 412,080</b>	<b>\$ 346,901</b>

- (A) Certain of the securities listed above are issued by affiliate(s) of the indicated portfolio company. Additionally, the majority of the securities listed above, totaling \$315.7 million at fair value, is pledged as collateral to our Credit Facility as described further in Note 5 *Borrowings*.
- (B) Percentages represent the weighted average cash interest rates in effect at September 30, 2014, and due date represents the contractual maturity date. Unless indicated otherwise, all cash interest rates are indexed to 30-day LIBOR. If applicable, paid-in-kind ( PIK ) interest rates are noted separately from the cash interest rates.
- (C) Security is non-income producing.
- (D) Refer to Note 10 *Commitments and Contingencies* for additional information regarding these guaranties.
- (E) Last Out Tranche ( LOT ) of senior debt, meaning if the portfolio company is liquidated, the holder of the LOT is paid after the other senior debt but before the senior subordinated debt.
- (F) Where applicable, aggregates all shares of such class of stock owned without regard to specific series owned within such class (some series of which may or may not be voting shares) or aggregates all warrants to purchase shares of such class of stock owned without regard to specific series of such class of stock such warrants allow us to purchase.
- (G) Debt security is on non-accrual status.
- (H) \$5.1 million of the debt security participated to a third party but accounted for as collateral for a secured borrowing for accounting principles generally accepted in the U.S. ( GAAP ) purposes.
- (I) Debt security has a fixed interest rate.
- (J) New proprietary portfolio investment valued at cost, as it was determined that the price paid during the three months ended September 30, 2014 best represents fair value as of September 30, 2014.
- (K) One of our affiliated funds, Gladstone Capital Corporation, co-invested with us in this portfolio company pursuant to an exemptive order granted by the Securities and Exchange Commission ( SEC ).
- (L) Non-Control/Non-Affiliate investments, as defined by the Investment Company Act of 1940, as amended, (the 1940 Act ), are those that are neither Control nor Affiliate investments and in which we own less than 5.0% of the issued and outstanding voting securities.
- (M) Affiliate investments, as defined by the 1940 Act, are those in which we own, with the power to vote, between and inclusive of 5.0% and 25.0% of the issued and outstanding voting securities.
- (N) Control investments, as defined by the 1940 Act, are those where we have the power to exercise a controlling influence over the management or policies of the portfolio company, which may include owning, with the power to vote, more than 25.0% of the issued and outstanding voting securities.

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS**

**MARCH 31, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value	
<b>NON-CONTROL/NON-AFFILIATE INVESTMENTS<sup>(L)</sup>:</b>						
Acme Cryogenics, Inc.	Chemicals, Plastics, and Rubber	Senior Subordinated Term Debt (11.5%, Due 3/2015) <sup>(K)</sup>	\$ 14,500	\$ 14,500	\$ 14,500	
		Preferred Stock (898,814 shares) <sup>(C)(F)</sup>		6,984	11,276	
		Common Stock (418,072 shares) <sup>(C)(F)</sup>			1,045	
		Common Stock Warrants (465,639 shares) <sup>(C)(F)</sup>			25	
				22,554	25,776	
Alloy Die Casting Corp.	Diversified/Conglomerate Manufacturing	Senior Term Debt (13.5%, Due 10/2018) <sup>(D)</sup>	12,215	12,215	12,261	
		Preferred Stock (4,064 shares) <sup>(C)(F)</sup>		4,064	1,948	
		Common Stock (630 shares) <sup>(C)(F)</sup>			41	
				16,320	14,209	
Auto Safety House, LLC	Automobile	Line of Credit, \$1,000 available (7.0%, Due 10/2018) <sup>(D)(K)</sup>	5,000	5,000	4,925	
		Guaranty (\$500) Guaranty (\$250)				
				5,000	4,925	
B-Dry, LLC	Personal, Food and Miscellaneous Services	Line of Credit, \$0 available (6.5%, Due 5/2014)	750	750	566	
		Senior Term Debt (13.5%, Due 5/2014)	6,433	6,443	4,865	
		Senior Term Debt (13.5%, Due 5/2014)	2,840	2,840	2,144	
		Common Stock Warrants (85 shares) <sup>(C)(F)</sup>			300	
				10,333	7,575	

## Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

Cavert II Holding Corp.	Containers, Packaging, and Glass	Preferred Stock (18,446 shares) <sup>(C)(F)</sup>		1,845	3,023
				1,845	3,023
Country Club Enterprises, LLC	Automobile	Senior Subordinated Term Debt (18.6%, Due 11/2014)	4,000	4,000	4,000
		Preferred Stock (7,079,792 shares) <sup>(C)(F)</sup>		7,725	3,670
		Guaranty (\$2,000)			
		Guaranty (\$878)			
				11,725	7,670
Drew Foam Company, Inc.	Chemicals, Plastics, and Rubber	Senior Term Debt (13.5%, Due 8/2017)	10,913	10,913	10,913
		Preferred Stock (34,045 shares) <sup>(C)(F)</sup>		3,375	1,351
		Common Stock (5,372 shares) <sup>(C)(F)</sup>		63	
				14,351	12,264
Frontier Packaging, Inc.	Containers, Packaging, and Glass	Senior Term Debt (12.0%, Due 12/2017)	12,500	12,500	12,500
		Preferred Stock (1,373 shares) <sup>(C)(F)</sup>		1,373	1,522
		Common Stock (152 shares) <sup>(C)(F)</sup>		152	843
				14,025	14,865
Funko, LLC	Personal and Non-Durable Consumer Products (Manufacturing Only)	Senior Subordinated Term Debt (12.0% and 1.5% PIK, Due 5/2019) <sup>(D)</sup>	7,587	7,587	7,729
		Preferred Stock (1,305 shares) <sup>(C)(F)</sup>		1,305	2,276
				8,892	10,005
Ginsey Home Solutions, Inc.	Home and Office Furnishings, Housewares, and Durable Consumer Products	Senior Subordinate Term Debt (13.5%, Due 1/2018) <sup>(I)</sup>	13,050	13,050	13,050
		Preferred Stock (18,898 shares) <sup>(C)(F)</sup>		9,393	3,082
		Common Stock (63,747 shares) <sup>(C)(F)</sup>		8	
				22,451	16,132
Jackrabbit, Inc.	Farming and Agriculture	Line of Credit, \$3,000 available (13.5%, Due 4/2014)			

		Senior Term Debt (13.5%, Due 4/2018)	11,000	11,000	11,000
		Preferred Stock (3,556 shares) <sup>(C)(F)</sup>		3,556	1,963
		Common Stock (548 shares) <sup>(C)(F)</sup>		94	
				14,650	12,963
Mathey Investments, Inc.	Machinery (Nonagriculture, Nonconstruction, Nonelectronic)	Senior Term Debt (10.0%, Due 3/2016)			
			1,375	1,375	1,375
		Senior Term Debt (12.0%, Due 3/2016)	3,727	3,727	3,727
		Senior Term Debt (12.5%, Due 3/2016) <sup>(E)(K)</sup>	3,500	3,500	3,500
		Common Stock (29,102 shares) <sup>(C)(F)</sup>		777	4,895
				9,379	13,497

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)**

**MARCH 31, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value	
Mitchell Rubber Products, Inc.	Chemicals, Plastics, and Rubber	Subordinated Term Debt (13.0%, Due 10/2016) <sup>(D)(K)</sup>	\$ 13,560	\$ 13,560	\$ 13,628	
		Preferred Stock (27,900 shares) <sup>(C)(F)</sup>		2,790	1,086	
		Common Stock (27,900 shares) <sup>(C)(F)</sup>			28	
					16,378	14,714
Noble Logistics, Inc.	Cargo Transport	Line of Credit, \$0 available (10.5%, Due 1/2015) <sup>(D)</sup>	800	800	204	
		Senior Term Debt (11.0%, Due 1/2015) <sup>(D)</sup>	7,227	7,227	1,842	
		Senior Term Debt (10.5%, Due 1/2015) <sup>(D)</sup>	3,650	3,650	931	
		Senior Term Debt (10.5%, Due 1/2015) <sup>(D)(E)</sup>	3,650	3,650	931	
					15,327	3,908
Precision Southeast, Inc.	Diversified/Conglomerate Manufacturing	Senior Term Debt (14.0%, Due 12/2015)	5,617	5,617	5,617	
		Preferred Stock (19,091 shares) <sup>(C)(F)</sup>		1,909		
		Common Stock (90,909 shares) <sup>(C)(F)</sup>			91	
					7,617	5,617
Quench Holdings Corp.	Home and Office Furnishings, Housewares, and Durable Consumer Products	Common Stock (4,770,391 shares) <sup>(C)(F)</sup>		3,397	5,056	
				3,397	5,056	
SBS, Industries, LLC			11,355	11,355	11,355	



Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

	Machinery (Nonagriculture, Nonconstruction, Nonelectronic)	Senior Term Debt (14.0%, Due 8/2016)			
		Preferred Stock (19,935 shares) <sup>(C)(F)</sup>		1,994	1,064
		Common Stock (221,500 shares) <sup>(C)(F)</sup>		221	
				13,570	12,419
Schylling Investments, LLC	Leisure, Amusement, Motion Pictures, Entertainment	Senior Term Debt (13.0%, Due 8/2017) <sup>(D)</sup>	13,081	13,081	13,228
		Preferred Stock (4,000 shares) <sup>(C)(F)</sup>		4,000	
				17,081	13,228
Star Seed, Inc.	Farming and Agriculture	Senior Term Debt (12.5%, Due 4/2018) <sup>(D)</sup>	7,500	7,500	7,594
		Preferred Stock (1,499 shares) <sup>(C)(F)</sup>		1,499	
		Common Stock (600 shares) <sup>(C)(F)</sup>		1	
				9,000	7,594
<b>Total Non-Control/Non-Affiliate Investments (represents 65.4% of total investments at fair value)</b>				<b>\$ 233,895</b>	<b>\$ 205,440</b>

**AFFILIATE INVESTMENTS<sup>(M)</sup>:**

Behrens Manufacturing, LLC	Diversified/Conglomerate Manufacturing	Senior Term Debt (13.0%, Due 12/2018)	\$ 9,975	\$ 9,975	\$ 9,975
		Preferred Stock (2,923 shares) <sup>(C)(F)</sup>		2,922	2,754
				12,897	12,729
Channel Technologies Group, LLC	Diversified/Conglomerate Manufacturing	Preferred Stock (2,279 shares) <sup>(C)(F)</sup>		2,864	3,122
		Common Stock (2,279,020 shares) <sup>(C)(F)</sup>			
				2,864	3,122
Danco Acquisition Corp.	Diversified/Conglomerate Manufacturing	Line of Credit, \$700 available (4.0%, Due 8/2015) <sup>(D)</sup>	3,450	3,450	690
		Senior Term Debt (4.0%, Due 8/2015) <sup>(D)</sup>	2,575	2,575	515
		Senior Term Debt (4.0%, Due 8/2015) <sup>(D)</sup>	8,795	8,795	1,759

Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

		Senior Term Debt (5.0%, Due 8/2015) <sup>(D)(E)</sup>	1,150	1,150	236
		Preferred Stock (25 shares) <sup>(C)(F)</sup>		2,500	
		Common Stock (1,241 shares) <sup>(C)(F)</sup>		3	
				18,473	3,200
Edge Adhesives Holdings, Inc.	Diversified/Conglomerate Manufacturing	Line of Credit, \$705 available (10.5%, Due 8/2014) <sup>(H)</sup>	795	795	795
		Senior Term Debt (12.5%, Due 2/2019) <sup>(H)</sup>	9,300	9,300	9,300
		Senior Subordinated Term Debt (13.5%, Due 2/2019) <sup>(H)</sup>	2,400	2,400	2,400
		Preferred Stock (3,474 shares) <sup>(C)(F)(H)</sup>		3,474	3,474
				15,969	15,969
Head Country Food Products, Inc.	Beverage, Food and Tobacco	Line of Credit, \$500 available (10.0%, Due 8/2014) <sup>(H)</sup>			
		Senior Term Debt (12.5%, Due 2/2019) <sup>(H)</sup>	9,050	9,050	9,050
		Preferred Stock (4,000 shares) <sup>(C)(F)(H)</sup>		4,000	4,000
				13,050	13,050

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.*

**GLADSTONE INVESTMENT CORPORATION**  
**CONDENSED CONSOLIDATED SCHEDULE OF INVESTMENTS (Continued)**

**MARCH 31, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS)**

Company <sup>(A)</sup>	Industry	Investment <sup>(B)</sup>	Principal	Cost	Fair Value	
Meridian Rack & Pinion, Inc.	Automobile	Senior Term Debt (13.5%, Due 12/2018) <sup>(D)</sup>	\$ 9,660	\$ 9,660	\$ 9,672	
		Preferred Stock (3,381 shares) <sup>(C)(F)</sup>		3,381	3,468	
				13,041	13,140	
SOG Specialty K&T, LLC	Leisure, Amusement, Motion Pictures, Entertainment	Senior Term Debt (13.3%, Due 8/2016)	6,200	6,200	6,200	
		Senior Term Debt (14.8%, Due 8/2016)	12,199	12,199	12,199	
		Preferred Stock (9,749 shares) <sup>(C)(F)</sup>		9,749	8,240	
				28,148	26,639	
Tread Corp.	Oil and Gas	Line of Credit, \$779 available (12.5%, Due 6/2014) <sup>(G)(K)</sup>	2,471	2,471		
		Senior Subordinated Term Debt (12.5%, Due 2/2015) <sup>(G)(K)</sup>	5,000	5,000		
		Senior Subordinated Term Debt (12.5%, Due 2/2015) <sup>(G)(K)</sup>	2,750	2,750		
		Senior Subordinated Term Debt (12.5%, Due 2/2015) <sup>(G)(K)</sup>	1,000	1,000		
		Senior Subordinated Term Debt (12.5%, Due on Demand) <sup>(G)(K)</sup>	510	510		
		Preferred Stock (3,332,765 shares) <sup>(C)(F)</sup>			3,333	
		Common Stock (7,716,320 shares) <sup>(C)(F)</sup>				501
		Common Stock Warrants (2,372,727 shares) <sup>(C)(F)</sup>			3	
				15,568		
<b>Total Affiliate Investments (represents 27.9% of total investments at fair value)</b>				<b>\$ 120,010</b>	<b>\$ 87,849</b>	

**CONTROL INVESTMENTS<sup>(N)</sup>:**

Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

Galaxy Tool Holding Corp.	Aerospace and Defense	Senior Subordinated Term Debt (13.5%, Due 8/2017)	\$ 15,520	\$ 15,520	\$ 15,520
		Preferred Stock (6,039,387 shares) <sup>(C)(F)</sup>		11,464	2,992
		Common Stock (88,843 shares) <sup>(C)(F)</sup>		48	
				27,032	18,512
NDLI Acquisition Inc.	Cargo Transport	Preferred Stock (2,600 shares) <sup>(C)(F)</sup>		2,600	2,592
		Common Stock (545 shares) <sup>(C)(F)</sup>			
				2,600	2,592
<b>Total Control Investments (represents 6.7% of total investments at fair value)</b>			<b>\$ 29,632</b>	<b>\$ 21,104</b>	
<b>TOTAL INVESTMENTS<sup>(J)</sup></b>			<b>\$ 383,537</b>	<b>\$ 314,393</b>	

- (A) Certain of the securities listed above are issued by affiliate(s) of the indicated portfolio company.
- (B) Percentages represent the weighted average cash interest rates in effect at March 31, 2014, and due date represents the contractual maturity date. Unless indicated otherwise, all cash interest rates are indexed to 30-day LIBOR. If applicable, paid-in-kind ( PIK ) interest rates are noted separately from the cash interest rates.
- (C) Security is non-income producing.
- (D) Fair value based primarily on opinions of value submitted by Standard & Poor's Securities Evaluations, Inc. as of March 31, 2014.
- (E) Last Out Tranche ( LOT ) of senior debt, meaning if the portfolio company is liquidated, the holder of the LOT is paid after the other senior debt but before the senior subordinated debt.
- (F) Where applicable, aggregates all shares of such class of stock owned without regard to specific series owned within such class (some series of which may or may not be voting shares) or aggregates all warrants to purchase shares of such class of stock owned without regard to specific series of such class of stock such warrants allow us to purchase.
- (G) Debt security is on non-accrual status.
- (H) New proprietary portfolio investment valued at cost, as it was determined that the price paid during the three months ended March 31, 2014 best represents fair value as of March 31, 2014.
- (I) \$5 million of the debt security participated to a third party but accounted for as collateral for a secured borrowing for accounting principles generally accepted in the U.S. ( GAAP ) purposes.
- (J) Cumulative gross unrealized depreciation for federal income tax purposes is \$83,197; cumulative gross unrealized appreciation for federal income tax purposes is \$13,913. Cumulative net unrealized depreciation is \$69,284, based on a tax cost of \$383,677.
- (K) Debt security has a fixed interest rate.
- (L) Non-Control/Non-Affiliate investments, as defined by the Investment Company Act of 1940, as amended, (the 1940 Act ), are those that are neither Control nor Affiliate investments and in which we own less than 5.0% of the issued and outstanding voting securities.
- (M) Affiliate investments, as defined by the 1940 Act, are those in which we own, with the power to vote, between and inclusive of 5.0% and 25.0% of the issued and outstanding voting securities.
- (N) Control investments, as defined by the 1940 Act, are those where we have the power to exercise a controlling influence over the management or policies of the portfolio company, which may include owning, with the power to vote, more than 25.0% of the issued and outstanding voting securities.

*THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE CONDENSED CONSOLIDATED  
FINANCIAL STATEMENTS.*

---

**GLADSTONE INVESTMENT CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**SEPTEMBER 30, 2014**

**(DOLLAR AMOUNTS IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA AND AS OTHERWISE INDICATED)**

**NOTE 1. ORGANIZATION**

Gladstone Investment Corporation ( Gladstone Investment ) was incorporated under the General Corporation Law of the State of Delaware on February 18, 2005, and completed an initial public offering on June 22, 2005. The terms the Company, we, our and us all refer to Gladstone Investment and its consolidated subsidiaries. We are an externally advised, closed-end, non-diversified management investment company that has elected to be treated as a business development company ( BDC ) under the Investment Company Act of 1940, as amended (the 1940 Act ). In addition, we have elected to be treated for tax purposes as a regulated investment company ( RIC ) under the Internal Revenue Code of 1986, as amended (the Code ). We were established for the purpose of investing in debt and equity securities of established private businesses in the United States ( U.S. ). Debt investments primarily come in the form of three types of loans: senior term loans, senior subordinated loans and junior subordinated debt. Equity investments primarily take the form of preferred or common equity (or warrants or options to acquire the foregoing), often in connection with buyouts and other recapitalizations. Our investment objectives are: (a) to achieve and grow current income by investing in debt securities of established businesses that we believe will provide stable earnings and cash flow to pay expenses, make principal and interest payments on our outstanding indebtedness and make distributions to stockholders that we anticipate will grow over time, and (b) to provide our stockholders with long-term capital appreciation in the value of our assets by investing in equity securities of established businesses that we believe can grow over time to permit us to sell our equity investments for capital gains. We aim to maintain a portfolio allocation of approximately 80% debt investments and 20% equity investments, at cost.

Gladstone Business Investment, LLC ( Business Investment ), a wholly-owned subsidiary, was established on August 11, 2006 for the sole purpose of owning our portfolio of investments in connection with our line of credit. The financial statements of Business Investment are consolidated with those of Gladstone Investment. We also have significant subsidiaries whose financial statements are not consolidated with ours. Refer to Note 12 *Unconsolidated Significant Subsidiaries* for additional information regarding our unconsolidated significant subsidiaries.

