GLADSTONE CAPITAL CORP
Form 497
October 10, 2007

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The information in this prospectus supplement and the accompanying prospectus is not complete and may be changed. This prospectus supplement and the accompanying prospectus are not an offer to sell these securities and are not soliciting an offer to buy these securities in any jurisdiction where the offer or sale is not permitted.

Subject to Completion, Dated October 10, 2007

Filed Pursuant to Rule 497

Registration No. 333-143027

PROSPECTUS SUPPLEMENT
(To Prospectus dated July 5, 2007)

GLADSTONE CAPITAL CORPORATION

2,500,000 Shares

Common Stock

This is a public offering of common stock of Gladstone Capital Corporation. We are offering an aggregate of 2,500,000 Shares of our Common Stock, $0.001 par value per share. Our common stock is listed on the Nasdaq Global Select Market under the symbol "GLAD." We are a closed-end, non-diversified management investment company that has elected to be treated as a business development company under the Investment Company Act of 1940. On October 9, 2007, the last reported sale price of our common stock on the Nasdaq Global Select Market was $20.00 per share.

Investing in our common stock involves risks. See "Risk Factors" beginning on page 9.

Neither the Securities and Exchange Commission, nor any state securities commission, nor any other regulatory body has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

	Per Share	Total
Public offering price	$	$
Underwriting discount (sales load)	$	$
Proceeds, before expenses, to us (1)	$	$

(1) Before deducting estimated expenses payable by us of $430,000.

The underwriter may also purchase up to an additional 375,000 shares of common stock at the public offering price, less the underwriting discount, within 30 days from the date of this prospectus supplement solely to cover over-allotments. If the over-allotment option is exercised in full, the total public offering price will be $ and the total underwriting discount (sales load) will be $. The proceeds to us would be $, before deducting estimated expenses payable by us of $430,000.

The underwriter expects to deliver the shares to purchasers on or about October , 2007.

Deutsche Bank Securities

The date of this prospectus supplement is October , 2007.

PROSPECTUS SUPPLEMENT
SUMMARY

This summary highlights some information from this prospectus supplement and the accompanying prospectus, and it may not contain all of the information that is important to you. To understand the terms of the common stock offered hereby, you should read this prospectus supplement and the accompanying prospectus carefully. Together, these documents describe the specific terms of the shares we are offering. You should carefully read the section titled "Risk Factors" in the accompanying prospectus and the documents identified in the section "Additional Information." Except where the context suggests otherwise, the terms "we," "us," "our," the "Company" and "Gladstone Capital" refer to Gladstone Capital Corporation; "Adviser" refers to Gladstone Management Corporation; "Administrator" refers to Gladstone Administration, LLC; and "Gladstone Companies" refers to the Adviser and its affiliated companies. Except as otherwise noted, all information in this prospectus supplement and the accompanying prospectus assumes no exercise of the underwriter's over-allotment option.

Overview

We are a specialty finance company that provides capital to small and medium sized U.S. businesses. We operate as a closed-end, non-diversified management investment company, and have elected to be treated as a business development company under the Investment Company Act of 1940, as amended, or the 1940 Act. In addition, for tax purposes we have elected to be treated as a regulated investment company, or RIC, under the Internal Revenue Code of 1986, as amended.

We seek to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, senior subordinated notes and junior subordinated notes, of established private businesses that are substantially backed by leveraged buyout funds, venture capital funds or others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants or other equity instruments that we may receive when we make loans.

We seek to invest in small and medium-sized private U.S. businesses that meet certain criteria, including the potential for growth, adequate assets for loan collateral, experienced management teams with significant ownership interest in the business, adequate capitalization, profitable operations based on cash flow, substantial ownership by leveraged buyout funds or venture capital funds and potential opportunities for us to realize appreciation and gain liquidity in our equity positions. We may achieve liquidity 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 seek to invest primarily in three categories of debt of private companies:

Senior Subordinated Notes. We seek to invest a portion of our assets in senior subordinated notes. Holders of senior subordinated notes are subordinated to the rights of holders of senior debt to receive principal and interest payments or, in the case of last out tranches of senior debt, liquidation proceeds from the borrower. As a result, senior subordinated notes are riskier than senior notes. Although such loans are sometimes secured by significant collateral, the lender is largely dependent on the borrower's cash flow for repayment. Additionally, lenders may receive warrants to acquire shares of stock in borrowers or other yield enhancements in connection with

these loans. Senior subordinated notes include second lien loans and syndicated second lien loans.