We are externally managed by Gladstone Management Corporation (the Adviser ), an affiliate of ours and a SEC registered investment adviser, pursuant to an investment advisory agreement and management agreement. Administrative services are provided by Gladstone Administration, LLC (the Administrator ), an affiliate of ours and the Adviser, pursuant to an administration agreement.

**NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Unaudited Interim Financial Statements and Basis of Presentation*

We prepare our interim financial statements in accordance with accounting principles generally accepted in the U.S. ( GAAP ) for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Articles 6 and 10 of SEC Regulation S-X. Accordingly, we have omitted certain disclosures accompanying annual financial statements prepared in accordance with GAAP. The accompanying *Condensed Consolidated Financial Statements* include our accounts and those of our wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated. Under Article 6 of Regulation S-X, and the authoritative accounting guidance provided by the

American Institute of Certified Public Accountants Audit and Accounting Guide for Investment Companies, we are not required to consolidate any portfolio company investments, including those in which we have a controlling interest. In our opinion, all adjustments, consisting solely of normal recurring accruals, necessary for the fair statement of financial statements for the interim periods have been included. The results of operations for the three and six months ended September 30, 2014, are not necessarily indicative of results that ultimately may be achieved for the year. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in our annual report on Form 10-K for the fiscal year ended March 31, 2014, as filed with the SEC on May 13, 2014.

Our fiscal year-end *Condensed Consolidated Statement of Assets and Liabilities* presented in this Form 10-Q was derived from audited financial statements, but does not include all disclosures required by GAAP.

#### *Revisions*

Certain amounts in the prior year's consolidated financial statements have been revised to correct the presentation for the three and six months ended September 30, 2014 with no effect on our financial condition or results of operations. Certain amounts that were revised relate to our change in the classification of certain of our investments between control, affiliate and non-control/non-affiliate. The general change in the definitions from prior reported periods to the three and six months ended September 30, 2014, relate to the use of voting equity securities as the primary determinate of classification compared to the use of both voting and non-voting equity securities in prior periods.

Other revisions related to the net presentation of certain fees in our results of operations. The Adviser services, administers and collects on the loans held by Business Investment, in return for which the Adviser receives a 2% annual fee from Business Investment. All loan servicing fees are credited back to us by our Advisor. Previously, we incorrectly presented the loan servicing fee on a net basis, which is zero because it is 100% credited back to us. We have revised our fee presentation related to these loan servicing fees to reflect the gross fee and related gross credit amounts.

Management evaluated these errors in presentation and concluded they were not material to the previously issued financial statements for the three and six months ended September 30, 2013. The impact of the revisions are shown in the table below:

	Three Months Ended September 30, 2013		Six Months Ended September 30, 2013	
	As Previously Reported	As Revised	As Previously Reported	As Revised
<b>Interest income</b>				
Non-Control/Non-Affiliate investments	\$ 917	\$ 5,216	\$ 1,353	\$ 9,893
Affiliate investments	1,107	473	2,215	931
Control investments	5,682	2,017	11,319	4,063
Cash and cash equivalents			1	1
<b>Total interest income</b>	<b>7,706</b>	<b>7,706</b>	<b>14,888</b>	<b>14,888</b>
<b>Other income</b>				
Non-Control/Non-Affiliate investments		25		241
Affiliate investments	333	333	333	333
Control investments	3,320	3,295	3,536	3,295
<b>Total other income</b>	<b>3,653</b>	<b>3,653</b>	<b>3,869</b>	<b>3,869</b>
<b>Expenses</b>				
Non-revised expenses, in aggregate	5,465	5,465	9,341	9,341
Loan servicing fee		1,116		2,141
Expenses before credits from Adviser	5,465	6,581	9,341	11,482
Credit of loan servicing fee		(1,116)		(2,141)
Other credits to Adviser fees	(334)	(334)	(845)	(845)
<b>Total expenses net of credits to fees</b>	<b>5,131</b>	<b>5,131</b>	<b>8,496</b>	<b>8,496</b>
<b>Net unrealized (depreciation) appreciation</b>				
Non-Control/Non-Affiliate investments	(106)	1,258	(3,116)	(8,378)
Affiliate investments	1,571	411	2,449	(3,022)
Control investments	(17,149)	(17,353)	(26,423)	(15,690)
Other	(409)	(409)	445	445



<b>Total net unrealized depreciation</b>	<b>\$ (16,093)</b>	<b>\$ (16,093)</b>	<b>\$ (26,645)</b>	<b>\$ (26,645)</b>
--	--------------------	--------------------	--------------------	--------------------

*Investment Valuation Policy*

Accounting Recognition

We record our investments at fair value in accordance with the Financial Accounting Standards Board (the FASB ) Accounting Standards Codification Topic 820, *Fair Value Measurements and Disclosures* ( ASC 820 ) and the 1940 Act. Investment transactions are recorded on the trade date. Realized gains or losses are measured by the difference between the net proceeds from the repayment or sale and amortized cost basis of the investment, without regard to unrealized depreciation or appreciation previously recognized, and include investments charged off during the period, net of recoveries. Unrealized depreciation or appreciation primarily reflect the change in investment fair values, including the reversal of previously recorded unrealized depreciation or appreciation when gains or losses are realized.

Board Responsibility

In accordance with the 1940 Act, our board of directors (our Board of Directors ) has the ultimate responsibility for reviewing and approving, in good faith, the fair value of our investments based on our established investment valuation policy (the Policy ). Our Board of Directors reviews valuation recommendations that are provided by professionals of the Adviser and Administrator with oversight and direction from the Valuation Officer, employed by the Administrator (the Valuation Team ). There is no single standard for determining fair value (especially for privately-held businesses), as fair value depends upon the specific facts and circumstances of each individual investment. In determining the fair value of our investments, the Valuation Team, led by the Valuation Officer, uses the Policy, which has been approved by our Board of Directors, and each quarter our Board of Directors reviews the Policy to determine if changes thereto are advisable and also reviews whether the Valuation Team has applied the Policy consistently.

### Use of Third Party Valuation Firms

The Valuation Team engages third party valuation firms to provide independent assessments of the fair value of certain of our investments. Currently, the third-party service provider Standard & Poor's Securities Evaluation, Inc. ( SPSE ) provides estimates of fair value on the majority of our debt investments.

The Valuation Team generally assigns SPSE's estimates of fair value to our debt investments where we do not have the ability to effectuate a sale of the applicable portfolio company. The Valuation Team corroborates SPSE's estimates of fair value using one or more of the valuation techniques discussed below. The Valuation Team's estimates of value on a specific debt investment may significantly differ from SPSE's. When this occurs, our Board of Directors reviews whether the Valuation Team has followed the Policy, whether the Valuation Team's recommended value is reasonable in light of the Policy and other facts and circumstances, and in light of all relevant information, then votes to accept or reject the Valuation Team's recommended valuation.

### Valuation Techniques

In accordance with ASC 820, the Valuation Team uses the following techniques when valuing our investment portfolio:

***Total Enterprise Value*** In determining the fair value using a total enterprise value ( TEV ), the Valuation Team first calculates the TEV of the portfolio company by incorporating some or all of the following factors: the portfolio company's ability to make payments and other specific portfolio company attributes; the earnings of the portfolio company (the trailing or projected twelve month revenue or earnings before interest, taxes, depreciation and amortization ( EBITDA )); EBITDA or revenue multiples obtained from our indexing methodology whereby the original transaction EBITDA or revenue multiple at the time of our closing is indexed to a general subset of comparable disclosed transactions and EBITDA or revenue multiples from recent sales to third parties of similar securities in similar industries; a comparison to publicly traded securities in similar industries; and other pertinent factors. To gather information regarding these factors, the Valuation Team generally references industry statistics and may use outside experts. Once the TEV is determined for a portfolio company, the Valuation Team then allocates the TEV to the portfolio company's securities in order of their relative priority in the capital structure. Generally, the Valuation Team uses TEV to value our equity investments and, in the circumstances where we have the ability to effectuate a sale of a portfolio company, our debt investments.

TEV is primarily calculated using EBITDA or revenue multiples; however, TEV may also be calculated using a discounted cash flow ( DCF ) analysis whereby future expected cash flows of the portfolio company are discounted to determine a net present value using estimated risk-adjusted discount rates, which incorporate adjustments for nonperformance and liquidity risks. Generally, the Valuation Team uses the DCF to calculate the TEV to corroborate estimates of value for our equity investments, where we do not have the ability to effectuate a sale of a portfolio company or for debt of credit impaired portfolio companies.

***Yield Analysis*** The Valuation Team generally determines the fair value of our debt investments using the yield analysis, which includes a DCF calculation and the Valuation Team's own assumptions, including, but not limited to, estimated remaining life, current market yield, current leverage, and interest rate spreads. This technique develops a modified discount rate that incorporates risk premiums including, among other things, increased probability of default, increased loss upon default and increased liquidity risk. Generally, the Valuation Team uses the yield analysis to corroborate both estimates of value provided by SPSE and market

quotes.

In addition to the above valuation techniques, the Valuation Team may also consider other factors when determining fair values of our investments, including, but not limited to: the nature and realizable value of the collateral, including external parties' guaranties; any relevant offers or letters of intent to acquire the portfolio company; and the markets in which the portfolio company operates. If applicable, new debt and equity investments made during the three months ended September 30, 2014 are generally valued at original cost basis. Fair value measurements of our investments may involve subjective judgments and estimates and due to the inherent uncertainty of determining these fair values, the fair value of our investments may fluctuate from period to period. Additionally, changes in the market environment and other events that may occur over the life of the investment may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. Further, such investments are generally subject to legal and other restrictions on resale or otherwise are less liquid than publicly traded securities. If we were required to liquidate a portfolio investment in a forced or liquidation sale, we could realize significantly less than the value at which it is recorded.

Refer to Note 3 *Investments* for additional information regarding fair value measurements and our application of ASC 820.

---

### *Interest Income Recognition*

Interest income, adjusted for amortization of premiums, amendment fees and acquisition costs and the accretion of discounts, is recorded on the accrual basis to the extent that such amounts are expected to be collected. Generally, when a loan becomes 90 days or more past due, or if our qualitative assessment indicates that the debtor is unable to service its debt or other obligations, we will place the loan on non-accrual status and cease recognizing interest income on that loan until the borrower has demonstrated the ability and intent to pay contractual amounts due. However, we remain contractually entitled to this interest. Interest payments received on non-accrual loans may be recognized as income or applied to the cost basis, depending upon management's judgment. Generally, non-accrual loans are restored to accrual status when past-due principal and interest are paid, and, in management's judgment, are likely to remain current, or due to a restructuring, the interest income is deemed to be collectible. As of September 30, 2014, our loans to Tread Corp. ( Tread ) were on non-accrual, with an aggregate debt cost basis of \$12.0 million, or 4.0% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0. As of March 31, 2014, our loans to Tread were on non-accrual, with an aggregate debt cost basis of \$11.7 million, or 4.2% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0.

PIK interest, computed at the contractual rate specified in the loan agreement, is added to the principal balance of the loan and recorded as interest income. During the three and six months ended September 30, 2014, we recorded PIK income of \$29 and \$58, respectively. During the three and six months ended September 30, 2013, we recorded PIK income of \$29 and \$39, respectively.

### *Other Income Recognition*

We generally record success fees upon receipt of cash. Success fees are contractually due upon a change of control in a portfolio company. We recorded \$0.5 million of success fees for the three and six months ended September 30, 2014. During the three months ended September 30, 2014, we received success fees of \$0.2 million from each of Auto Safety House, LLC ( ASH ) and Frontier Packaging, Inc ( Frontier ) and \$0.1 million from Mathey Investments, Inc ( Mathey ). We recorded \$2.1 million and \$2.3 million of success fees during the three and six months ended September 30, 2013, respectively. During the three months ended September 30, 2013, we received \$0.3 million in success fee prepayments from Cavert II Holding Corp. ( Cavert ) and we received \$1.8 million related to the exit of Venyu Solutions, Inc. ( Venyu ).

We accrue dividend income on preferred and common equity securities to the extent that such amounts are expected to be collected and if we have the option to collect such amounts in cash or other consideration. For the three and six months ended September 30, 2014, we recorded \$1.4 million of dividend income from Mathey. For the three and six months ended September 30, 2013, we recorded \$1.4 million in dividend income related to the exit of Venyu.

Both dividend and success fee income are recorded in Other income in our accompanying *Condensed Consolidated Statements of Operations*.

### *Recent Accounting Pronouncements*

In June 2013, the FASB issued ASU 2013-08, *Financial Services - Investment Companies (Topic 946): Amendments to the Scope, Measurement, and Disclosure Requirements*, which amends the criteria that define an investment company and clarifies the measurement guidance and requires new disclosures for investment companies. Under ASU 2013-08, an entity already regulated under the 1940 Act is automatically an investment company under the new GAAP definition, so there was no impact from adopting this standard on our financial position or results of operations. We adopted ASU 2013-08 beginning with our quarter ended June 30, 2014, and have increased our disclosure requirements as necessary. We did not adopt any new accounting standards during the three months ending September 30, 2014.

### NOTE 3. INVESTMENTS

#### *Fair Value*

In accordance with ASC 820, our investments' fair value is determined to be the price that would be received for an investment in a current sale, which assumes an orderly transaction between market participants on the measurement date. This fair value definition focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. ASC 820 also establishes the following three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of a financial instrument as of the measurement date.

Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical financial instruments in active markets;

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

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs are those inputs that reflect assumptions that market participants would use when pricing the financial instrument and can include the Valuation Team's own assumptions based upon the best available information.

When a determination is made to classify our investments within Level 3 of the valuation hierarchy, such determination is based upon the significance of the unobservable factors to the overall fair value measurement. However, Level 3 financial instruments typically include, in addition to the unobservable, or Level 3, inputs, observable inputs (or, components that are actively quoted and can be validated to external sources). The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. As of September 30 and March 31, 2014, all of our investments were valued using Level 3 inputs and during the three and six months ended September 30, 2014 and 2013, there were no investments transferred in to or out of Level 1, 2 or 3.

The following table presents our investments carried at fair value as of September 30 and March 31, 2014, by caption on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* and by security type and input level on the ASC 820 fair value hierarchy:

	<b>Total Recurring Fair Value Measurement Reported in <i>Condensed Consolidated Statements of Assets and Liabilities</i></b>	
	<b>September 30, 2014</b>	<b>March 31, 2014</b>
<b>Non-Control/Non-Affiliate Investments</b>		
Senior debt	\$ 92,782	\$ 109,479
Senior subordinated debt	39,048	52,907
Preferred equity	23,360	32,259
Common equity/equivalents	17,780	10,795
<b>Total Non-Control/Non-Affiliate Investments</b>	<b>172,970</b>	<b>205,440</b>
<b>Affiliate Investments</b>		
Senior debt	99,916	60,391
Senior subordinated debt	16,906	2,400
Preferred equity	39,839	25,058
<b>Total Affiliate Investments</b>	<b>156,661</b>	<b>87,849</b>
<b>Control Investments</b>		
Senior subordinated debt	15,520	15,520
Preferred equity		5,584
Common equity/equivalents	1,750	
<b>Total Control Investments</b>	<b>17,270</b>	<b>21,104</b>
<b>Total Investments at fair value using Level 3 inputs</b>	<b>\$ 346,901</b>	<b>\$ 314,393</b>

In accordance with the FASB's ASU No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (IFRS)*, (ASU 2011-04), the following table provides quantitative information about our Level 3 fair value measurements of our investments as of September 30 and March 31, 2014. The below table is not intended to be all-inclusive, but rather provides information on the significant Level 3 inputs as they relate to our fair value measurements. The weighted average calculations in the table below are based on the principal balances for all debt-related calculations and on the cost basis for all equity-related calculations for the particular input.

**Quantitative Information about Level 3 Fair Value Measurements**

	Fair Value as of		Valuation Technique/ Methodology	Unobservable Input	Range / Weighted Average as of		Range / Weighted Average as of	
	September 30, 2014	March 31, 2014			September 30, 2014	March 31, 2014		
Senior debt	\$ 133,667	\$ 115,081	TEV	EBITDA multiples	3.6x	7.0x / 5.3x	4.6x	7.3x / 5.6x
	59,031	54,789	Yield Analysis	Discount Rate	8%	30% / 22%	8%	30% / 19%
Senior subordinated debt	47,320	49,470	TEV	EBITDA multiples	4.2x	7.1x / 5.5x	4.1x	7.3x / 5.0x
	24,154	21,357	Yield Analysis	Discount Rate	13%	17% / 16%	13%	13% / 13%
Preferred equity	63,199	62,901	TEV	EBITDA multiples	3.6x	8.7x / 5.8x	3.5x	8.5x / 5.1x
				EBITDA	\$344 - \$12,790	/\$3,744	\$36 - \$10,621	/\$4,266
Common equity/equivalents	19,530	10,795	TEV	EBITDA multiples	3.5x	18.0x / 11.0x	3.4x	16.0x / 10.5x
				EBITDA	\$197 - \$ 9,291	/\$5,018	\$36 - \$10,621	/\$6,008
<b>Total</b>	<b>\$ 346,901</b>	<b>\$ 314,393</b>						

Fair value measurements can be sensitive to changes in one or more of the valuation inputs. Changes in market yields, discounts rates, leverage, EBITDA or EBITDA multiples (or revenue or revenue multiples), each in isolation, may change the fair value of certain of our investments. Generally, an increase in market yields, discount rates or leverage or a decrease in EBITDA or EBITDA multiples (or revenue or revenue multiples) may result in a decrease in the fair value of certain of our investments.

The following tables provide the changes in fair value, broken out by security type, during the three and six months ended September 30, 2014 and 2013 for all of our investments.