Senior Notes. We seek to invest a portion of our assets in senior notes of borrowers. Using its assets and cash flow as collateral, the borrower typically uses senior notes to cover a substantial portion of the funding needed to operate. Senior lenders are exposed to the least risk of all providers of debt because they command a senior position with respect to scheduled interest and principal payments and typically receive a first priority lien on a substantial portion of the borrower's assets. However, unlike senior subordinated and junior subordinated lenders, senior lenders typically do not receive any stock, warrants to purchase stock of the borrowers or other yield enhancements. As such, they generally do not participate in the equity appreciation of the value of the business. Senior notes may include revolving lines of credit, senior term loans, senior syndicated loans and senior last-out tranche loans.

Junior Subordinated Notes. We also seek to invest a small portion of our assets in junior subordinated notes. Holders of junior subordinated notes are subordinated to the rights of the holders of senior debt and senior subordinated debt to receive principal and interest payments from the borrower, and junior subordinated notes are typically unsecured or have such a low priority lien on existing assets that there is little chance of collateral yielding any payment to the junior subordinated lender in the event assets are sold in foreclosure. The risk profile of junior subordinated notes is high, which permits the junior subordinated lender to obtain higher interest rates and more equity and equity-like compensation.

Our loans typically range from $5 million to $15 million, although this investment size may vary proportionately as the size of our capital base changes, generally mature in no more than seven years, and accrue interest at fixed or variable rates. Because the majority of the loans in our portfolio consist of term debt of private companies who typically cannot or will not expend the resources to have their debt securities rated by a credit rating agency, we expect that most if not all of the debt securities we acquire will be unrated. Accordingly, we cannot accurately predict what ratings these loans might receive if they were in fact rated, and thus cannot determine whether or not they could be considered "investment grade" quality.

We hold our loan investment portfolio through our wholly-owned subsidiary, Gladstone Business Loan LLC.

Portfolio Composition

Approximately 68% of the aggregate cost value of our investment portfolio as of September 30, 2007 was senior debt, approximately 32% was senior subordinated debt and there were no investments in junior subordinated debt. As of September 30, 2007, we had approximately $355.8 million invested at cost in 56 portfolio companies. The aggregate fair value of our investments as of September 30, 2007 was approximately $349.8 million.

The table below sets forth, as of September 30, 2007, the fair value and percentage of total investments of our investment portfolio by industry classifications.

	September 30, 2007	
Industry Classification	**Fair Value**	**% of Total Investments**
Aerospace & Defense	$ 4,615,750	1.3%
Automobile	6,245,938	1.8%
Broadcast (TV, Radio & Cable)	30,151,019	8.6%
Cargo Transport	15,685,197	4.5%
Chemicals, Plastics & Rubber	25,110,192	7.2%
Diversified/Conglomerate Manufacturing	3,710,700	1.1%
Electronics	31,351,318	9.0%
Farming & Agriculture	11,537,833	3.3%
Finance	2,460,125	0.7%
Healthcare, Education & Childcare	36,927,299	10.5%
Home & Office Furnishings	17,057,109	4.9%
Leisure, Amusement, Movies & Entertainment	9,508,750	2.7%
Machinery	9,883,350	2.8%
Mining, Steel, Iron & Non-precious Metals	27,057,277	7.7%
Personal & Non-durable Consumer Products	8,977,500	2.6%
Printing, Publishing & Broadcasting	83,973,941	24.0%
Retail Stores	14,986,500	4.3%
Textiles & Leather	10,604,732	3.0%
Total	$ 349,844,530	100.0%

Our Investment Adviser and Administrator

Our Adviser is our affiliate and investment adviser and is led by a management team which has extensive experience in our lines of business. Our Adviser also has a wholly-owned subsidiary, our Administrator, which employs our chief financial officer, chief compliance officer, controller, treasurer and their respective staffs. All of our directors and executive officers serve as either directors or executive officers, or both, of Gladstone Commercial, a publicly traded real estate investment trust; Gladstone Investment, a publicly traded business development company; our Adviser; and our Administrator.

Our Adviser and our Administrator also provide investment advisory and administrative services to our affiliates Gladstone Commercial, Gladstone Investment and Gladstone Land Corporation, an agricultural real estate company owned by Mr. Gladstone. In the future, our Adviser may provide investment advisory and administrative services to other funds, both public and private, of which it is the sponsor.