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

	Senior Debt	Senior Subordinated Debt	Preferred Equity	Common Equity/Equivalents	Total
<b>Three months ended September 30, 2014:</b>					
Fair value as of June 30, 2014	\$ 177,599	\$ 70,382	\$ 60,934	\$ 12,917	\$ 321,832
Total (losses) gains:					
Net realized losses <sup>(A)(D)</sup>			(12)		(12)
Net unrealized (depreciation) appreciation <sup>(B)</sup>	(2,028)	29	(4,207)	4,711	(1,495)
New investments, repayments and settlements <sup>(C)</sup> :					
Issuances / Originations	17,127	1,805	6,472	1,902	27,306
Settlements / Repayments		(742)			(742)
Sales <sup>(D)</sup>			12		12



Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

<b>Fair value as of September 30, 2014</b>	<b>\$ 192,698</b>	<b>\$ 71,474</b>	<b>\$ 63,199</b>	<b>\$ 19,530</b>	<b>\$ 346,901</b>
<b>Six months ended September 30, 2014:</b>					
Fair value as of March 31, 2014	\$ 169,870	\$ 70,827	\$ 62,901	\$ 10,795	\$ 314,393
Total (losses) gains:					
Net realized losses <sup>(A)(D)</sup>			(12)		(12)
Net unrealized appreciation (depreciation) <sup>(B)</sup>	4,941	(1,445)	(6,365)	6,834	3,965
New investments, repayments and settlements <sup>(C)</sup> :					
Issuances / Originations	17,887	2,834	6,723	1,901	29,345
Settlements / Repayments		(742)	(60)		(802)
Sales <sup>(D)</sup>			12		12
<b>Fair value as of September 30, 2014</b>	<b>\$ 192,698</b>	<b>\$ 71,474</b>	<b>\$ 63,199</b>	<b>\$ 19,530</b>	<b>\$ 346,901</b>

	Senior Debt	Senior Subordinated Debt	Preferred Equity	Common Equity/ Equivalents	Total
<b>Three months ended September 30, 2013:</b>					
Fair value as of June 30, 2013	\$ 118,790	\$ 93,969	\$ 84,541	\$ 11,027	\$ 308,327
Total gains (losses):					
Net realized gains <sup>(A)(D)</sup>			24,804		24,804
Net unrealized appreciation (depreciation) <sup>(B)</sup>	438	(158)	(2,658)	4,068	1,690
Reversal of previously-recorded appreciation upon realization <sup>(B)</sup>			(17,374)		(17,374)
New investments, repayments and settlements <sup>(C)</sup> :					
Issuances / Originations	16,000	429	4,000		20,429
Settlements / Repayments	(360)	(19,500)			(19,860)
Sales <sup>(D)</sup>			(30,804)		(30,804)
<b>Fair value as of September 30, 2013</b>	<b>\$ 134,868</b>	<b>\$ 74,740</b>	<b>\$ 62,509</b>	<b>\$ 15,095</b>	<b>\$ 287,212</b>
<b>Six months ended September 30, 2013:</b>					
Fair value as of March 31, 2013	\$ 103,882	\$ 86,811	\$ 82,157	\$ 13,632	\$ 286,482
Total gains (losses):					
Net realized gains <sup>(A)(D)</sup>			24,804		24,804
Net unrealized (depreciation) appreciation <sup>(B)</sup>	(3,406)	(1,102)	(6,580)	1,370	(9,718)
Reversal of previously-recorded depreciation (appreciation) upon realization <sup>(B)</sup>	2		(17,374)		(17,372)
New investments, repayments and settlements <sup>(C)</sup> :					
Issuances / Originations	36,690	8,931	10,306	93	56,020
Settlements / Repayments	(2,300)	(19,900)			(22,200)
Sales <sup>(D)</sup>			(30,804)		(30,804)
<b>Fair value as of September 30, 2013</b>	<b>\$ 134,868</b>	<b>\$ 74,740</b>	<b>\$ 62,509</b>	<b>\$ 15,095</b>	<b>\$ 287,212</b>

- (A) Included in Net realized (loss) gain on our accompanying *Condensed Consolidated Statements of Operations* for the periods ended September 30, 2014 and 2013.
- (B) Included in Net unrealized (depreciation) appreciation on our accompanying *Condensed Consolidated Statements of Operations* for the periods ended September 30, 2014 and 2013.
- (C) Includes increases in the cost basis of investments resulting from new portfolio investments, the amortization of discounts, PIK and other non-cash disbursements to portfolio companies, as well as decreases in the cost basis of investments resulting from principal repayments or sales, the amortization of premiums and acquisition costs, and other cost-basis adjustments.
- (D) Included in Net realized (losses) gains and Sales are post-closing adjustments recorded in the current period related to exits from prior periods.

#### *Investment Activity*

During the six months ended September 30, 2014, the following significant transactions occurred:

In May 2014, NDLI Acquisition Inc. completed the purchase of certain of Noble Logistics, Inc.'s assets out of bankruptcy. The resulting entity was listed as one portfolio company under NDLI Inc. on our *Condensed Consolidated Schedules of Investments* beginning in the period ended June 30, 2014.

In August 2014, we made a \$1.8 million equity investment in Tread Real Estate Corp. ( TREC ), which purchased the building owned by another one of our portfolio companies, Tread. This building has subsequently been leased back to Tread.

In September 2014, we invested \$20.2 million in Cambridge Sound Management, Inc. ( CSM ) through a combination of debt and equity. CSM, based in Waltham, Massachusetts, is the developer of sound systems and solutions.

Refer to Note 13 *Subsequent Events* for significant portfolio activity that occurred after September 30, 2014.

*Investment Concentrations*

As of September 30, 2014, our investment portfolio consisted of investments in 30 portfolio companies located in 14 states across 15 different industries with an aggregate fair value of \$346.9 million, of which our investments in Acme Cryogenics, Inc. ( Acme ), SOG Specialty K&T, LLC ( SOG ), and CSM, our three largest portfolio investments at fair value, collectively comprised \$71.3 million, or 20.6%, of our total investment portfolio at fair value. The following table summarizes our investments by security type as of September 30 and March 31, 2014:

	September 30, 2014				March 31, 2014			
	Cost		Fair Value		Cost		Fair Value	
Senior debt	\$ 214,181	52.0%	\$ 192,698	55.5%	\$ 196,293	51.2%	\$ 169,870	54.0%
Senior subordinated debt	84,439	20.5	71,474	20.6	82,348	21.5	70,827	22.5
Total debt	298,620	72.5	264,172	76.1	278,641	72.7	240,697	76.5
Preferred equity	104,761	25.4	63,199	18.3	98,099	25.6	62,901	20.0
Common equity/equivalents	8,699	2.1	19,530	5.6	6,797	1.7	10,795	3.5
Total equity/equivalents	113,460	27.5	82,729	23.9	104,896	27.3	73,696	23.5
<b>Total Investments</b>	<b>\$ 412,080</b>	<b>100.0%</b>	<b>\$ 346,901</b>	<b>100.0%</b>	<b>\$ 383,537</b>	<b>100.0%</b>	<b>\$ 314,393</b>	<b>100.0%</b>

Investments at fair value consisted of the following industry classifications as of September 30 and March 31, 2014:

	September 30, 2014		March 31, 2014	
	Fair Value	Percentage of Total Investments	Fair Value	Percentage of Total Investments
Diversified/Conglomerate Manufacturing	\$ 54,626	15.7%	\$ 54,845	17.4%
Chemicals, Plastics, and Rubber	53,751	15.5	52,753	16.8
Home and Office Furnishings, Housewares, and Durable Consumer Products	39,888	11.5	21,188	6.7
Leisure, Amusement, Motion Pictures, Entertainment	37,070	10.7	39,867	12.7
Machinery (Non-agriculture, Non-construction, Non-electronic)	30,069	8.7	25,917	8.2
Farming and Agriculture	26,827	7.7	20,557	6.5
Automobile	25,049	7.2	25,735	8.2
Containers, Packaging, and Glass	18,333	5.3	17,889	5.7
Aerospace and Defense	15,520	4.5	18,512	5.9
Personal and Non-Durable Consumer Products (Manufacturing Only)	13,508	3.9	10,005	3.2

Edgar Filing: GLADSTONE INVESTMENT CORPORATION/DE - Form 10-Q

Cargo Transport	<b>12,390</b>	<b>3.6</b>	6,500	2.1
Beverage Food and Tobacco	<b>10,807</b>	<b>3.1</b>	13,050	4.2
Personal, Food and Miscellaneous Services	<b>7,313</b>	<b>2.1</b>	7,575	2.4
Buildings and Real Estate	<b>1,750</b>	<b>0.5</b>		
<b>Total Investments</b>	<b>\$ 346,901</b>	<b>100.0%</b>	\$ 314,393	100.0%

Investments at fair value were included in the following geographic regions of the U.S. as of September 30 and March 31, 2014:

	September 30, 2014		March 31, 2014	
	Fair Value	Percentage of Total Investments	Fair Value	Percentage of Total Investments
West	<b>\$ 122,276</b>	<b>35.2%</b>	\$ 117,781	37.5%
South	<b>101,950</b>	<b>29.4</b>	89,915	28.6
Northeast	<b>86,996</b>	<b>25.1</b>	67,862	21.6
Midwest	<b>35,679</b>	<b>10.3</b>	38,835	12.3
<b>Total Investments</b>	<b>\$ 346,901</b>	<b>100.0%</b>	\$ 314,393	100.0%

The geographic region indicates the location of the headquarters for our portfolio companies. A portfolio company may have additional business locations in other geographic regions.

*Investment Principal Repayments*

The following table summarizes the contractual principal repayment and maturity of our investment portfolio by fiscal year, assuming no voluntary prepayments, as of September 30, 2014:

		<b>Amount</b>
For the remaining six months ending		
March 31:	2015	\$ 43,144
For the fiscal year ending March 31:	2016	44,103
	2017	24,915
	2018	74,632
	2019	84,181
	Thereafter	27,645
	<b>Total contractual repayments</b>	<b>\$ 298,620</b>
	Investments in equity securities	113,460
	<b>Total cost basis of investments held at September 30, 2014:</b>	<b>\$ 412,080</b>

*Receivables from Portfolio Companies*

Receivables from portfolio companies represent non-recurring costs that we incurred on behalf of portfolio companies and are included in other assets on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. We maintain an allowance for uncollectible receivables from portfolio companies, which is determined based on historical experience and management's expectations of future losses. We charge the accounts receivable to the established provision when collection efforts have been exhausted and the receivables are deemed uncollectible. As of September 30 and March 31, 2014, we had gross receivables from portfolio companies of \$1.0 million and \$0.9 million, respectively. The allowance for uncollectible receivables was \$0.2 million as of September 30 and March 31, 2014.

**NOTE 4. RELATED PARTY TRANSACTIONS***Investment Advisory and Management Agreement*

We entered into an investment advisory and management agreement with the Adviser (the *Advisory Agreement*). The Adviser is controlled by our chairman and chief executive officer. In accordance with the *Advisory Agreement*, we pay the Adviser certain fees as compensation for its services, such fees consisting of a base management fee and an incentive fee, each as described below. On July 15, 2014, our Board of Directors approved the renewal of the *Advisory Agreement* through August 31, 2015.

The following table summarizes the management fees, loan servicing fees which are paid in accordance with our line of credit, incentive fees and associated credits reflected in our accompanying *Condensed Consolidated Statements of Operations*:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Average total assets subject to base management fee <sup>(A)</sup>	\$ 348,800	\$ 312,200	\$ 341,000	\$ 311,000
Multiplied by prorated annual base management fee of 2%	0.5%	0.5%	1.0%	1.0%
Base management fee <sup>(B)</sup>	1,744	1,561	3,410	3,110
Other credits to Adviser fees <sup>(B)</sup>	(606)	(334)	(988)	(845)
Net base management fee	\$ 1,138	\$ 1,227	\$ 2,422	\$ 2,265
Loan servicing fee <sup>(B)</sup>	1,158	1,116	2,293	2,141
Credit of loan servicing fee <sup>(B)</sup>	(1,158)	(1,116)	(2,293)	(2,141)
Net loan servicing fee	\$	\$	\$	\$
Incentive fee <sup>(B)</sup>	\$ 1,051	\$ 1,557	\$ 2,266	\$ 1,722

- (A) Average gross assets subject to the base management fee is defined as total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings, valued at the end of the applicable quarters within the respective periods and adjusted appropriately for any share issuances or repurchases during the periods.
- (B) Reflected as a line item on our accompanying *Condensed Consolidated Statement of Operations*.

**Base Management Fee**

The base management fee is computed and payable quarterly and is assessed at an annual rate of 2%. It is computed on the basis of the value of our average gross assets at the end of the two most recently completed quarters, which are total assets, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents resulting from borrowings. As a BDC, we make available significant managerial assistance to our portfolio companies and provide other services to such portfolio companies. Although neither we nor the Adviser receive fees in connection with managerial assistance, the Adviser provides other services to our portfolio companies and receives fees for these other services. 50% of certain of these fees and



100% of others historically have been credited against the base management fee that we would otherwise be required to pay to the Adviser. Effective October 1, 2013, 100% of all these fees are credited against the base management fee that we would otherwise be required to pay to the Adviser; however, pursuant to the terms of the Advisory Agreement, a small percentage of certain of such fees are retained by the Adviser in the form of reimbursement for certain tasks completed by personnel of the Adviser.

### **Loan Servicing Fee**

In addition, the Adviser services, administers and collects on the loans held by Business Investment, in return for which our

Adviser receives a 2% annual fee payable monthly by Business Investment based on the monthly aggregate balance of loans held by Business Investment in accordance with our line of credit. All loan servicing fees are credited back to us by the Adviser. Overall, the base management fee due to the Adviser cannot exceed 2% of total assets (as reduced by cash and cash equivalents pledged to creditors) during any given fiscal year.

### **Incentive Fee**

The incentive fee consists of two parts: an income-based incentive fee and a capital gains-based incentive fee. The income-based incentive fee rewards the Adviser if our quarterly net investment income (before giving effect to any incentive fee) exceeds 1.75% of our net assets (the hurdle rate). We will pay the Adviser an income-based incentive fee with respect to our pre-incentive fee net investment income in each calendar quarter as follows:

no incentive fee in any calendar quarter in which our pre-incentive fee net investment income does not exceed the hurdle rate (7.0% annualized);

100% of our 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

20% of the amount of our pre-incentive fee net investment income, if any, that exceeds 2.1875% in any calendar quarter (8.75% annualized).

The second part of the incentive fee is a capital gains-based incentive fee that will be determined and payable in arrears as of the end of each fiscal year (or upon termination of the Advisory Agreement, as of the termination date) and equals 20% of our realized capital gains as of the end of the fiscal year. In determining the capital gains-based incentive fee payable to the Adviser, we will calculate the cumulative aggregate realized capital gains and cumulative aggregate realized capital losses since our inception, and the aggregate net unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in our portfolio. For this purpose, cumulative aggregate realized capital gains, if any, equals the sum of the differences between the net sales price of each investment, when sold, and the original cost of such investment since our inception. Cumulative aggregate realized capital losses equals the sum of the amounts by which the net sales price of each investment, when sold, is less than the original cost of such investment since our inception. Aggregate net unrealized capital depreciation equals the sum of the difference, if negative, between the valuation of each investment as of the applicable calculation date and the original cost of such investment. At the end of the applicable year, the amount of capital gains that serves as the basis for our calculation of the capital gains-based incentive fee equals the cumulative aggregate realized capital gains less cumulative aggregate realized capital losses, less aggregate net unrealized capital depreciation, with respect

to our portfolio of investments. If this number is positive at the end of such year, then the capital gains-based incentive fee for such year equals 20% of such amount, less the aggregate amount of any capital gains-based incentive fees paid in respect of our portfolio in all prior years. No capital gains-based incentive fee has been recorded since our inception through September 30, 2014, as cumulative net unrealized capital depreciation has exceeded cumulative realized capital gains net of cumulative realized capital losses.

Additionally, in accordance with GAAP, a capital gains-based incentive fee accrual is calculated using the aggregate cumulative realized capital gains and losses and aggregate cumulative unrealized capital depreciation included in the calculation of the capital gains-based incentive fee plus the aggregate cumulative unrealized capital appreciation. If such amount is positive at the end of a period, then GAAP requires us to record a capital gains-based incentive fee equal to 20% of such amount, less the aggregate amount of actual capital gains-based incentive fees paid in all prior years. If such amount is negative, then there is no accrual for such year. GAAP requires that the capital gains-based incentive fee accrual consider the cumulative aggregate unrealized capital appreciation in the calculation, as a capital gains-based incentive fee would be payable if such unrealized capital appreciation were realized. There can be no assurance that such unrealized capital appreciation will be realized in the future. No GAAP accrual for a capital gains-based incentive fee has been recorded since our inception through September 30, 2014.

*Administration Agreement*

We have entered into an administration agreement (the *Administration Agreement* ) with the Administrator, whereby we pay for our allocable portion of the Administrator's expenses incurred while performing services to us, including, but not limited to, rent and the salaries and benefits expenses of the Administrator's employees, including our chief financial officer and treasurer, chief compliance officer, and general counsel and secretary (who also serves as the Administrator's president). Prior to July 1, 2014, our allocable portion was derived by multiplying that portion of the Administrator's expenses allocable to all funds managed by the Adviser by the percentage of our total assets at the beginning of each quarter in comparison to the total assets of all funds managed by the Adviser. As approved by our Board of Directors, effective July 1, 2014, our allocable portion of the Administrator's expenses will be derived by multiplying the Administrator's total expenses by the approximate percentage of time the Administrator's employees perform services for us in relation to their time spent performing services for all companies serviced by the Administrator under contractual agreements. On July 15, 2014, our Board of Directors approved the annual renewal of the Administration Agreement through August 31, 2015.

*Related Party Fees Due*

Amounts due to related parties on our accompanying Condensed Consolidated Statements of Assets and Liabilities were as follows:

	<b>As of September 30, 2014</b>	As of March 31 2014
Base management fee due to Adviser	\$ 259	\$ 63
Incentive fee due to Adviser	1,051	1,161
Other (from) due to Adviser	(3)	1
<b>Total fees due to Adviser</b>	<b>\$ 1,307</b>	<b>\$ 1,225</b>
<b>Fee due to Administrator</b>	<b>\$ 209</b>	<b>\$ 224</b>
<b>Total related party fees due</b>	<b>\$ 1,516</b>	<b>\$ 1,449</b>

**NOTE 5. BORROWINGS***Line of Credit*

On June 26, 2014, we, through our wholly-owned subsidiary, Business Investment, entered into Amendment No. 1 to the Fifth Amended and Restated Credit Agreement originally entered into on April 30, 2013, with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the *Administrative Agent* ), Branch Banking and Trust Company ( *BB&T* ) as a lender and managing agent, and the Adviser, as servicer, to extend the revolving period and reduce the interest rate of the line of credit (the *Credit Facility* ). The revolving period was extended 14 months to June 26, 2017, and if not renewed or extended by June 26, 2017, all principal and interest will be due and payable on or before June 26, 2019 (two years after the revolving period end date). In addition, we have retained the two one-year extension options, to be agreed upon by all parties, which may be exercised on or before June 26, 2015 and 2016, respectively, and upon exercise, the options would extend the revolving period to June 26, 2018 and 2019 and the maturity date to June 26, 2020 and 2021, respectively. Subject to certain terms and conditions, the Credit Facility can be expanded by up to \$145 million, to a total facility amount of \$250 million, through additional commitments of existing or new committed lenders. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.25% per annum, down from 3.75% prior to the amendment, and the Credit Facility includes a fee of 0.50% on

undrawn amounts. Once the revolving period ends, the interest rate margin increases to 3.75% for the period from June 26, 2017 to June 26, 2018, and further increases to 4.25% through maturity. We incurred fees of \$0.4 million in connection with this Amendment No 1.

On September 19, 2014, we further increased our borrowing capacity under the Credit Facility from \$105 million to \$185 million by entering into Joinder Agreements pursuant to the Credit Facility, by and among Business Investment, the Administrative Agent, the Adviser and each of East West Bank, Manufacturers and Traders Trust, Customers Bank and Talmer Bank and Trust. We incurred fees of \$0.8 million in connection with this expansion.

The following tables summarize noteworthy information related to our Credit Facility:

	<b>As of September 30, 2014</b>	<b>As of March 31, 2014</b>
Commitment amount	\$ <b>185,000</b>	\$ 105,000
Borrowings outstanding at cost	<b>87,750</b>	61,250
Commitment availability	<b>97,250</b>	43,750

	For the Three Months Ended		For the Six Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Weighted average borrowings outstanding	\$ 64,934	\$ 41,424	\$ 62,690	\$ 37,063
Effective interest rate <sup>(A)</sup>	3.9%	4.8%	4.1%	4.7%
Commitment (unused) fees incurred	\$ 65	\$ 81	\$ 121	\$ 133

(A) Excludes the impact of deferred financing fees.

Interest is payable monthly during the term of the Credit Facility. Available borrowings are subject to various constraints imposed under the Credit Facility, based on the aggregate loan balance pledged by Business Investment, which varies as loans are added and repaid, regardless of whether such repayments are prepayments or made as contractually required. Based on these constraints and pledged collateral, as of September 30, 2014, we had \$27.1 million in available borrowings.

The Administrative Agent also requires that any interest or principal payments on pledged loans be remitted directly by the borrower into a lockbox account with The Bank of New York Mellon Trust Company, N.A as custodian. The Administrative Agent is also the trustee of the account and remits the collected funds to us once a month.

Among other things, our Credit Facility contains covenants that require Business Investment to maintain its status as a separate legal entity, prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions) and restrict certain material changes to our credit and collection policies without the lenders' consent. Our Credit Facility generally also limits payments on distributions to the aggregate net investment income for each of the twelve month periods ending March 31, 2015, 2016 and 2017. Business Investment is also subject to certain limitations on the type of loan investments it can apply toward available credit in the borrowing base, including restrictions on geographic concentrations, sector concentrations, loan size, payment frequency and status, average life and lien property. Our Credit Facility further requires Business Investment to comply with other financial and operational covenants, which obligate Business Investment to, among other things, maintain certain financial ratios, including asset and interest coverage and a minimum number of obligors required in the borrowing base of the credit agreement. Additionally, we are subject to a performance guaranty that requires us to maintain (i) a minimum net worth (defined in our Credit Facility to include our mandatory redeemable term preferred stock) of \$170 million plus 50% of all equity and subordinated debt raised after April 30, 2013, which equates to \$170 million as of September 30, 2014, (ii) asset coverage with respect to senior securities representing indebtedness of at least 200%, in accordance with Section 18 of the 1940 Act and (iii) its status as a BDC under the 1940 Act and as a RIC under the Code. As of September 30, 2014, and as defined in the performance guaranty of our Credit Facility, we had a minimum net worth of \$264.8 million, an asset coverage of 264% and an active status as a BDC and RIC. Our Credit Facility requires a minimum of 12 obligors in the borrowing base and, as of September 30, 2014, Business Investment had 22 obligors. As of September 30, 2014, we continued to be in compliance with all covenants.

We have entered into an interest rate cap agreement with Keybank National Association that effectively limits the interest rate on a portion of our borrowings under the line of credit pursuant to the terms of our Credit Facility. The agreement, which expires April 2016, provides that the interest rate on \$45 million of our borrowings is capped at 6%, plus 3.25% per annum, when 30-day LIBOR is in excess of 6%.

#### *Secured Borrowing*

In August 2012, we entered into a participation agreement with a third-party related to \$5.0 million of our senior subordinated term debt investment in Ginsey Home Solutions, Inc. (Ginsey). In May 2014, we amended the agreement with the third-party to include an additional \$0.1 million. ASC 860 requires us to treat the participation as a financing-type transaction. Specifically, the third-party has a senior claim to our remaining investment in the event of

default by Ginsey which, in part, resulted in the loan participation bearing a rate of interest lower than the contractual rate established at origination. Therefore, our accompanying *Condensed Consolidated Statements of Assets and Liabilities* reflects the entire senior subordinated term debt investment in Ginsey and a corresponding \$5.1 million secured borrowing liability. The secured borrowing has a stated interest rate of 7.0% and a maturity date of January 3, 2018.

#### *Fair Value*

We elected to apply ASC 825, Financial Instruments, specifically for our Credit Facility, which was consistent with the application of ASC 820 to our investments. Generally, the Valuation Team estimates the fair value of our Credit Facility using a yield analysis, which includes a DCF calculation, and its own assumptions in the absence of observable market data, including estimated remaining life, counterparty credit risk, current market yield and interest rate spreads of similar securities as of the measurement date. During the three months ended September 30, 2014, due to the addition of four new lenders, amongst other things, cost was deemed to approximate fair value. At each of September 30 and March 31, 2014, all of our borrowings were valued using Level 3 inputs. The following tables present the short-term loan, where applicable, and Credit Facility carried at fair value as of September 30 and March 31, 2014, by caption on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* for Level 3 of the hierarchy established by ASC 820 and a roll-forward of the changes in fair value during the three and six months ended September 30, 2014 and 2013:

	<b>Level 3 Borrowings</b>	
	<b>Total Recurring Fair Value Measurement</b>	
	<b>Reported in <i>Condensed Consolidated</i></b>	
	<b><i>Statements of Assets and Liabilities</i></b>	
	<b>September 30, 2014</b>	<b>March 31, 2014</b>
Credit Facility	\$ 87,750	\$ 61,701

**Fair Value Measurements of Borrowings Using Significant**

**Unobservable Inputs (Level 3)**

	<b>Credit Facility</b>
<b>Three months ended September 30, 2014:</b>	
Fair value at June 30, 2014	\$ 62,950
Borrowings	30,500
Repayments	(5,700)
Net unrealized appreciation <sup>(A)</sup>	
<b>Fair value at September 30, 2014</b>	<b>\$ 87,750</b>
<b>Six months ended September 30, 2014:</b>	
Fair value at March 31, 2014	\$ 61,701
Borrowings	36,800
Repayments	(10,300)
Net unrealized depreciation <sup>(A)</sup>	(451)
<b>Fair value at September 30, 2014</b>	<b>\$ 87,750</b>

**Fair Value Measurements of Borrowings Using Significant**

**Unobservable Inputs (Level 3)**

	<b>Short-Term Loan</b>	<b>Credit Facility</b>	<b>Total</b>
<b>Three months ended September 30, 2013:</b>			
Fair value at June 30, 2013	\$ 26,009	\$ 49,000	\$ 75,009
Borrowings	22,005	43,000	65,005
Repayments	(26,009)	(58,000)	(84,009)
Net unrealized appreciation <sup>(A)</sup>		341	341
<b>Fair value at September 30, 2013</b>	<b>\$ 22,005</b>	<b>\$ 34,341</b>	<b>\$ 56,346</b>
<b>Six months ended September 30, 2013:</b>			
Fair value at March 31, 2013	\$ 58,016	\$ 31,854	\$ 89,870
Borrowings	48,014	71,500	119,514
Repayments	(84,025)	(68,500)	(152,525)
Net unrealized depreciation <sup>(A)</sup>		(513)	(513)
<b>Fair value at September 30, 2013</b>	<b>\$ 22,005</b>	<b>\$ 34,341</b>	<b>\$ 56,346</b>

(A) Included in net unrealized (depreciation) appreciation on our accompanying *Condensed Consolidated Statement of Operations* for periods ended September 30, 2014 and 2013.

The fair value of the collateral under our Credit Facility was \$315.7 million and \$288.6 million as of September 30 and March 31, 2014, respectively.

#### **NOTE 6. MANDATORILY REDEEMABLE PREFERRED STOCK**

In March 2012, we completed a public offering of 1,600,000 shares of 7.125% Series A Cumulative Term Preferred Stock (our Term Preferred Stock ) at a public offering price of \$25.00 per share. Gross proceeds totaled \$40 million and net proceeds, after deducting underwriting discounts and offering expenses borne by us, were \$38 million. We incurred \$2 million in total offering costs related to these transactions, which have been recorded as deferred financing costs on our accompanying *Condensed Consolidated Statements of Assets and Liabilities* and will be amortized over the redemption period ending February 28, 2017.

The shares have a redemption date of February 28, 2017, and are traded under the ticker symbol GAINP on the NASDAQ Global Select Market. The Term Preferred Stock is not convertible into our common stock or any other security. The Term Preferred Stock provides for a fixed dividend equal to 7.125% per year, payable monthly. We are required to redeem all of the outstanding Term Preferred Stock on February 28, 2017, for cash at a redemption price equal to \$25.00 per share, plus an amount equal to accumulated but unpaid dividends, if any, to, but excluding, the date of redemption. In addition, three other potential redemption triggers are as follows: (1) upon the occurrence of certain events that would constitute a change in control of us, we would be required to redeem all



of the outstanding Term Preferred Stock, (2) if we fail to maintain an asset coverage ratio of at least 200%, we are required to redeem a portion of the outstanding Term Preferred Stock or otherwise cure the ratio redemption trigger and (3) at our sole option, at any time on or after February 28, 2016, we may redeem some or all of the Term Preferred Stock.

For six months ended September 30, 2014 and 2013, our Board of Directors declared and paid a monthly distribution of \$0.1484375 per share, or \$0.8906250 per share in aggregate, to preferred stockholders. The tax character of distributions paid by us to preferred stockholders is from ordinary income.

In accordance with ASC 480, *Distinguishing Liabilities from Equity*, mandatorily redeemable financial instruments should be classified as liabilities on the balance sheet and, therefore, the related dividend payments are treated as dividend expense on our accompanying *Condensed Consolidated Statements of Operations* at the ex-dividend date. The fair value of the Term Preferred Stock, which we consider to be a level 1 liability within the fair value hierarchy, based on the last reported closing sale price as of September 30 and March 31, 2014, was \$42.1 million and \$42.4 million, respectively.

## NOTE 7. COMMON STOCK

### *Registration Statement*

We filed a registration statement on Form N-2 (File No. 333-181879) with the SEC on June 4, 2012, and subsequently filed a Pre-Effective Amendment No. 1 to the registration statement on July 17, 2012, which the SEC declared effective on July 26, 2012. On June 7, 2013, we filed Post-Effective Amendment No. 2 to the registration statement, which the SEC declared effective on July 26, 2013. On June 3, 2014, we filed Post-Effective Amendment No. 3 to the registration statement, and subsequently filed a Post-Effective Amendment No. 4 to the registration statement on September 2, 2014, which the SEC declared effective on September 4, 2014. The registration statement permits us to issue, through one or more transactions, up to an aggregate of \$300 million in securities, consisting of common stock, preferred stock, subscription rights, debt securities and warrants to purchase common stock, including through a combined offering of two or more of such securities.

## NOTE 8. NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS PER COMMON SHARE

The following table sets forth the computation of basic and diluted net increase in net assets resulting from operations per weighted average common share for the three and six months ended September 30, 2014 and 2013:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2014	2013	2014	2013
Numerator for basic and diluted net increase in net assets resulting from operations per common share	\$ 2,697	\$ 14,939	\$ 13,467	\$ 8,420
Denominator for basic and diluted weighted average common shares	26,475,958	26,475,958	26,475,958	26,475,958
<b>Basic and diluted net increase in net assets resulting from operations per average</b>	<b>\$ 0.10</b>	<b>\$ 0.57</b>	<b>\$ 0.51</b>	<b>\$ 0.32</b>

**common share****NOTE 9. DISTRIBUTIONS TO COMMON STOCKHOLDERS**

To qualify to be taxed as a RIC under Subtitle A, Chapter 1 of Subchapter M of the Code, we are required to distribute to our stockholders 90% of our investment company taxable income, which is generally our net ordinary income plus the excess of our net short-term capital gains over net long-term capital losses. The amount to be paid out as a distribution is determined by our Board of Directors each quarter and is based on management's estimate of our estimated taxable income. Based on that estimate, our Board of Directors declares three monthly distributions each quarter.

Our Board of Directors declared the following monthly distributions to common stockholders for the six months ended September 30, 2014 and 2013:

<b>Fiscal Year</b>	<b>Declaration Date</b>	<b>Record Date</b>	<b>Payment Date</b>	<b>Distribution per Common Share</b>
<b>2015</b>	April 8, 2014	April 21, 2014	April 30, 2014	<b>\$ 0.06</b>
	April 8, 2014	May 20, 2014	May 30, 2014	<b>0.06</b>
	April 8, 2014	June 19, 2014	June 30, 2014	<b>0.06</b>
	July 15, 2014	July 25, 2014	August 5, 2014	<b>0.06</b>
	July 15, 2014	August 20, 2014	August 29, 2014	<b>0.06</b>
	July 15, 2014	September 19, 2014	September 30, 2014	<b>0.06</b>
		<b>Six months ended September 30, 2014:</b>	<b>\$</b>	<b>0.36</b>

<b>Fiscal Year</b>	<b>Declaration Date</b>	<b>Record Date</b>	<b>Payment Date</b>	<b>Distribution per Common Share</b>
<b>2014</b>	April 9, 2013	April 22, 2013	April 30, 2013	\$ 0.05
	April 9, 2013	May 14, 2013	May 31, 2013	0.05
	April 9, 2013	June 19, 2013	June 28, 2013	0.05
	July 9, 2013	July 17, 2013	July 31, 2013	0.05
	July 9, 2013	August 19, 2013	August 30, 2013	0.05
	July 9, 2013	September 16, 2013	September 30, 2013	0.05
<b>Six months ended September 30, 2013:</b>				<b>\$ 0.30</b>

Aggregate common distributions declared quarterly and paid for the six months ended September 30, 2014 and 2013 were approximately \$9.5 million and \$7.9 million, respectively. We determine the tax characterization of our common distributions as of the end of our fiscal year based upon our taxable income for the full year and distributions paid during the full year. Therefore, a determination of tax attributes made on a quarterly basis may not be representative of the actual tax attributes of distributions for a full year. If we determined the tax attributes of our distributions as of September 30, 2014, 100% would be from ordinary income and 0% would be a return of capital. For the six months ended September 30, 2014, we recorded a \$0.2 million adjustment for estimated book-tax differences which decreased Capital in excess of par value and increased Net investment income in excess of distributions. For the fiscal year ended March 31, 2014, taxable income available for common distributions exceeded distributions declared and paid, and, in accordance with Section 855(a) of the Code, we elected to treat \$3.9 million of the first common distributions paid in fiscal year 2015, as having been paid in the prior year.

## **NOTE 10. COMMITMENTS AND CONTINGENCIES**

### *Legal Proceedings*

We are party to certain legal proceedings incidental to the normal course of our business, including the enforcement of our rights under contracts with our portfolio companies. We are required to establish reserves for litigation matters where those matters present loss contingencies that are both probable and estimable. When loss contingencies are not both probable and estimable, we do not establish reserves. Based on current knowledge, we do not believe that loss contingencies, if any, arising from pending investigations, litigation or regulatory matters will have a material adverse effect on our financial condition, results of operation or cash flows. Additionally, based on current knowledge, we do not believe such loss contingencies are probable and estimable and therefore, as of September 30, 2014, we have not established reserves for such loss contingencies.

### *Financial Commitments and Obligations*

As of September 30, 2014, we have lines of credit commitments to certain of our portfolio companies that have not been fully drawn. Since these lines of credit have expiration dates and we expect many will never be fully drawn, the total line of credit commitment amounts do not necessarily represent future cash requirements.

In addition to the lines of credit to certain portfolio companies, we have also extended certain guarantees on behalf of some of our portfolio companies. As of September 30, 2014, we have not been required to make any payments on the guarantees discussed below, and we consider the credit risk to be remote and the fair values of the guarantees to be minimal.

In February 2010, we executed a guarantee of a wholesale financing facility agreement (the Floor Plan Facility ) between Agricredit Acceptance, LLC ( Agricredit ) and Country Club Enterprises, LLC ( CCE ). The Floor Plan Facility provides CCE with financing of up to \$2.0 million to bridge the time and cash flow gap between the order and delivery of golf carts to customers. The guarantee was renewed in February 2011, 2012, 2013 and 2014 and expires in February 2015, unless it is renewed again by us, CCE and Agricredit. In connection with this guarantee and its subsequent renewals, we recorded aggregate premiums of \$0.4 million from CCE.

In April 2010, we executed a guarantee of vendor recourse for up to \$2.0 million in individual customer transactions (the Recourse Facility ) between Wells Fargo Financial Leasing, Inc. and CCE. The Recourse Facility provides CCE with the ability to provide vendor recourse up to a limit of \$2.0 million on transactions with long-time customers who lack the financial history to qualify for third-party financing. The terms to maturity of these individual transactions range from October 2014 to October 2016. In connection with this guarantee, we received aggregate premiums of \$0.1 million from CCE.

The following table summarizes the dollar balance of unused line of credit commitments and guarantees as of September 30 and March 31, 2014:

	<b>September 30, 2014</b>	<b>March 31, 2014</b>
Unused line of credit commitments	\$ 2,716	\$ 6,684
Guarantees	2,716	3,628
<b>Total</b>	<b>\$ 5,432</b>	<b>\$ 10,312</b>

*Escrow Holdbacks*

From time to time, we will enter into arrangements relating to exits of certain investments whereby specific amounts of the proceeds are held in escrow to be used to satisfy potential obligations, as stipulated in the sales agreements. We record escrow amounts in restricted cash on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. In August 2013, the sale of Venyu resulted in \$4.9 million in escrow amounts, of which \$0.6 million is held on behalf of the other sellers, which we record in other liabilities on our accompanying *Condensed Consolidated Statements of Assets and Liabilities*. In September 2014, \$1.9 million of the escrow funds related to were released. As of September 30, 2014, there remains \$2.9 million in escrow amounts, of which \$0.6 million is held on behalf of the sellers, related to the sale of Venyu. We establish a contingent liability against the escrow amounts if we determine that it is probable and estimable that a portion of the escrow amounts will not be ultimately received at the end of the escrow period. The aggregate contingent liability recorded against the escrow amounts was \$35 for both September 30 and March 31, 2014.

**NOTE 11. FINANCIAL HIGHLIGHTS**

	Three Months Ended September 30, 2014		Six Months Ended September 30, 2013	
	2014	2013	2014	2013
<b>Per Common Share Data</b>				
NAV at beginning of period <sup>(A)</sup>	\$ 8.57	\$ 8.70	\$ 8.34	\$ 9.10
Net investment income <sup>(B)</sup>	0.16	0.24	0.34	0.39
Realized gain on sale of investments and other <sup>(B)</sup>		0.94		0.94
Net unrealized (depreciation) appreciation of investments and other <sup>(B)</sup>	(0.06)	(0.61)	0.17	(1.01)
Total from investment operations <sup>(B)</sup>	0.10	0.57	0.51	0.32
Cash distributions from net investment income <sup>(B)(C)</sup>	(0.18)	(0.15)	(0.36)	(0.30)
NAV at end of period <sup>(A)</sup>	\$ 8.49	\$ 9.12	\$ 8.49	\$ 9.12
<b>Per common share market value</b>				
at beginning of period	\$ 7.40	\$ 7.35	\$ 8.27	\$ 7.31
at end of period	7.11	7.05	7.11	7.05
Total return <sup>(D)</sup>	(1.55)%	(2.02)%	(9.82)%	0.54%
Common stock outstanding at end of period	26,475,958	26,475,958	26,475,958	26,475,958
<b>Statement of Assets and Liabilities Data:</b>				
Net assets at end of period	\$ 224,773	\$ 241,440	\$ 224,773	\$ 241,440
Average net assets <sup>(E)</sup>	227,307	237,871	225,013	237,509
<b>Senior Securities Data<sup>(F)</sup>:</b>				
Total borrowings, at cost	\$ 92,846	\$ 61,005	\$ 92,846	\$ 61,005

Mandatorily redeemable preferred stock	<b>40,000</b>	40,000	<b>40,000</b>	40,000
Asset coverage ratio <sup>(G)</sup>	<b>264%</b>	328%	<b>264%</b>	328%
Average coverage per unit <sup>(H)</sup>	\$ <b>2,636</b>	\$ 3,276	\$ <b>2,636</b>	\$ 3,276
<b>Ratios/Supplemental Data:</b>				
Ratio of expenses to average net assets <sup>(I)(J)(L)</sup>	<b>11.67%</b>	11.07%	<b>11.67%</b>	9.67%
Ratio of net expenses to average net assets <sup>(I)(K)</sup>	<b>8.56</b>	8.63	<b>8.75</b>	7.15
Ratio of net investment income to average net assets <sup>(I)</sup>	<b>7.40</b>	10.47	<b>8.06</b>	8.64

- (A) Based on actual common shares outstanding at the end of the corresponding period.
- (B) Based on weighted average per basic common share data.
- (C) Distributions are determined based on taxable income calculated in accordance with income tax regulations, which may differ from amounts determined under GAAP.
- (D) Total return equals the change in the market value of our common stock from the beginning of the period, taking into account dividends reinvested in accordance with the terms of our dividend reinvestment plan. Total return does not take into account distributions that may be characterized as a return of capital. For further information on the estimated character of our distributions to common stockholders, please refer to Note 9 *Distributions to Common Stockholders*.
- (E) Calculated using the average balance of net assets at the end of each month of the reporting period.
- (F) The 1940 Act currently permits BDCs to issue senior securities representing indebtedness and senior securities that are stock, to which we refer as senior securities.
- (G) As a BDC, we are generally required to maintain an asset coverage ratio (as defined in Section 18(h) of the 1940 Act) of at least 200% on our senior securities representing indebtedness and our senior securities that are stock. Our mandatorily redeemable preferred stock is a senior security that is stock.
- (H) Asset coverage per unit is the asset coverage ratio expressed in terms of dollar amounts per one thousand dollars of indebtedness.
- (I) Amounts are annualized.
- (J) Ratio of expenses to average net assets is computed using expenses before credits from the Adviser.
- (K) Ratio of net expenses to average net assets is computed using total expenses net of any credits received from the Adviser.
- (L) The ratio of expenses to average net assets for the three and six months ended September 30, 2013 were revised from the previously reported ratios, which were 9.19% and 7.87% ,respectively, to correct an error as discussed in footnote 2.