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

Our Investment Objectives and Our Strategy

Our strategy is to make loans at favorable interest rates to small and medium-sized businesses that we believe have traditionally been underserved by conventional lenders. Our Adviser uses the loan referral networks of Messrs. Gladstone, Stelljes and Brubaker and of its managing directors to identify and make senior and subordinated loans to borrowers that need funds to finance growth, restructure their balance sheets or effect a change of control. We believe that our business strategy will enable us to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, senior subordinated notes and junior subordinated notes of established private businesses that are backed by leveraged buyout funds, venture capital funds or others. In addition, from time to time we might acquire existing loans that meet this profile from leveraged buyout funds, venture capital funds and others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants or other equity instruments that we might receive when we make loans.

We target small and medium-sized private businesses that meet certain criteria, including the potential for growth, adequate assets for loan collateral, and experienced management teams with significant ownership interest in the business, adequate capitalization, and profitable operations based on cash flow and potential opportunities for us to realize appreciation and gain liquidity in our various equity positions. We may achieve liquidity in an equity position 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, although we cannot assure you that we will always have these rights. We can also achieve a similar effect by requiring the borrower to pay us conditional interest, which we refer to as a success fee, upon the occurrence of certain events. Success fees are dependent upon the success of the borrower and the occurrence of a triggering event, and are paid in lieu of warrants to own common stock of the borrower.

RECENT DEVELOPMENTS

Portfolio Activity

Subsequent to June 30, 2007, we have not invested in any new portfolio companies, however, we have extended approximately $7.9 million of revolver draws and term loan commitments to existing portfolio companies. Also subsequent to the quarter ended June 30, 2007, we cancelled a past due note of approximately $800,000 of MCA Communications, LLC by accepting a deed in lieu of foreclosure, which converted the outstanding note obligations into a majority owned equity interest in the portfolio company.

In addition, since June 30, 2007 we were repaid in full on three investments for an aggregate of approximately $17.9 million and also received revolver repayments and scheduled amortization payments of an aggregate of approximately $4.1 million.

Portfolio Valuation

As of September 30, 2007, the fair value of our portfolio of investments decreased by $4.9 million, or approximately 1.3%, from the quarter ended June 30, 2007. Our Board of Directors approved the aggregate fair value of our portfolio of investments at September 30, 2007, based in part on its acceptance of opinions of value submitted by Standard & Poors Securities Evaluation Services, Inc. ("SPSE") regarding certain debt securities, and on input from our Adviser, in accordance with our quarterly valuation process as more particularly described under "Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies Investment Valuation."

THE OFFERING

Common Stock offered by us	2,500,000 shares
Common Stock outstanding after this offering (1)(2)	17,262,574 shares
Use of proceeds	We expect to use all of the net proceeds of this offering to repay outstanding indebtedness under our line of credit. See "Use of Proceeds."
Nasdaq Global Select Market Symbol	GLAD
Risk Factors	See "Risk Factors" in the accompanying prospectus and other information in this prospectus supplement and the accompanying prospectus for a discussion of factors you should carefully consider before deciding to invest in shares of our common stock.
Current distribution rate	We currently make distributions to stockholders on a monthly basis at the rate of $0.14 per month. Our distribution rate is subject to change or discontinuance at any time in the discretion of our Board of Directors. Our future earnings and operating cash flow may not be sufficient to support a dividend.

(1) Excludes 375,000 shares of common stock issuable pursuant to the over-allotment option granted to the underwriter exercisable within 30 days from the date of this prospectus supplement.

(2) Based on the number of shares outstanding as of October 10, 2007.

FEES AND EXPENSES

The following table is intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. Except where the context suggests otherwise, whenever this prospectus supplement contains a reference to fees or expenses paid by "us" or "Gladstone Capital," or that "we" will pay fees or expenses, stockholders will indirectly bear such fees or expenses as investors in Gladstone Capital. The following percentages were calculated based on net assets as of June 30, 2007.

	Current
Stockholder Transaction Expenses	
Sales load (as a percentage of offering price) (1)	5.5%
Dividend reinvestment plan expenses (2)	None
Estimated annual expenses (as a percentage of net assets attributable to common stock)	
Management fees (3)	3.51%
Incentive fees payable under investment advisory and management agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income) (4)	2.15%
Interest Payments on Borrowed Funds (5)	3.03%
Other expenses	1.00%
Total annual expenses (estimated) (3)(6)	9.69%

(1) Represents the estimated underwriting discount with respect to our common stock being sold in this offering, a one-time fee we will pay to the underwriter in connection with this offering and is the only sales load to be paid in connection with this offering.