**NOTE 12. UNCONSOLIDATED SIGNIFICANT SUBSIDIARIES**

In accordance with the SEC's Regulation S-X, we have one unconsolidated subsidiary, Galaxy Tool Holdings, Inc. ( Galaxy ), that met at least one of the significance conditions of the SEC's Regulation S-X as of September 30, 2014 and 2013 and for the six months ended September 30, 2014 and 2013. Additionally, we have one unconsolidated subsidiary, SOG Specialty K&T, LLC ( SOG ), and one former unconsolidated subsidiary, Venyu Solutions Inc. ( Venyu ), which met at least one of the significance conditions of the SEC's Regulation S-X for the six months ended September 30, 2013. Accordingly, summarized, comparative financial information, in aggregate, is presented below for our significant unconsolidated subsidiaries.

<b>Income Statement<sup>(A)</sup></b>	<b>For the Six Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
Net Sales	\$ 32,746	\$ 46,573
Gross Profit	9,066	17,017
Net loss	(1,700)	294

(A) Reflects only four months of summarized income statement information of Venyu in 2013, as it was exited in August 2013.

**NOTE 13. SUBSEQUENT EVENTS***New Investment*

In October 2014, we invested \$24.4 million in Old World Christmas, Inc. ( OWC ) through a combination of debt and equity. OWC, headquartered in Spokane, Washington, is a designer and distributor of an extensive collection of blown glass Christmas ornaments, table top figurines, vintage-style light covers and nostalgic greeting cards into the independent gift channel.

*Distributions*

On October 7, 2014, our Board of Directors declared the following monthly cash distributions to common and preferred stockholders:

<b>Declaration Date</b>	<b>Record Date</b>	<b>Payment Date</b>	<b>Distribution per</b>	
			<b>Common Share</b>	<b>Distribution per Term Preferred Share</b>
October 7, 2014	October 22, 2014	October 31, 2014	\$ 0.06	\$ 0.1484375
October 7, 2014	November 17, 2014	November 26, 2014	0.06	0.1484375
October 7, 2014	December 19, 2014	December 31, 2014	0.06	0.1484375
<b>Total for the Quarter:</b>			<b>\$ 0.18</b>	<b>\$ 0.4453125</b>

Additionally, on October 7, 2014, our Board of Directors declared the following one-time special cash distribution to common stockholders:

<b>Declaration Date</b>	<b>Record Date</b>	<b>Payment Date</b>	<b>Distribution per Common Share</b>
October 7, 2014	December 19, 2014	December 31, 2014	\$ <b>0.05</b>

This represents the third calendar year in a row that a one-time special cash distribution to common stockholders has been declared by our Board of Directors.



---

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

All statements contained herein, other than historical facts, may constitute forward-looking statements. These statements may relate to, among other things, our future operating results, our business prospects and the prospects of our portfolio companies, actual and potential conflicts of interest with Gladstone Management Corporation and its affiliates, the use of borrowed money to finance our investments, the adequacy of our financing sources and working capital, and our ability to co-invest, among other factors. In some cases, you can identify forward-looking statements by terminology such as estimate, may, might, believe, will, provided, anticipate, future, could, growth, plan, intend, expect, should, would, if, seek, possible, negative of such terms or comparable terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others: (1) further adverse changes in the economy and the capital markets; (2) risks associated with negotiation and consummation of pending and future transactions; (3) the loss of one or more of our executive officers, in particular David Gladstone, Terry Lee Brubaker or David A.R. Dullum; (4) changes in our investment objectives and strategy; (5) availability, terms and deployment of capital; (6) changes in our industry, interest rates, exchange rates or the general economy; (7) the degree and nature of our competition; (8) our ability to maintain our qualification as a RIC and as business development company; and (9) those factors described in the Risk Factors section of our Annual Report on Form 10-K filed with the SEC on May 13, 2014. We caution readers not to place undue reliance on any such forward-looking statements. Actual results could differ materially from those anticipated in our forward-looking statements and future results could differ materially from historical performance. We have based forward-looking statements on information available to us on the date of this report. Except as required by the federal securities laws, we undertake no obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this Quarterly Report on Form 10-Q. Although we undertake no obligation to revise or update any forward-looking statements, 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 have filed or in the future may file with the Securities and Exchange Commission ( SEC ), including annual reports on Form 10-K, quarterly 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 accompanying *Condensed Consolidated Financial Statements* and the notes thereto contained elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014, filed with the SEC on May 13, 2014. Historical financial condition and results of operations and percentage relationships among any amounts in the financial statements are not necessarily indicative of financial condition or results of operations for any future periods.

### OVERVIEW

#### General

We are an externally-managed, closed-end, non-diversified management investment company that has elected to be regulated as a business development company ( BDC ) under the Investment Company Act of 1940, as amended (the 1940 Act ). In addition, for United States ( U.S. ) federal income tax purposes, we have elected to be treated as a regulated investment company ( RIC ) under Subchapter M of the Internal Revenue Code of 1986, as amended (the Code ). As a BDC and a RIC, we are also subject to certain constraints, including limitations imposed by the 1940 Act and the Code.

We were incorporated under the General Corporation Law of the State of Delaware on February 18, 2005. We were established for the purpose of investing in debt and equity securities of established private businesses in the U.S. Debt investments primarily come in the form of three types of loans: senior term loans, senior subordinated loans and junior subordinated debt. Equity investments primarily take the form of preferred or common equity (or warrants or options to acquire the foregoing), often in connection with buyouts and other recapitalizations. To a much lesser extent, we also invest in senior and subordinated syndicated loans. Our investment objectives are (a) to achieve and grow current income by investing in debt securities of established businesses that we believe will provide stable earnings and cash flow to pay expenses, make principal and interest payments on our outstanding indebtedness and make distributions to stockholders that we anticipate will grow over time and (b) to provide our stockholders with long-term capital appreciation in the value of our assets by investing in equity securities of established businesses that we hope will appreciate over time so that we can sell them for capital gains. We expect that our investment allocation over time will consist of approximately 80% in debt securities and 20% in equity securities. As of September 30, 2014, our investment allocation was 72% in debt securities and 28% in equity securities, at cost.

We focus on investing in small and medium-sized private U.S. businesses that meet certain of the following criteria which we believe will give us the best potential to sell our equity positions at a later date for capital gains: the potential for growth in cash flow, adequate assets for loan collateral, experienced management teams with a significant ownership interest in the borrower, profitable operations based on the borrower's cash flow and reasonable capitalization of the borrower (usually by leveraged buyout funds or venture capital funds). We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering of the borrower's stock or by exercising our right to require the borrower to repurchase our warrants, though there can be no assurance that we will always have these rights. We lend to borrowers that need funds to finance growth, restructure their balance sheets or effect a change of control. We invest by ourselves or jointly with other funds and/or management of the portfolio company, depending on the opportunity. If we are participating in an investment with one or more co-investors, our investment is likely to be smaller than if we were investing alone.

Our common stock and 7.125% Series A Cumulative Term Preferred Stock (our Term Preferred Stock) are traded on the NASDAQ Global Select Market (NASDAQ) under the symbols GAIN and GAINP, respectively.

We are externally managed by our investment advisor, Gladstone Management Corporation (the Adviser), an SEC registered investment adviser and an affiliate of ours, pursuant to an investment advisory and management agreement (the Advisory Agreement). The Adviser manages our investment activities. Our Board of Directors, which is composed of a majority of independent directors, supervises such investment activities. We have also entered into an administration agreement (the Administration Agreement) with Gladstone Administration, LLC (our Administrator), an affiliate of ours and the Adviser, whereby we pay separately for administrative services.

## **Business Environment**

The strength of the global economy, and the U.S. economy in particular, continues to be uncertain and volatile, and we remain cautious about a long-term economic recovery. The effects of the previous recession and the disruptions in the capital markets have impacted our liquidity options and increased our cost of debt and equity capital. In addition, the federal government shutdown in October 2013 combined with the uncertainty surrounding the ability of the federal government to address its fiscal condition in both the short and long term have increased domestic and global economic instability. Many of our portfolio companies, as well as those that we evaluate for possible investments, are adversely impacted by these political and economic conditions. If these conditions persist, it may adversely affect their ability to repay our loans or engage in a liquidity event, such as a sale, recapitalization or initial public offering.

### *Portfolio Activity*

While conditions remain challenging, we are seeing an increase in the number of new investment opportunities consistent with our investing strategy of providing a combination of debt and equity in support of management and sponsor-led buyouts of small and medium-sized companies in the U.S. During the three months ended September 30, 2014, we invested a total of \$21.9 million in two new deals, and subsequent to September 30, 2014, we invested \$24.4 million in another new deal. These new investments, along with the capital raising efforts discussed below, have allowed us to invest \$356.4 million in 22 new proprietary debt and equity deals since October 2010.

These new investments, as well as the majority of our debt securities in our portfolio, have a success fee component, which enhances the yield on our debt investments. Unlike paid-in-kind (PIK) income, we generally do not recognize success fees as income until they are received in cash. Due to their contingent nature, there are no guarantees that we will be able to collect any or all of these success fees or know the timing of such collections. As a result, as of September 30, 2014, we had unrecognized success fees of \$21.0 million, or \$0.79 per common share, which do not meet the recognition criteria under the relevant accounting guidance.

The improved investing environment presented us with an opportunity to realize gains and other income from our investment in Venyu Solutions, Inc. ( Venyu ) as a result of its sale in August 2013. As a result of the sale, we received net cash proceeds of \$32.2 million, resulting in a realized gain of \$24.8 million and dividend income of \$1.4 million. In addition, we received full repayment of our debt investments of \$19 million and \$1.8 million in success fee income. This represents our fourth management-supported buyout liquidity event since June 2010, and in the aggregate, these four liquidity events have generated \$54.5 million in realized gains and \$13.1 million in other income, for a total increase to our net assets of \$67.6 million. We believe each of these transactions was an equity-oriented investment success and exemplify our investment strategy of striving to achieve returns through current income on the debt portion of our investments and capital gains from the equity portion. These successes, in part, enabled us to increase the monthly distribution 50% since March 2011, allowed us to declare and pay a \$0.03 per common share one-time special distribution in fiscal year 2012, a \$0.05 per common share one-time special distribution in November 2013, and a \$0.05 per common share one-time special distribution payable in December 2014.

With the four liquidity events that have generated \$54.5 million in realized gains since June 2010, we have nearly overcome our cumulative realized losses since inception that were primarily incurred during the recession and in connection with the sale of performing loans at a realized loss to pay off a former lender. We took the opportunity during the fiscal year ended March 31, 2014, to strategically sell our investments in two of our portfolio companies, ASH Holding Corp. ( ASH ) and Packerland Whey Products, Inc. ( Packerland ) to existing members of their management teams and other existing owners, respectively, which resulted in realized losses of \$11.4 million and \$1.8 million, respectively, as well as the write off our equity investments in Noble Logistics, Inc. ( Noble ), which resulted in a realized loss of \$3.4 million. These sales and write off, while at a realized loss, were accretive to our net asset value in aggregate by \$5.7 million, reduced our distribution requirements related to our realized gains and reduced our non-accruals outstanding.

### *Capital Raising Efforts*

Despite the challenges that have existed in the economy for the past several years, we have been able to meet our capital needs through increases to our revolving line of credit (our Credit Facility ) and by accessing the capital markets in the form of public offerings of stock. For example, in October 2012, we issued 4.4 million shares of common stock for gross proceeds of \$33 million. Regarding our Credit Facility over the last two years, we have successfully extended the revolving period multiple times, most recently to June 2017, increased the commitment from \$60 million to \$185 million and reduced the interest rate margin from 3.75% to 3.25%.

Although we were able to access the capital markets during 2012, we believe market conditions continue to affect the trading price of our common stock and thus our ability to finance new investments through the issuance of equity. On October 27, 2014, the closing market price of our common stock was \$7.27, which represented a 14.4% discount to our September 30, 2014 net asset value ( NAV ) per share of \$8.49. When our stock trades below NAV, our ability to issue equity is constrained by provisions of the 1940 Act, which generally prohibit the issuance and sale of our common stock at an issuance price below the then current NAV per share without stockholder approval, other than through sales to our then-existing stockholders pursuant to a rights offering.

At our 2014 Annual Meeting of Stockholders held on August 7, 2014, our stockholders approved a proposal authorizing us to issue and sell shares of our common stock at a price below our then current NAV per share, subject to certain limitations, including that the number of shares issued and sold pursuant to such authority does not exceed 25% of our then outstanding common stock immediately prior to each such sale, provided that our Board of Directors makes certain determinations prior to any such sale. This August 2014 stockholder authorization is in effect for one year from the date of stockholder approval. Prior to the August 2014 stockholder authorization, we sought and obtained stockholder approval concerning a similar proposal at the Annual Meeting of Stockholders held in August 2012, and with our Board of Directors subsequent approval, we issued shares of our common stock in October and November 2012 at a price per share below the then current NAV per share. The resulting proceeds, in part, have allowed us to grow the portfolio by making new investments, generate additional income through these new investments, provide us additional equity capital to help ensure continued compliance with regulatory tests and increase our debt capital while still complying with our applicable debt-to-equity ratios.

### *Regulatory Compliance*

Our ability to seek external debt financing, to the extent that it is available under current market conditions, is further subject to the asset coverage limitations of the 1940 Act, which require us to have an asset coverage ratio (as defined in Section 18(h) of the 1940 Act), of at least 200% on our senior securities representing indebtedness and our senior securities that are stock, which we refer to collectively as Senior Securities. As of September 30, 2014, our asset coverage ratio was 264%. Our status as a RIC under Subchapter M of the Code, in addition to other requirements, also requires us, at the close of each quarter of the taxable year, to meet an asset diversification test, which requires that at least 50% of the value of our assets consists of cash, cash items, U.S. government securities or certain other qualified

securities (the 50% threshold ). In the past, we have obtained this ratio by entering into a short-term loan at quarter end to purchase qualifying assets; however, a short term loan was not necessary at the end of the quarter ended September 30, 2014. Until the composition of our assets is above the required 50% threshold on a consistent basis by a significant margin, we may have to continue to obtain short-term loans on a quarterly basis. When deployed, this strategy, while allowing us to satisfy the 50% threshold for our RIC status, limits our ability to use increased debt capital to make new investments, due to our asset coverage ratio limitations under the 1940 Act.

## Investment Highlights

During the six months ended September 30, 2014, we disbursed \$21.9 million in new debt and equity investments and extended \$7.4 million of investments to existing portfolio companies through revolver draws or additions to term notes. From our initial public offering in June 2005 through September 30, 2014, we have made 221 investments in 109 companies for a total of approximately \$956.9 million, before giving effect to principal repayments on investments and divestitures.

### *Investment Activity*

During the six months ended September 30, 2014, the following significant transactions occurred:

In May 2014, NDLI Acquisition Inc. completed the purchase of certain of Noble's assets out of bankruptcy. The resulting entity was listed as one portfolio company under NDLI Inc. on our *Condensed Consolidated Schedules of Investments* beginning in the period ended June 30, 2014.

In August 2014, we made a \$1.8 million equity investment in Tread Real Estate Corp. ( TREC ), which purchased the building owned by another one of our portfolio companies, Tread. This building has subsequently been leased back to Tread.

In September 2014, we invested \$20.2 million in Cambridge Sound Management, Inc. ( CSM ) through a combination of debt and equity. CSM, based in Waltham, Massachusetts, is the developer of sound systems and solutions.

Subsequent to September 30, 2014, the following significant transaction occurred:

In October 2014, we invested \$24.4 million in Old World Christmas, Inc. ( OWC ) through a combination of debt and equity. OWC, headquartered in Spokane, Washington, is a designer and distributor of an extensive collection of blown glass Christmas ornaments, table top figurines, vintage-style light covers and nostalgic greeting cards into the independent gift channel.

## Recent Developments

### *Credit Facility Extension and Expansion*

On June 26, 2014, we, through our wholly-owned subsidiary, Business Investment, entered into Amendment No. 1 to the Fifth Amended and Restated Credit Agreement originally entered into on April 30, 2013, with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the Administrative Agent ), Branch Banking and Trust Company ( BB&T ) as a lender and managing agent, and the Adviser, as servicer, to extend the revolving period and reduce the interest rate of the line of credit. The revolving period was extended 14 months to June 26, 2017, and if not renewed or extended by June 26, 2017, all principal and interest will be due and payable on or before June 26, 2019 (two years after the revolving period end date). In addition, we have retained the two one-year extension options, to be agreed upon by all parties, which may be exercised on or before June 26, 2015 and 2016, respectively, and upon exercise, the options would extend the revolving period to June 26, 2018 and 2019 and the maturity date to June 26, 2020 and 2021, respectively. Subject to certain terms and conditions, the Credit Facility can be expanded by up to \$145 million, to a total facility amount of \$250 million, through additional commitments of existing or new committed

lenders. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.25% per annum, down from 3.75% prior to the amendment, and the Credit Facility includes an unused fee of 0.50% on undrawn amounts. Once the revolving period ends, the interest rate margin increases to 3.75% for the period from June 26, 2017 to June 26, 2018, and further increases to 4.25% through maturity. We incurred fees of \$0.4 million in connection with this amendment.

On September 19, 2014, we further increased our borrowing capacity under the Credit Facility from \$105 million to \$185 million by entering into Joinder Agreements pursuant to the Credit Facility, by and among Business Investment, the Administrative Agent, the Adviser and each of East West Bank, Manufacturers and Traders Trust, Customers Bank and Talmer Bank and Trust. We incurred fees of \$0.8 million in connection with this expansion.



**RESULTS OF OPERATIONS***Comparison of the Three Months Ended September 30, 2014, to the Three Months Ended September 30, 2013*

	For the Three Months Ended September 30,			
	2014	2013	\$ Change	% Change
<b>INVESTMENT INCOME</b>				
Interest income	\$ 8,570	\$ 7,706	\$ 864	11.2%
Other income	501	3,653	(3,152)	(86.3)
Total investment income	9,071	11,359	(2,288)	(20.1)
<b>EXPENSES</b>				
Base management fee	1,744	1,561	183	11.7
Incentive fee	1,051	1,557	(506)	(32.5)
Administration fee	209	156	53	34.0
Interest and dividend expense	1,432	1,309	123	9.4
Amortization of deferred financing costs	282	256	26	10.2
Other	755	626	129	20.6
Expenses before credits from Adviser	5,473	5,465	8	0.1
Other credits to Adviser fees	(606)	(334)	(272)	(81.4)
Total expenses net of credits to fees	4,867	5,131	(264)	(5.1)
<b>NET INVESTMENT INCOME</b>	<b>4,204</b>	<b>6,228</b>	<b>(2,024)</b>	<b>(32.5)</b>
<b>UNREALIZED (LOSS) GAIN:</b>				
Net realized (loss) gain on investments	(12)	24,804	(24,816)	NM
Net unrealized depreciation of investments	(1,495)	(15,684)	14,189	(90.5)
Net unrealized depreciation of other		(409)	409	100.0
Net realized and unrealized (loss) gain on investments and other	(1,507)	8,711	(10,218)	NM
<b>NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS</b>	<b>\$ 2,697</b>	<b>\$ 14,939</b>	<b>\$(12,242)</b>	<b>(81.9)</b>
<b>BASIC AND DILUTED PER COMMON SHARE:</b>				
Net investment income	\$ 0.16	\$ 0.24	\$ (0.08)	(33.3)%
Net increase in net assets resulting from operations	\$ 0.10	\$ 0.57	\$ (0.47)	(82.5)

NM = Not Meaningful

**Investment Income**

Total investment income decreased by 20.1% for the three months ended September 30, 2014, as compared to the prior year period. This decrease was due to a decrease in other income, which primarily consisted of success fee and dividend income resulting from our exit of Venyu during the three months ended September 30, 2013. The decrease in other income was partially offset by an increase in interest income resulting from an increase in the size of our portfolio during the three months ended September 30, 2014.

Interest income from our investments in debt securities increased 11.2% for the three months ended September 30, 2014, as compared to the prior year period. The level of interest income from investments is directly related to the principal balance of our interest-bearing investment portfolio outstanding during the period multiplied by the weighted average yield. The weighted average principal balance of our interest-bearing investment portfolio during the three months ended September 30, 2014, was approximately \$270.9 million, compared to approximately \$242.8 million for the prior year period. This increase was primarily due to approximately \$92.9 million in new investments originated after September 30, 2013, including Alloy Die Casting Corp. ( ADC ), Behrens Manufacturing, LLC ( Behrens ), Meridian Rack & Pinion, Inc. ( Meridian ), Head Country Inc. ( Head Country ), Edge Adhesives Holdings, Inc. ( Edge ), TREC, and CSM. At September 30, 2014, loans of one portfolio company, Tread Corp. (Tread ), were on non-accrual, with an aggregate weighted average principal balance of \$12.0 million. At September 30, 2013, loans to two portfolio companies, ASH and Tread, were on non-accrual, with an aggregate weighted average principal balance of \$26.1 million during the three months ended September 30, 2013. The weighted average yield on our interest-bearing investments was 12.6% for the three months ended September 30, 2014 and 2013, excluding cash and cash equivalents and receipts recorded as other income. The weighted average yield varies from period to period, based on the current stated interest rate on interest-bearing investments.

The following table lists the investment income for our five largest portfolio company investments based on fair value during the respective periods:

Portfolio Company	As of September 30, 2014		Three months ended September 30, 2014	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,139	7.8%	\$ 426	4.7%
SOG Specialty Knives and Tools, LLC	23,989	6.9	670	7.4
Cambridge Sound Management, LLC <sup>(A)</sup>	20,175	5.8	6	0.1
Jackrabbit, Inc.	19,327	5.6	380	4.2
Edge Adhesives Holdings, Inc.	18,074	5.2	440	4.9
<b>Subtotal five largest investments</b>	<b>108,704</b>	<b>31.3</b>	<b>1,922</b>	<b>21.3</b>
Other portfolio companies	238,197	68.7	7,149	78.7
<b>Total investment portfolio</b>	<b>\$ 346,901</b>	<b>100.0%</b>	<b>\$ 9,071</b>	<b>100.0%</b>

Portfolio Company	As of September 30, 2013		Three months ended September 30, 2013	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,771	9.7%	\$ 426	3.8%
Galaxy Tool Holding Corp.	24,156	8.4	535	4.7
SOG Specialty Knives and Tools, LLC	24,131	8.4	670	5.9
Schylling Investments, LLC <sup>(A)</sup>	20,000	7.0	312	2.7
Channel Technologies Group, LLC	19,642	6.8	468	4.1
<b>Subtotal five largest investment<sup>(B)</sup></b>	<b>115,700</b>	<b>40.3</b>	<b>2,411</b>	<b>21.2</b>
Other portfolio companies	171,512	59.7	8,948	78.8
<b>Total investment portfolio</b>	<b>\$ 287,212</b>	<b>100.0%</b>	<b>\$ 11,359</b>	<b>100.0%</b>

(A) New investment during the applicable period.

(B) We exited Venyu in August 2013. Investment income for Venyu for the three months ended September 30, 2013 was \$3.7 million, or 32.6% of total investment income.

Other income decreased 86.3% from the prior year period. During the three months ended September 30, 2014, other income primarily consisted of \$0.2, \$0.2, and \$0.1 million resulting from prepayments of success fees received from ASH, Frontier Packaging, Inc. ( Frontier ), and Mathey Investments, Inc. ( Mathey ), respectively. During the three months ended September 30, 2013, other income primarily consisted of \$3.3 million in success fee and dividend income received in connection with the exit of Venyu and \$0.3 million in success fee income resulting from prepayments received from Cavert II Holding Corp. ( Cavert ).

## Expenses

Total expenses, excluding any voluntary and irrevocable credits to the base management and incentive fees, increased 0.1% for the three months ended September 30, 2014, as compared to the prior year period, primarily due to an increase in the base management fee, interest expense, and other expenses as compared to the prior year period. This was partially offset by a decrease in the incentive fee for the three months ended September 30, 2014, as compared to the prior year period.

The base management fee increased for the three months ended September 30, 2014, as compared to the prior year period, as a result of the increased size of our portfolio over the respective periods. An incentive fee of \$1.1 million was earned by the Adviser during the three months ended September 30, 2014, compared to an incentive fee of \$1.6 million for the prior year period. The base

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

	<b>Three Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
Average gross assets subject to base management fee <sup>(A)</sup>	<b>\$ 348,800</b>	\$ 312,200
Multiplied by prorated annual base management fee of 2%	<b>0.5%</b>	0.5%
Base management fee <sup>(B)</sup>	<b>1,744</b>	1,561
Other credits to Adviser fees <sup>(B)</sup>	<b>(606)</b>	(334)
Net base management fee	<b>\$ 1,138</b>	\$ 1,227
Incentive fee <sup>(B)</sup>	<b>\$ 1,051</b>	\$ 1,557

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

(B) Reflected as a line item on our accompanying *Condensed Consolidated Statement of Operations*. Interest and dividend expense increased 9.4% for the three months ended September 30, 2014, as compared to the prior year period, primarily due to increased average borrowings under the Credit Facility. The average balance outstanding on our Credit Facility during the three months ended September 30, 2014, was \$64.9 million, as compared to \$41.4 million in the prior year period. The increase in average borrowings under the Credit Facility was partially offset by the decrease in interest rate due to an amendment of the Credit facility that occurred June 26, 2014.

Other expenses increased 20.6% for the three months ended September 30, 2014, as compared to the prior year period, primarily due to an increase in legal expenses, as compared to the prior year period.

### **Realized and Unrealized (Loss) Gain on Investments**

#### *Realized (Loss) Gain*

During the three months ended September 30, 2014, we recorded a realized loss of \$12 relating to post-closing adjustments on previous investment exits. During the three months ended September 30, 2013, we recorded a realized gain of \$24.8 million related to the Venyu exit.

#### *Unrealized (Depreciation) Appreciation*

During the three months ended September 30, 2014, we recorded net unrealized depreciation on investments in the aggregate amount of \$1.5 million. The unrealized appreciation (depreciation) across our investments for the three months ended September 30, 2014, were as follows:

## Three months ended September 30, 2014

Portfolio Company	Reversal of			Net Gain (Loss)
	Realized (Loss)	Unrealized Appreciation (Depreciation)	Unrealized Depreciation (Appreciation)	
Funko, LLC	\$	\$ 3,116	\$	\$ 3,116
Jackrabbit, Inc.		2,364		2,364
SBS, Industries, LLC		2,323		2,323
Alloy Die Casting Corp.		1,682		1,682
Mathey Investments, Inc.		1,628		1,628
Frontier Packaging, Inc.		1,034		1,034
Ginsey Home Solutions, Inc.		640		640
Tread Corp.		467		467
B-Dry, LLC		(251)		(251)
Drew Foam Company, Inc.		(338)		(338)
Head Country Inc.		(399)		(399)
Mitchell Rubber Products, Inc.		(452)		(452)
Behrens Manufacturing, LLC		(548)		(548)
Country Club Enterprises, LLC		(626)		(626)
NDLI Inc.		(1,297)		(1,297)
Acme Cryogenics, Inc.		(1,306)		(1,306)
Danco Acquisition Corp.		(1,367)		(1,367)
SOG Specialty K&T, LLC		(1,398)		(1,398)
Galaxy Tool Holding Corp.		(6,666)		(6,666)
Other, net (<\$250 Net)	(12)	(101)		(113)
<b>Total</b>	<b>\$ (12)</b>	<b>\$ (1,495)</b>	<b>\$</b>	<b>\$ (1,507)</b>

The primary change in our net unrealized depreciation of \$1.5 million for the three months ended September 30, 2014, was a decrease in the equity valuation of one of our portfolio companies, Galaxy Tool Holding Corp. ( Galaxy ), due to a decrease in company performance. This was partially offset by increased performance in several of our portfolio companies and, to a lesser extent, an increase in certain comparable multiples used to estimate the fair value of our investments.

During the three months ended September 30, 2013, we recorded net unrealized depreciation on investments in the aggregate amount of \$15.7 million, which included the reversal of \$17.4 million in aggregate unrealized appreciation, related to the Venyu exit. Excluding reversals, we had \$1.7 million in net unrealized appreciation for the three months ended September 30, 2013.

The realized gains and unrealized appreciation (depreciation) across our investments for the three months ended September 30, 2013, were as follows:

Portfolio Company	Three months ended September 30, 2013			
	Realized Gain	Unrealized Appreciation (Depreciation)	Reversal of Unrealized Appreciation	Net Gain (Loss)
Venyu Solutions, Inc. <sup>(A)</sup>	\$ 24,804	\$	\$ (17,374)	\$ 7,430
Channel Technologies Group, LLC		3,372		3,372
Jackrabbit, Inc.		3,261		3,261
Country Club Enterprises, LLC		1,565		1,565
Star Seed, Inc.		926		926
Acme Cryogenics, Inc.		864		864
Frontier Packaging, Inc.		757		757
Funko, LLC		396		396
B-Dry, LLC		(502)		(502)
Mitchell Rubber Products, Inc.		(629)		(629)
Ginsey Home Solutions, Inc.		(800)		(800)
Drew Foam Company, Inc.		(998)		(998)
Quench Holdings Corp.		(1,648)		(1,648)
SBS, Industries, LLC		(2,291)		(2,291)
SOG Specialty K&T, LLC		(2,767)		(2,767)
Other, net (<\$250 Net)		184		184
<b>Total</b>	<b>\$ 24,804</b>	<b>\$ 1,690</b>	<b>\$ (17,374)</b>	<b>\$ 9,120</b>

(A) Venyu was sold in August 2013.

Excluding reversals, the primary changes in our net unrealized appreciation of \$1.7 million for the three months ended September 30, 2013, were due to increased equity valuations in several of our portfolio companies, primarily due to increased portfolio company performance and, to a lesser extent, an increase in certain comparable multiples used to estimate the fair value of our investments.

Over our entire investment portfolio, we recorded approximately \$2.0 million of net unrealized depreciation on our debt positions and \$0.5 million of net unrealized appreciation on our equity holdings for the three months ended September 30, 2014. At September 30, 2014, the fair value of our investment portfolio was less than our cost basis by

approximately \$65.2 million, as compared to \$63.7 million at June 30, 2014, representing net unrealized depreciation of \$1.5 million for the three months ended September 30, 2014. We believe that our aggregate investment portfolio is valued at a depreciated value due to the lingering effects of the recent recession on the performance of certain of our portfolio companies. Our entire portfolio was fair valued at 84.2% of cost as of September 30, 2014. The unrealized depreciation of our investments does not have an impact on our current ability to pay distributions to stockholders; however, it may be an indication of future realized losses, which could ultimately reduce our income available for distribution.

#### **Unrealized Appreciation on Other**

There was no unrealized appreciation on our Credit Facility recognized for the three months ended September 30, 2014. During the three months ended September 30, 2013, there was net unrealized appreciation of \$0.4 million on our Credit Facility. The Credit Facility was fair valued at \$87.8 million and \$61.7 million as of September 30 and March 31, 2014, respectively.



**Comparison of the Six Months Ended September 30, 2014, to the Six Months Ended September 30, 2013**

	Six Months Ended September 30,			
	2014	2013	\$ Change	% Change
<b>INVESTMENT INCOME</b>				
Interest income	<b>\$ 16,974</b>	\$ 14,888	\$ 2,086	14.0%
Other income	<b>1,934</b>	3,869	(1,935)	(50.0)
Total investment income	<b>18,908</b>	18,757	151	0.8
<b>EXPENSES</b>				
Base management fee	<b>3,410</b>	3,110	300	9.6
Incentive fee	<b>2,266</b>	1,722	544	31.6
Administration fee	<b>444</b>	399	45	11.3
Interest and dividend expense	<b>2,883</b>	2,499	384	15.4
Amortization of deferred financing fees	<b>536</b>	499	37	7.4
Other	<b>1,294</b>	1,112	182	16.4
Expenses before credits from Adviser	<b>10,833</b>	9,341	1,492	16.0
Other credits to Adviser fees	<b>(988)</b>	(845)	(143)	(16.9)
Total expenses net of credits to fee	<b>9,845</b>	8,496	1,349	15.9
<b>NET INVESTMENT INCOME</b>	<b>9,063</b>	10,261	(1,198)	(11.7)
<b>REALIZED AND UNREALIZED (LOSS) GAIN ON:</b>				
Net realized (loss) gain on sale of investments	<b>(12)</b>	24,804	(24,816)	NM
Net unrealized appreciation (depreciation) on investments	<b>3,965</b>	(27,090)	31,055	NM
Net unrealized depreciation on other	<b>451</b>	445	6	1.3
Net gain (loss) on investments and other	<b>4,404</b>	(1,841)	6,245	NM
<b>NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS</b>	<b>\$ 13,467</b>	\$ 8,420	\$ 5,047	59.9
<b>BASIC AND DILUTED PER COMMON SHARE:</b>				
Net investment income	<b>\$ 0.34</b>	\$ 0.39	\$ (0.05)	(12.8)
Net increase in net assets resulting from operations	<b>\$ 0.51</b>	\$ 0.32	\$ 0.19	59.4

NM = Not Meaningful

Total investment income increased by 0.8% for the six months ended September 30, 2014, as compared to the prior year period. This increase was primarily due an overall increase in interest income in the six months ended September 30, 2014, as a result of an increase in the size of our loan portfolio during the six months ended September 30, 2014. This was partially offset by a decrease in other income during the six months ended September 30, 2014 as compared to the prior year period, due to success fee and dividend income resulting from our exit from Venyu during the six months ended September 30, 2013.

Interest income from our investments in debt securities increased 14.0% for the six months ended September 30, 2014, as compared to the prior year period. The level of interest income from investments is directly related to the principal balance of our interest-bearing investment portfolio outstanding during the period multiplied by the weighted average yield. The weighted average principal balance of our interest-bearing investment portfolio during the six months ended September 30, 2014, was approximately \$269.2 million, compared to approximately \$236.4 million for the prior year period. This increase was primarily due to approximately \$92.9 million in new investments originated after September 30, 2013, including ADC, Behrens, Meridian, Head Country, Edge, TREC, and CSM. At September 30, 2014, loans to one portfolio company, Tread, were on non-accrual, with an aggregate weighted average principal balance of \$12.0 million. As of September 30, 2013, loans to two portfolio companies, ASH and Tread, were on non-accrual, with an aggregate weighted average principal balance of \$25.8 million during the six months ended September 30, 2013. The weighted average yield on our interest-bearing investments was 12.6% for the six months ended September 30, 2014 and 2013, excluding cash and cash equivalents and receipts recorded as other income. The weighted average yield varies from period to period, based on the current stated interest rate on interest-bearing investments.

The following table lists the investment income from investments for our five largest portfolio company investments based on fair value during the respective periods:

Portfolio Company	As of September 30, 2014		Six Months Ended September 30, 2014	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,139	7.8%	\$ 848	4.5%
SOG Specialty Knives and Tools, LLC	23,989	6.9	1,366	7.2
Cambridge Sound Management, LLC <sup>(A)</sup>	20,175	5.8	6	0.0
Jackrabbit, Inc.	19,327	5.6	755	4.0
Edge Adhesives Holdings, Inc.	18,074	5.2	847	4.5
<b>Subtotal five largest investments</b>	<b>108,704</b>	<b>31.3</b>	<b>3,822</b>	<b>20.2</b>
Other portfolio companies	238,197	68.7	15,086	79.8
<b>Total investment portfolio</b>	<b>\$ 346,901</b>	<b>100.0%</b>	<b>\$ 18,908</b>	<b>100.0%</b>

Portfolio Company	As of September 30, 2013		Six Months Ended September 30, 2013	
	Fair Value	% of Portfolio	Investment Income	% of Total Investment Income
Acme Cryogenics, Inc.	\$ 27,771	9.7%	\$ 848	4.5%
Galaxy Tool Holding Corp.	24,156	8.4	1,065	5.7
SOG Specialty Knives and Tools, LLC	24,131	8.4	1,332	7.1
Schylling Investments, LLC <sup>(A)</sup>	20,000	7.0	312	1.7
Channel Technologies Group, LLC	19,642	6.8	926	4.9
<b>Subtotal five largest investment<sup>(B)</sup></b>	<b>115,700</b>	<b>40.3</b>	<b>4,483</b>	<b>23.9</b>
Other portfolio companies	171,512	59.7	14,274	76.1
<b>Total investment portfolio</b>	<b>\$ 287,212</b>	<b>100.0%</b>	<b>\$ 18,757</b>	<b>100.0%</b>

(A) New investment during the applicable period.

(B) We exited Venyu in August 2013. Investment income for Venyu for the six months ended September 30, 2013 was \$4.3 million, or 23.1% of total investment income.

Other income decreased 50.0% from the prior year period. During the six months ended September 30, 2014, other income primarily consisted of \$1.3 million of dividend income received from Mathey. During the six months ended September 30, 2013, other income primarily consisted of \$3.3 million in success fee and dividend income received in connection with the exit of Venyu.