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

(3) Our annual base management fee is 2.0% (0.5% quarterly) of our average gross assets, which is defined as total assets of Gladstone Capital, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents pledged to creditors. See "Management Certain Transactions Advisory and Administration Agreements" in the accompanying prospectus and footnote 4 below.

(4) The incentive fee consists of two parts: an income-based fee and a capital gains-based fee. The income-based fee will be payable quarterly in arrears, and will equal 20% of the excess, if any, of our pre-incentive fee net investment income that exceeds a 1.75% quarterly (7.0% annualized) hurdle rate, subject to a "catch-up" provision measured as of the end of each calendar quarter. The "catch-up" provision requires us to pay 100% of our pre-incentive fee net investment income with respect to that portion of such income, if any, that exceeds the hurdle rate but is less than 125% of the quarterly hurdle rate (or 2.1875%) in any calendar quarter (8.75% annualized). The catch-up provision is meant to provide our Adviser with 20% of our pre-incentive fee net investment income as if a hurdle rate did not apply when our pre-incentive fee net investment income exceeds 125% of the quarterly hurdle rate in any calendar quarter (8.75% annualized). The income-based incentive fee will be computed and paid on income that may include interest that is accrued but not yet received in cash. Our pre-incentive fee net investment income used to calculate this part of the income incentive fee is also included in the amount of our gross assets used to calculate the 2% base management fee (see footnote 3 above). The quarter ended December 31, 2006 was the first quarter under our new advisory agreement and, as a result, was the first quarter in which the incentive fee was earned. For purposes of this computation, the aggregate gross amount of the December 31, 2006, March 31, 2007 and June 30, 2007 fees, exclusive of any credits, was annualized to determine the percentage the fee represents of net assets. After giving effect to credits against the incentive fee, the annualized incentive fee was 0.48% of net assets as of June 30, 2007. There can be no assurance that our Adviser will give any credits against the incentive fee in the future. The capital gains-based portion of the fee did not have an effect on the incentive fee for purposes of this calculation since we have not realized overall net capital gains to date.

Examples of how the incentive fee would be calculated (exclusive of any credits) are as follows:

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

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

= 100% × (2.00% - 1.75%)

= 0.25%

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

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

= (100% × 0.4375%) + (20% × 0.1125%)

= 0.4375% + 0.0225%

= 0.46%

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

= 20% × (6% - 1%)

= 20% × 5%

= 1%

For a more detailed discussion of the calculation of the two-part incentive fee, see "Management Certain Transactions Advisory and Administration Agreements" in the accompanying prospectus.

(5) We have entered into a revolving credit facility, under which our borrowing capacity is $220 million, effective May 29, 2007. We have drawn down on this credit facility and we expect to borrow additional funds in the future up to an amount so that our asset coverage, as defined in the 1940 Act, is at least 200% after each issuance of our senior securities. Assuming that we borrowed $220 million at an interest rate of 6.08%, interest payments on borrowed funds would have been 6.21% of our net assets as of June 30, 2007.

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

Example

The following example demonstrates the projected dollar amount of total cumulative expenses that would be incurred over various periods with respect to a hypothetical investment in this offering. In calculating the following expense amounts, we have assumed that our annual expenses would remain at the levels set forth in the table above and that you would pay a sales load of 5.5% (the estimated underwriting discount to be paid by us with respect to the common stock being sold by us in this offering).

	1 Year	3 Years	5 Years	10 Years

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$ 125	$ 261	$ 389	$ 684

While the example assumes, as required by the Securities and Exchange Commission, which we refer to as the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. Additionally, we have assumed that the entire amount of such 5% annual return would constitute ordinary income as we have not historically realized positive capital gains (computed net of all realized capital losses and unrealized capital depreciation) on our investments, nor do we expect to realize positive capital gains in the

foreseeable future. Because the assumed 5% annual return is significantly below the hurdle rate of 7% (annualized) that we must achieve under the investment advisory and management agreement to trigger the payment of an income-based incentive fee, we have assumed, for purposes of the above example, that no income-based incentive fee would be payable if we realized a 5% annual return on our investments. Additionally, because we have not historically realized positive capital gains (computed net of all realized capital losses and unrealized capital depreciation) on our investments, we have assumed that we will not trigger the payment of any capital gains-based incentive fee in any of the indicated time periods. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our expenses, and returns to our investors after such expenses, would be higher than reflected in the example. In addition, while the example assumes reinvestment of all dividends and distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the dividend payable to a participant by the market price per share of our common stock at the close of trading on the valuation date for the dividend. See "Dividend Reinvestment Plan" for additional information regarding our dividend reinvestment plan.