## Expenses

Total expenses, excluding any voluntary and irrevocable credits to the base management and incentive fees, increased 16.0% for the six months ended September 30, 2014, as compared to the prior year period, primarily due to an increase in the base management fee, incentive fee and interest expense, as compared to the prior year period.

The base management fee increased for the six months ended September 30, 2014, as compared to the prior year period, as a result of the increased size of our portfolio over the respective periods. Additionally, an incentive fee of \$2.3 million was earned by the Adviser during the six months ended September 30, 2014, compared to \$1.7 million for the prior year period. The base management and incentive fees are computed quarterly, as described under Investment Advisory and Management Agreement in Note 4 of the notes to our accompanying *Condensed Consolidated Financial Statements* and are summarized in the following table:

	<b>Six Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
Average gross assets subject to base management fee <sup>(A)</sup>	\$ 341,000	\$ 311,000
Multiplied by prorated annual base management fee of 2%	1.0%	1.0%
Base management fee <sup>(B)</sup>	3,410	3,110
Other credits to Advisor fees <sup>(B)</sup>	(988)	(845)
Net base management fee	\$ 2,422	\$ 2,265
Incentive fee <sup>(B)</sup>	\$ 2,266	\$ 1,722

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

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

Interest and dividend expense increased 15.4% for the six months ended September 30, 2014, as compared to the prior year period, primarily due to increased average borrowings under the Credit Facility. The average balance outstanding on our Credit Facility during the six months ended September 30, 2014, was \$62.7 million, as compared to \$37.1 million in the prior year period. The increase in average borrowings under the Credit Facility was partially offset by the decrease in interest rate due to an amendment of the Credit facility that occurred June 26, 2014.

### Realized and Unrealized (Loss) Gain on Investments

#### *Realized (Loss) Gain*

During the six months ended September 30, 2014, we recorded a realized loss of \$12 relating to post-closing adjustments on the previous investment exits. During the six months ended September 30, 2013, we recorded a realized gain of \$24.8 million related to the Venyu sale.

#### *Unrealized Appreciation (Depreciation)*

During the six months ended September 30, 2014, we recorded net unrealized appreciation on investments in the aggregate amount of \$4.0 million. The unrealized appreciation (depreciation) across our investments for the six months ended September 30, 2014, were as follows:

Portfolio Company	Six months ended September 30, 2014			
	Realized (Loss)	Unrealized Appreciation (Depreciation)	Reversal of Unrealized (Appreciation) Depreciation	Net Gain (Loss)
Jackrabbit, Inc.	\$	\$ 6,364	\$	\$ 6,364
NDLI Inc.		4,464		4,464
Funko, LLC		3,445		3,445
Mathey Investments, Inc.		2,309		2,309
SBS, Industries, LLC		1,843		1,843
Edge Adhesives Holdings, Inc.		868		868
Alloy Die Casting Corp.		610		610
Drew Foam Company, Inc.		418		418
Frontier Packaging, Inc.		327		327
B-Dry, LLC		(262)		(262)
Tread Corp.		(283)		(283)
Quench Holdings Corp.		(303)		(303)
Country Club Enterprises, LLC		(781)		(781)
Channel Technologies Group, LLC		(1,012)		(1,012)
Ginsey Home Solutions, Inc.		(1,612)		(1,612)
Head Country Inc.		(2,243)		(2,243)
Mitchell Rubber Products, Inc.		(2,283)		(2,283)
Danco Acquisition Corp.		(2,511)		(2,511)
SOG Specialty K&T, LLC		(2,650)		(2,650)
Galaxy Tool Holding Corp.		(2,992)		(2,992)
Other, net (<\$250 Net)	(12)	249		237

<b>Total</b>	\$ (12)	\$	3,965	\$	\$ 3,953
--------------	---------	----	-------	----	----------

The primary changes in our net unrealized appreciation for the six months ended September 30, 2014, were due to an increase in equity valuations in several of our portfolio companies, primarily due to an increase portfolio company performance and increases in certain comparable multiples used to estimate the fair value of our investments.

During the six months ended September 30, 2013, we recorded net unrealized depreciation on investments in the aggregate amount of \$27.1 million, which included the reversal of \$17.4 million in aggregate unrealized appreciation, related to the Venyu sale. Excluding reversals, we had \$9.7 million in net unrealized depreciation for the six months ended September 30, 2013.

The realized gains and unrealized appreciation (depreciation) across our investments for the six months ended September 30, 2013, were as follows:

Portfolio Company	Six months ended September 30, 2013			
	Realized Gain	Unrealized (Depreciation) Appreciation	Reversal of Unrealized (Appreciation) Depreciation	Net Gain (Loss)
Venyu Solutions, Inc. <sup>(A)</sup>	\$ 24,804	\$ (1,596)	\$ (17,374)	\$ 5,834
Galaxy Tool Holding Corp.		3,280		3,280
Jackrabbit, Inc.		3,261		3,261
Channel Technologies Group, LLC		3,152	2	3,154
Frontier Packaging, Inc.		1,852		1,852
Country Club Enterprises, LLC		1,584		1,584
Star Seed, Inc.		926		926
Acme Cryogenics, Inc.		430		430
Funko, LLC		396		396
Noble Logistics, Inc.		(383)		(383)
Tread Corp.		(1,000)		(1,000)
Precision Southeast, Inc.		(1,059)		(1,059)
Mitchell Rubber Products, Inc.		(1,554)		(1,554)
Drew Foam Company, Inc.		(2,166)		(2,166)
SBS, Industries, LLC		(2,808)		(2,808)
B-Dry, LLC		(3,512)		(3,512)
Ginsey Home Solutions, Inc.		(4,502)		(4,502)
SOG Specialty K&T, LLC		(5,691)		(5,691)
Other, net (<\$250 Net)		(328)		(328)
<b>Total</b>	<b>\$ 24,804</b>	<b>\$ (9,718)</b>	<b>\$ (17,372)</b>	<b>\$ (2,286)</b>

(A) Venyu was sold in August 2013.

The primary changes in our net unrealized depreciation for the six months ended September 30, 2013, were due to decreased equity valuations in several of our portfolio companies, primarily due to decreased portfolio company performance and decreases in certain comparable multiples used to estimate the fair value of our investments.

Over our entire investment portfolio, we recorded, in the aggregate, approximately \$3.5 million and \$0.5 million of net unrealized appreciation on our debt and equity investments, respectively, for the six months ended September 30, 2014. As of September 30, 2014, the fair value of our investment portfolio was less than our cost basis by approximately \$65.2 million, as compared to \$69.2 million at March 31, 2014, representing net unrealized appreciation of \$4.0 million for the six months ended September 30, 2014. We believe that our aggregate investment portfolio is valued at a depreciated value due to the lingering effects of the recent recession on the performance of certain of our portfolio companies. Our entire portfolio was fair valued at 84.2% of cost as of September 30, 2014. The unrealized depreciation of our investments does not have an impact on our current ability to pay distributions to stockholders; however, it may be an indication of future realized losses, which could ultimately reduce our income available for distribution.

**Net Unrealized Depreciation on Other**

For the six months ended September 30, 2014 and 2013, we recorded \$0.5 million and \$0.4 million, respectively, of net unrealized depreciation on our Credit Facility.



## LIQUIDITY AND CAPITAL RESOURCES

### Operating Activities

Net cash (used in) provided by operating activities for the six months ended September 30, 2014, was approximately \$(16.8) million, as compared to \$3.4 million during the six months ended September 30, 2013. Even though we disbursed \$56.0 million in the prior year period to purchase investments compared to \$29.3 million in the current period, the prior year period had significant cash inflows from the sale of Venyu to offset the purchase of investments. The sale of Venyu resulted in proceeds of \$30.8 million and principal repayments of \$19.0 million. Our cash flows from operations generally come from cash collections of interest and dividend income from our portfolio companies, as well as cash proceeds received through repayments of loan investments and sales of equity investments. These cash collections are primarily used to pay distributions to our stockholders, interest payments on our Credit Facility, dividend payments on our Term Preferred Stock, management fees to the Adviser, and other entity-level expenses.

As of September 30, 2014, we had equity investments in or loans to 30 private companies with an aggregate cost basis of approximately \$412.1 million. As of September 30, 2013, we had equity investments in or loans to 24 private companies with an aggregate cost basis of approximately \$354.2 million. The following table summarizes our total portfolio investment activity during the six months ended September 30, 2014 and 2013:

	<b>Six Months Ended September 30,</b>	
	<b>2014</b>	<b>2013</b>
Beginning investment portfolio, at fair value	\$ 314,393	\$ 286,482
New investments	21,925	54,590
Disbursements to existing portfolio companies	7,362	1,400
Increase in investment balance due to PIK	58	30
Scheduled principal repayments		(110)
Unscheduled principal repayments	(802)	(22,090)
Proceeds from sales	12	(30,804)
Net realized (loss) gain	(12)	24,804
Net unrealized appreciation (depreciation)	3,965	(9,718)
Reversal of net unrealized appreciation		(17,372)
Ending investment portfolio, at fair value	\$ 346,901	\$ 287,212

The following table summarizes the contractual principal repayment and maturity of our investment portfolio by fiscal year, assuming no voluntary prepayments, as of September 30, 2013:

		<b>Amount</b>
For the remaining six months ending		
March 31:	2015	\$ 43,144
For the fiscal year ending March 31:	2016	44,103
	2017	24,915
	2018	74,632
	2019	84,181
	Thereafter	27,645

<b>Total contractual repayments</b>	<b>\$ 298,620</b>
Investments in equity securities	113,460
<b>Total cost basis of investments held at September 30, 2014:</b>	<b>\$ 412,080</b>

### Financing Activities

Net cash provided by financing activities for the six months ended September 30, 2014, was approximately \$15.3 million, which consisted primarily of \$26.5 million of net borrowings on our Credit Facility, partially offset by \$9.5 million in distributions to common stockholders. Net cash used in financing activities for the six months ended September 30, 2013, was approximately \$42.1 million and consisted primarily of net repayments of our short-term borrowings of \$36.0 million and distributions to common stockholders of \$7.9 million, partially offset by \$3.0 million in net borrowings from our Credit Facility.

### Distributions

To qualify to be taxed as a RIC and thus avoid corporate level tax on the income we distribute to our stockholders, we are required under Subchapter M of the Code, to distribute at least 90% of our ordinary income and short-term capital gains to our stockholders on an annual basis. In accordance with these requirements, we declared and paid monthly cash distributions of \$0.06 per common share for each of the six months from April 2014 through September 2014. In October 2014, our Board of Directors also declared a monthly distribution of \$0.06 per common share for each of October, November and December 2014 as well as a one-time special distribution of \$0.05 in December 2014. Our Board of Directors declared these distributions based on estimates of net taxable income for the fiscal year ending March 31, 2015.

For the fiscal year ended March 31, 2014, our distributions to common stockholders totaled \$18.8 million, and were less than our taxable income over the same year. At March 31, 2014, we elected to treat \$3.9 million, of the first distribution paid after year-end as having been paid in the prior year, in accordance with Section 855(a) of the Code. Additionally, the covenants in our Credit Facility generally restrict the amount of distributions that we can pay out to be no greater than our net investment income.

We also declared and paid monthly cash distributions of \$0.1484375 per share of Term Preferred Stock for each of the six months from April 2014 through September 2014. In October 2014, our Board of Directors also declared a monthly distribution of \$0.1484375 per preferred share for each of October, November and December 2014. In accordance with accounting principles generally accepted in the U.S. ( GAAP ), we treat these monthly distributions as an operating expense. For tax purposes, these preferred distributions are deemed to be paid entirely out of ordinary income to preferred stockholders.

## **Equity**

### *Registration Statement*

We filed a registration statement on Form N-2 (File No. 333-181879) with the SEC on June 4, 2012, and subsequently filed a Pre-Effective Amendment No. 1 to the registration statement on July 17, 2012, which the SEC declared effective on July 26, 2012. On June 7, 2013, we filed Post-Effective Amendment No. 2 to the registration statement, which the SEC declared effective on July 26, 2013. On June 3, 2014, we filed Post-Effective Amendment No. 3 to the registration statement, and subsequently filed a Post-Effective Amendment No. 4 to the registration statement on September 2, 2014, which the SEC declared effective on September 4, 2014. The registration statement permits us to issue, through one or more transactions, up to an aggregate of \$300 million in securities, consisting of common stock, preferred stock, subscription rights, debt securities and warrants to purchase common stock, including through a combined offering of two or more of such securities.

### *Common Stock*

Pursuant to our registration statement on Form N-2 (Registration No. 333-181879), on October 5, 2012, we completed a public offering of 4 million shares of our common stock at a public offering price of \$7.50 per share, which was below then current NAV of \$8.65 per share. Gross proceeds totaled \$30 million and net proceeds, after deducting underwriting discounts and offering expenses borne by us, were \$28.3 million, which was used to repay borrowings under our Credit Facility. In connection with the offering, the underwriters exercised their option to purchase an additional 395,825 shares at the public offering price to cover over-allotments, which resulted in gross proceeds of \$3.0 million and net proceeds, after deducting underwriting discounts, of \$2.8 million.

We anticipate issuing equity securities to obtain additional capital in the future. However, we cannot determine the terms of any future equity issuances or whether we will be able to issue equity on terms favorable to us, or at all. When our common stock is trading below NAV per share, as it has consistently since September 30, 2008, the 1940 Act places regulatory constraints on our ability to obtain additional capital by issuing common stock. Generally, the 1940 Act provides that we may not issue and sell our common stock at a price below our NAV per common share, other than to our then existing common stockholders pursuant to a rights offering, without first obtaining approval from our stockholders and our independent directors. On October 27, 2014, the closing market price of our common stock was \$7.27 per share, representing a 14.4% discount to our NAV of \$8.49 as of September 30, 2014. To the extent that our common stock continues to trade at a market price below our NAV per common share, we will generally be precluded from raising equity capital through public offerings of our common stock, other than pursuant to stockholder approval or through a rights offering to existing common stockholders. At our 2014 Annual Meeting of Stockholders held on August 7, 2014, our stockholders approved a proposal authorizing us to issue and sell shares of our common stock at a price below our then current NAV per common share for a period of one year from the date of

such approval, provided that our Board of Directors makes certain determinations prior to any such sale.

*Term Preferred Stock*

Pursuant to our prior registration statement on Form N-2 (File No. 333-160720), in March 2012, we completed an offering of 1.6 million shares of Term Preferred Stock at a public offering price of \$25.00 per share. Gross proceeds totaled \$40 million, and net proceeds, after deducting underwriting discounts and offering expenses borne by us were \$38 million, a portion of which was used to repay borrowings under our Credit Facility, with the remaining proceeds being held to make additional investments and for general corporate purposes. We incurred \$2 million in total offering costs related to the offering, which have been recorded as an asset in accordance with GAAP and are being amortized over the redemption period ending February 28, 2017.

The Term Preferred Stock provides for a fixed dividend equal to 7.125% per year, payable monthly (which equates to \$2.9 million per year). We are required to redeem all of the outstanding Term Preferred Stock on February 28, 2017, for cash at a redemption price equal to \$25.00 per share plus an amount equal to accumulated but unpaid dividends, if any, to the date of redemption. The Term

Preferred Stock has a preference over our common stock with respect to dividends, whereby no distributions are payable on our common stock unless the stated dividends, including any accrued and unpaid dividends, on the Term Preferred Stock have been paid in full. The Term Preferred Stock is not convertible into our common stock or any other security. In addition, three other potential redemption triggers are as follows: (1) upon the occurrence of certain events that would constitute a change in control of us, we would be required to redeem all of the outstanding Term Preferred Stock; (2) if we fail to maintain an asset coverage ratio of at least 200%, we are required to redeem a portion of the outstanding Term Preferred Stock or otherwise cure the ratio redemption trigger and (3) at our sole option, at any time on or after February 28, 2016, we may redeem some or all of the Term Preferred Stock.

The Term Preferred Stock has been recorded as a liability in accordance with GAAP and, as such, affects our asset coverage, exposing us to additional leverage risks.

### **Revolving Credit Facility**

On June 26, 2014, we, through our wholly-owned subsidiary, Business Investment, entered into Amendment No. 1 to the Fifth Amended and Restated Credit Agreement originally entered into on April 30, 2013, with Key Equipment Finance Inc., as administrative agent, lead arranger and a lender (the Administrative Agent), Branch Banking and Trust Company (BB&T) as a lender and managing agent, and the Adviser, as servicer, to extend the revolving period and reduce the interest rate of the line of credit (the Credit Facility). The revolving period was extended 14 months to June 26, 2017, and if not renewed or extended by June 26, 2017, all principal and interest will be due and payable on or before June 26, 2019 (two years after the revolving period end date). In addition, we have retained the two one-year extension options, to be agreed upon by all parties, which may be exercised on or before June 26, 2015 and 2016, respectively, and upon exercise, the options would extend the revolving period to June 26, 2018 and 2019 and the maturity date to June 26, 2020 and 2021, respectively. Subject to certain terms and conditions, the Credit Facility can be expanded by up to \$145 million, to a total facility amount of \$250 million, through additional commitments of existing or new committed lenders. Advances under the Credit Facility generally bear interest at 30-day LIBOR, plus 3.25% per annum, down from 3.75% prior to the amendment, and the Credit Facility includes an unused fee of 0.50% on undrawn amounts. Once the revolving period ends, the interest rate margin increases to 3.75% for the period from June 26, 2017 to June 26, 2018, and further increases to 4.25% through maturity. We incurred fees of \$0.4 million in connection with this amendment.

On September 19, 2014, we further increased our borrowing capacity under the Credit Facility from \$105 million to \$185 million by entering into Joinder Agreements pursuant to the Credit Facility, by and among Business Investment, the Administrative Agent, the Adviser and each of East West Bank, Manufacturers and Traders Trust, Customers Bank and Talmer Bank and Trust. We incurred fees of \$0.8 million in connection with this expansion.

The Credit Facility contains covenants that require Business Investment to maintain its status as a separate legal entity; prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions) and restrict material changes to our credit and collection policies without lenders' consent. The facility generally also limits payments as distributions to the aggregate net investment income for each of the twelve month periods ending March 31, 2015, 2016 and 2017. We are also subject to certain limitations on the type of loan investments we can make, including restrictions on geographic concentrations, sector concentrations, loan size, dividend payout, payment frequency and status, average life and lien property. The Credit Facility also requires us to comply with other financial and operational covenants, which obligate us to, among other things, maintain certain financial ratios, including asset and interest coverage, a minimum net worth and a minimum number of obligors required in the borrowing base of the credit agreement. Additionally, we are subject to a performance guaranty that requires us to maintain (i) a minimum net worth of \$170 million plus 50% of all equity and subordinated debt raised after April 30, 2013, which equates to \$170 million as of September 30, 2014, (ii) asset coverage with respect to senior securities representing indebtedness of at least 200%, in accordance with Section 18 of the 1940 Act and (iii) our status as a BDC under the 1940 Act and as a RIC under the Code. As of September 30, 2014, and as defined in the performance guaranty of our Credit

Facility, we had a minimum net worth of \$264.8 million, an asset coverage of 264% and an active status as a BDC and RIC. As of October 28, 2014, we were in compliance with all covenants.

In July 2013, we entered into a forward interest rate cap agreement, effective October 2013 and expiring April 2016, for a notional amount of \$45 million. We incurred a premium fee of \$75 in conjunction with this agreement. The interest rate cap agreement effectively limits the interest rate on a portion of the borrowings pursuant to the terms of the Credit Facility.

The Administrative Agent also requires that any interest or principal payments on pledged loans be remitted directly by the borrower into a lockbox account, with The Bank of New York Mellon Trust Company, N.A. as custodian. The Administrative Agent is also the trustee of the account and generally remits the collected funds to us once a month.

## Contractual Obligations and Off-Balance Sheet Arrangements

We have lines of credit to certain of our portfolio companies that have not been fully drawn. Since these lines of credit have expiration dates and we expect many will never be fully drawn, the total line of credit commitment amounts do not necessarily represent future cash requirements. We estimate the fair value of the unused line of credit commitments as of September 30 and March 31, 2014 to be minimal.

In addition to the lines of credit to our portfolio companies, we have also extended certain guaranties on behalf of some of our portfolio companies, whereby we have guaranteed an aggregate of \$2.7 million of obligations of Country Club Enterprises, LLC ( CCE ). As of September 30, 2014, we have not been required to make any payments on any of the guaranties, and we consider the credit risks to be remote and the fair value of the guaranties to be minimal.

The following table shows our contractual obligations as of September 30, 2014, at cost:

Contractual Obligations <sup>(A)</sup>	Total	Payments Due by Period			More than 5 Years
		Less than 1 Year	1-3 Years	3-5 Years	
Credit Facility	87,750			87,750	
Term Preferred Stock	40,000			40,000	
Secured borrowing	5,096			5,096	
Interest payments on obligations <sup>(B)</sup>	26,082	6,732	11,884	7,466	
<b>Total</b>	<b>\$ 158,928</b>	<b>\$ 6,732</b>	<b>\$ 11,884</b>	<b>\$ 140,312</b>	<b>\$</b>

(A) Excludes our unused line of credit commitments and guaranties to our portfolio companies in the aggregate amount of \$5.4 million.

(B) Includes interest payments due on our Credit Facility and dividend obligations on the Term Preferred Stock. Dividend payments on the Term Preferred Stock assume quarterly declarations and monthly distributions through the date of mandatory redemption.

The majority of our debt securities in our portfolio have a success fee component, which can enhance the yield on our debt investments. Unlike PIK income, we generally do not recognize success fees as income until they are received in cash. Due to their contingent nature, there are no guarantees that we will be able to collect any or all of these success fees or know the timing of such collections. As a result, as of September 30, 2014, we had unrecognized success fees of \$21.0 million, or \$0.79 per common share, which do not meet the recognition criteria under the relevant accounting guidance.

## Critical Accounting Policies

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

## Investment Valuation

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

#### Accounting Recognition

We record our investments at fair value in accordance with the Financial Accounting Standards Board (the FASB ) Accounting Standards Codification Topic 820, *Fair Value Measurements and Disclosures* ( ASC 820 ) and the 1940 Act. Investment transactions are recorded on the trade date. Realized gains or losses are measured by the difference between the net proceeds from the repayment or sale and amortized cost basis of the investment, without regard to unrealized depreciation or appreciation previously recognized, and include investments charged off during the period, net of recoveries. Unrealized depreciation or appreciation primarily reflect the change in investment fair values, including the reversal of previously recorded unrealized depreciation or appreciation when gains or losses are realized.

In accordance with ASC 820, our investments fair value is determined to be the price that would be received for an investment in a current sale, which assumes an orderly transaction between market participants on the measurement date. This fair value definition focuses on exit price in the principal, or most advantageous, market and prioritizes, within a measurement of fair value, the use of market-based inputs over entity-specific inputs. ASC 820 also establishes the following three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of a financial instrument as of the measurement date.



Level 1 inputs to the valuation methodology are quoted prices (unadjusted) for identical financial instruments in active markets;

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

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement. Unobservable inputs are those inputs that reflect assumptions that market participants would use when pricing the financial instrument and can include the Valuation Team's own assumptions based upon the best available information.

When a determination is made to classify our investments within Level 3 of the valuation hierarchy, such determination is based upon the significance of the unobservable factors to the overall fair value measurement. However, Level 3 financial instruments typically include, in addition to the unobservable, or Level 3, inputs, observable inputs (or, components that are actively quoted and can be validated to external sources). The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. As of September 30 and March 31, 2014, all of our investments were valued using Level 3 inputs and during the six months ended September 30, 2014 and 2013, there were no investments transferred in to or out of Level 1, 2 or 3.

#### Board Responsibility

In accordance with the 1940 Act, our Board of Director has the ultimate responsibility for reviewing and approving, in good faith, the fair value of our investments based on our established investment valuation policy (the Policy). Our Board of Directors reviews valuation recommendations that are provided by professionals of the Adviser and Administrator with oversight and direction from the Valuation Team. There is no single standard for determining fair value (especially for privately-held businesses), as fair value depends upon the specific facts and circumstances of each individual investment. In determining the fair value of our investments, the Valuation Team, led by the Valuation Officer, uses the Policy, which has been approved by our Board of Directors, and each quarter our Board of Directors reviews the Policy to determine if changes thereto are advisable and also reviews whether the Valuation Team has applied the Policy consistently.

#### Use of Third Party Valuation Firms

The Valuation Team engages third party valuation firms to provide independent assessments of fair value of certain of our investments. Currently, the third-party service provider Standard & Poor's Securities Evaluation, Inc. (SPSE) provides estimates of fair value on the majority of our debt investments.

The Valuation Team generally assigns SPSE's estimates of fair value to our debt investments where we do not have the ability to effectuate a sale of the applicable portfolio company. The Valuation Team corroborates SPSE's estimates of fair value using one or more of the valuation techniques discussed below. The Valuation Team's estimates of value on a specific debt investment may significantly differ from SPSE's. When this occurs, our Board of Directors reviews whether the Valuation Team has followed the Policy and whether the Valuation Team's recommended value is reasonable in light of the Policy and other facts and circumstances and then votes to accept or reject the Valuation Team's recommended valuation.

Valuation Techniques

In accordance with ASC 820, the Valuation Team uses the following techniques when valuing our investment portfolio:

***Total Enterprise Value*** In determining the fair value using a total enterprise value ( TEV ), the Valuation Team first calculates the TEV of the portfolio company by incorporating some or all of the following factors: the portfolio company's ability to make payments and other specific portfolio company attributes; the earnings of the portfolio company (the trailing or projected twelve month revenue or earnings before interest, taxes, depreciation and amortization ( EBITDA )); EBITDA or revenue multiples obtained from our indexing methodology whereby the original transaction EBITDA or revenue multiple at the time of our closing is indexed to a general subset of comparable disclosed transactions and EBITDA or revenue multiples from recent sales to third parties of similar securities in similar industries; a comparison to publicly traded securities in similar industries; and other pertinent factors. To gather information regarding these factors, the Valuation Team generally references industry statistics and may use outside experts. Once the TEV is determined for a portfolio company, the Valuation Team then allocates the TEV to the portfolio company's securities in order of their relative priority in the capital structure. Generally, the Valuation Team uses TEV to value our equity investments and, in the circumstances where we have the ability to effectuate a sale of a portfolio company, our debt investments.

TEV is primarily calculated using EBITDA or revenue multiples; however, TEV may also be calculated using a discounted cash flow ( DCF ) analysis whereby future expected cash flows of the portfolio company are discounted to determine a net present value using estimated risk-adjusted discount rates, which incorporate adjustments for nonperformance and liquidity risks. Generally, the Valuation Team uses the DCF to calculate the TEV to corroborate estimates of value for our equity investments, where we do not have the ability to effectuate a sale of a portfolio company or for debt of credit impaired portfolio companies.

***Yield Analysis*** The Valuation Team generally determines the fair value of our debt investments using the yield analysis, which includes a DCF calculation and the Valuation Team's own assumptions, including, but not limited to, estimated remaining life, current market yield, current leverage, and interest rate spreads. This technique develops a modified discount rate that incorporates risk premiums including, among other things, increased probability of default, increased loss upon default and increased liquidity risk. Generally, the Valuation Team uses the yield analysis to corroborate both estimates of value provided by SPSE and market quotes.

In addition to the above valuation techniques, the Valuation Team may also consider other factors when determining fair values of our investments, including, but not limited to: the nature and realizable value of the collateral, including external parties' guaranties; any relevant offers or letters of intent to acquire the portfolio company; and the markets in which the portfolio company operates. If applicable, new debt and equity investments made during the three months ended September 30, 2014 are generally valued at original cost basis. Fair value measurements of our investments may involve subjective judgments and estimates and due to the inherent uncertainty of determining these fair values, the fair value of our investments may fluctuate from period to period. Additionally, changes in the market environment and other events that may occur over the life of the investment may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. Further, such investments are generally subject to legal and other restrictions on resale or otherwise are less liquid than publicly traded securities. If we were required to liquidate a portfolio investment in a forced or liquidation sale, we could realize significantly less than the value at which it is recorded.

#### Credit Monitoring and Risk Rating

The Adviser monitors a wide variety of key credit statistics that provide information regarding our portfolio companies to help us assess credit quality and portfolio performance and, in some instances, that is used as inputs in our valuation techniques. We, through the Adviser, participate in periodic board meetings of our portfolio companies in which we hold board seats and also generally require them to provide annual audited and monthly unaudited financial statements. Using these statements or comparable information and board discussions, the Adviser calculates and evaluates certain credit statistics.

We risk rate all of our investments in debt securities. We use a proprietary risk rating system. Our risk rating system uses a scale of 0 to >10, with >10 being the lowest probability of default. This system is used to estimate the probability of default on debt securities and the expected loss if there is a default. These types of systems are referred to as risk rating systems and are used by banks and rating agencies. The risk rating system covers both qualitative and quantitative aspects of the business and the securities we hold. During the three months ended June 30, 2014, we modified our risk rating model to incorporate additional factors in our qualitative and quantitative analysis. While the overall process did not change, we believe the additional factors enhance the quality of the risk ratings of our investments. No adjustments were made to prior periods as a result of this modification due to the immaterial effect on the overall portfolio ratings.

We seek to have our risk rating system mirror the risk rating systems of major risk rating organizations, such as those provided by a Nationally Recognized Statistical Rating Organization ( NRSRO ). While we seek to mirror the NRSRO

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

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

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

The above scale gives an indication of the probability of default and the magnitude of the expected loss if there is a default. Generally, our policy is to stop accruing interest on an investment if we determine that interest is no longer collectable. As of September 30 and March 31, 2014, Tread was the only portfolio investment on non-accrual with an aggregate fair value of \$0. Additionally, we do not risk rate our equity securities.

The following table lists the risk ratings for all proprietary loans in our portfolio as of September 30 and March 31, 2014, representing 100%, of the principal balance of all loans in our portfolio at the end of each period:

Rating	As of September 30, 2014	As of March 31, 2014
Highest	9.2	9.1
Average	6.2	5.7
Weighted Average	6.3	5.2
Lowest	2.8	2.6

## Tax Status

### Federal Income Taxes

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

In an effort to limit certain excise taxes imposed on RICs, we generally distribute during each calendar year, an amount at least equal to the sum of (1) 98% of our ordinary income for the calendar year, (2) 98.2% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and capital gains in excess of capital losses for preceding years that were not distributed during such years. However, we did incur an excise tax of \$0.3 million and \$31 for the calendar years ended December 31, 2013 and 2012, respectively. Under the RIC Modernization Act (the RIC Act ), we are permitted to carry forward capital losses incurred in taxable years beginning after March 31, 2011, for an unlimited period. However, any losses incurred during those future taxable years must be used prior to the losses incurred in pre-enactment taxable years, which carry an expiration date. Additionally, post-enactment capital loss carryforwards will retain their character as either short-term or long-term capital losses rather than only being considered short-term as permitted under previous regulation. Our total capital loss carryforward balance was \$0.2 million as of March 31, 2014.

### **Revenue Recognition**

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

loans are restored to accrual status when past-due principal and interest are paid, and, in management's judgment, are likely to remain current, or due to a restructuring, the interest income is deemed to be collectible. As of September 30, 2014, our loans to Tread were on non-accrual, with an aggregate debt cost basis of \$12.0 million, or 4.0% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0. As of March 31, 2014, our loans to Tread were on non-accrual, with an aggregate debt cost basis of \$11.7 million, or 4.2% of the cost basis of all debt investments in our portfolio, and an aggregate fair value of \$0.

PIK interest, computed at the contractual rate specified in the loan agreement, is added to the principal balance of the loan and recorded as interest income. During the three and six months ended September 30, 2014, we recorded PIK income of \$29 and \$58, respectively. During the three and six months ended September 30, 2013, we recorded PIK income of \$29 and \$39, respectively.

#### *Other Income Recognition*

We generally record success fees upon receipt of cash. Success fees are contractually due upon a change of control in a portfolio company. We recorded \$0.5 million of success fees for the three and six months ended September 30, 2014, respectively. During the three months ended September 30, 2014, we received success fees of \$0.2 million from each of ASH and Frontier and \$0.1 million from Mathey. We recorded \$2.1 million and \$2.3 million of success fees during the three and six months ended September 30, 2013, respectively. During the three months ended September 30, 2013, we received \$0.3 million Cavert in success fee prepayments and we received \$1.8 million related to the exit of Venyu.

We accrue dividend income on preferred and common equity securities to the extent that such amounts are expected to be collected and if we have the option to collect such amounts in cash or other consideration. For the three and six months ended September 30, 2014, we recorded \$1.4 million of dividend income from Mathey. For the three and six months ended September 30, 2013, we recorded \$1.4 million in dividend income related to the exit of Venyu.

Both dividend and success fee income are recorded in Other income in our accompanying *Condensed Consolidated Statements of Operations*.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk includes risks that arise from changes in interest rates, foreign currency exchange rates, commodity prices, equity prices and other market changes that affect market sensitive instruments. The prices of securities held by us may decline in response to certain events, including those directly involving the companies whose securities are owned by us; conditions affecting the general economy; overall market changes; local, regional or global political, social or economic instability; and interest rate fluctuations.

The primary risk we believe we are exposed to is interest rate risk. Because we borrow money to make investments, our net investment is dependent upon the difference between the rate at which we borrow funds and the rate at which we invest those funds. 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 use a combination of debt and equity capital to finance our investing activities. We do use interest rate risk management techniques to limit our exposure to interest rate fluctuations. Such techniques may include various interest rate hedging activities to the extent permitted by the 1940 Act.

Our target is to have approximately 20% of the loans in our portfolio at fixed rates and approximately 80% at variable rates or variables rates with a floor mechanism. Currently, all of our variable-rate loans have rates associated with either the current LIBOR or prime rate. As of September 30, 2014, our portfolio consisted of the following breakdown based on total principal balance of all outstanding debt investments:

83.1%	Variable rates with a floor
16.9	Fixed rates
<b>100.0%</b>	<b>Total</b>

There have been no material changes in the quantitative and qualitative market risk disclosures for the three and six months ended September 30, 2014 from that disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2014, as filed with the SEC on May 13, 2014.

### ITEM 4. CONTROLS AND PROCEDURES.

#### a) Evaluation of Disclosure Controls and Procedures

As of September 30, 2014 (the end of the period covered by this report), we, including our chief executive officer and chief financial officer, evaluated the effectiveness and design and operation of our disclosure controls and procedures. Based on that evaluation, our management, including the chief executive officer and chief financial officer, concluded that our disclosure controls and procedures were effective at a reasonable assurance level in timely alerting management, including the chief executive officer and chief financial officer, of material information about us required to be included in periodic SEC filings. However, in evaluation of the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

#### b) Changes in Internal Control over Financial Reporting

There were no changes in internal controls for the three months ended September 30, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.





## **PART II OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS.**

From time to time, we may become involved in various investigations, claims and legal proceedings that arise in the ordinary course of our business. Furthermore, third parties may try to seek to impose liability on us in connection with the activities of our portfolio companies. While we do not expect that the resolution of these matters if they arise would materially affect our business, financial condition or results of operations, resolution will be subject to various uncertainties and could result in the expenditure of significant financial and managerial resources.

### **ITEM 1A. RISK FACTORS.**

Our business is subject to certain risks and events that, if they occur, could adversely affect our financial condition and results of operations and the trading price of our securities. For a discussion of these risks, please refer to the Risk Factors section in our Annual Report on Form 10-K for the year ended March 31, 2014, as filed with the SEC on May 13, 2014

### **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

Not applicable.

### **ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

Not applicable.

### **ITEM 4. MINE SAFETY DISCLOSURES.**

Not applicable.

### **ITEM 5. OTHER INFORMATION.**

Not applicable.

### **ITEM 6. EXHIBITS**

See the exhibit index.

**SIGNATURE**

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.

**GLADSTONE INVESTMENT  
CORPORATION**

By: /s/ David Watson  
David Watson  
*Chief Financial Officer and Treasurer*

Dated: October 28, 2014

**EXHIBIT INDEX**

<b>Exhibit</b>	<b>Description</b>
3.1	Amended and Restated Certificate of Incorporation, incorporated by reference to Exhibit A.2 to Pre-Effective Amendment No. 1 to the Registration Statement on Form N-2 (File No. 333-123699), filed May 13, 2005.
3.2	Certificate of Designation of 7.125% Series A Cumulative Term Preferred Stock, incorporated by reference to Exhibit 2.A.2 to Post-Effective Amendment No. 5 to the Registration Statement on Form N-2 (File No. 333-160720), filed February 29, 2012.
3.3	Amended and Restated Bylaws, incorporated by reference to Exhibit B.2 to the Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2 (File No. 333-123699), filed June 21, 2005.
3.4	First Amendment to Amended and Restated Bylaws of the Registrant, incorporated by reference to Exhibit 99.1 to the Current Report on Form 8-K (File No. 814-00704), filed July 10, 2007.
4.1	Specimen Stock Certificate, incorporated by reference to Exhibit 99.D to Pre-Effective Amendment No. 3 to the Registration Statement on Form N-2 (File No. 333-123699), filed June 21, 2005.
4.2	Specimen 7.125% Series A Cumulative Term Preferred Stock Certificate, incorporated by reference to Exhibit 2.D.4 to Post-Effective Amendment No. 5 to the Registration Statement on Form N-2 (File No. 333-160720), filed February 29, 2012.
10.1	Joinder Agreement, dated as of September 19, 2014, by and among the Gladstone Business Investment, LLC, Gladstone Management Corporation, Key Equipment Finance, a division of KeyBank National Association and East West Bank, incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K (File No. 814-00704), filed September 22, 2014.
10.2	Joinder Agreement, dated as of September 19, 2014, by and among the Gladstone Business Investment, LLC, Gladstone Management Corporation, Key Equipment Finance, a division of KeyBank National Association and Manufacturers and Traders Trust, incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K (File No. 814-00704), filed September 22, 2014.
10.3	Joinder Agreement, dated as of September 19, 2014, by and among the Gladstone Business Investment, LLC, Gladstone Management Corporation, Key Equipment Finance, a division of KeyBank National Association and Customers Bank, incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K (File No. 814-00704), filed September 22, 2014.
10.4	Joinder Agreement, dated as of September 19, 2014, by and among the Gladstone Business Investment, LLC, Gladstone Management Corporation, Key Equipment Finance, a division of KeyBank National Association and Talmer Bank and Trust, incorporated by reference to Exhibit 10.4 to the Current Report on Form 8-K (File No. 814-00704), filed September 22, 2014.
11	Computation of Per Share Earnings (included in the notes to the financial statements contained in this report).*
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.+

\* Filed herewith

+ Furnished herewith

All other exhibits for which provision is made in the applicable regulations of the Securities and Exchange Commission are not required under the related instruction or are inapplicable and therefore have been omitted.