This example and the expenses in the table above should not be considered a representation of our future expenses, and actual expenses (including the cost of debt and incentive fees, if any, and other expenses) may be greater or less than those shown. As noted in the Fees and Expenses table above, we estimate that annual incentive fees payable under the investment advisory and management agreement will be 2.15% of net assets attributable to common stock.

USE OF PROCEEDS

We estimate that the net proceeds of this offering will be approximately $46,820,000 ($53,907,500 if the underwriter exercises its over-allotment option in full) after deducting the estimated underwriting discount and estimated offering expenses payable by us. We expect to use all of the net proceeds of this offering to repay amounts outstanding under our line of credit, which matures on May 23, 2008 and currently is accruing interest at approximately 6.08% per year.

CAPITALIZATION

The following table sets forth our actual capitalization at June 30, 2007:

on a historical basis;

on a pro forma as adjusted basis to reflect (i) the sale of 400,000 shares of common stock at $20.41 per share on July 24, 2007, (ii) the sale of 150,000 shares of common stock at $21.32 per share on August 22, 2007, (iii) the application of the net proceeds from such issuances to repay an aggregate of $11,140,060 of outstanding borrowings under our line of credit, and (iv) the cancellation of 37,109 shares of common stock associated with the cancellation of an employee loan; and

on a pro forma as further adjusted basis to give effect to (i) the sale of 2,500,000 shares of common stock in this offering at an assumed public offering price of $20.00 per share, which was the closing sale price of our common stock on the Nasdaq Global Select Market on October 9, 2007; and (ii) the application of the net proceeds from the offering, after deducting the estimated underwriting discount and offering expenses payable by us of an aggregate of $3,180,000, to repay an aggregate of $46,820,000 of outstanding borrowings under our line of credit as described in "Use of Proceeds."

	As of June 30, 2007		
	Actual	Pro Forma As Adjusted	Pro Forma As Further Adjusted (1)
		(unaudited)	(unaudited)
Assets			
Cash and cash equivalents	$ 3,491,495	$ 3,491,495	$ 3,491,495
Borrowings			
Borrowings under line of credit	161,188,000	150,047,940	103,227,940
Net Assets			
Common stock, $0.001 par value; 50,000,000 shares authorized; 14,249,683 shares issued and outstanding, actual, 14,762,574 shares issued and outstanding, pro forma as adjusted, and 17,262,574 shares issued and outstanding, pro forma as further adjusted	$ 14,250	$ 14,763	$ 17,263
Capital in excess of par value	225,449,718	235,872,554	282,690,054
Notes receivable-officers	(9,947,366)	(9,230,655)	(9,230,655)
Net unrealized appreciation on investments	(1,026,151)	(1,026,151)	(1,026,151)
Unrealized depreciation on derivative	(279,593)	(279,593)	(279,593)
Realized loss on sale of investments	(780,197)	(780,197)	(780,197)
Realized gain on settlement of derivatives	46,212	46,212	46,212
Accumulated undistributed net investment income	1,776,047	1,776,047	1,776,047
Total Net Assets	$ 215,252,920	$ 226,392,980	$ 273,212,980
Total Capitalization	$ 376,440,920	$ 376,440,920	$ 376,440,920

(1)

Assumes no exercise of the underwriter's over-allotment option to purchase 375,000 shares.

UNDERWRITING

Subject to the terms and conditions set forth in our underwriting agreement, we are offering the shares of our common stock described in this prospectus supplement through Deutsche Bank Securities Inc., the underwriter. The underwriter has agreed to purchase and we have agreed to sell to the underwriter, all of the shares offered by this prospectus supplement.

The underwriting agreement provides that the obligation of the underwriter to purchase the shares of common stock offered hereby is subject to certain conditions precedent and that the underwriter will purchase all of the shares of common stock offered by this prospectus supplement, other than those covered by the over-allotment option described below, if any of these shares are purchased.

The underwriter proposes to offer the shares of common stock to the public at the public offering price set forth on the cover of this prospectus supplement. If all the shares are not sold at the public offering price, the underwriter may change the offering price.

The underwriter has the option to purchase up to 375,000 additional shares of common stock from us at the same price it is paying for the 2,500,000 shares offered hereby. The underwriter may purchase additional shares only to cover over-allotments made in connection with this offering and only within 30 days after the date of this prospectus supplement. The underwriter will offer any additional shares that it purchases on the terms described in the preceding sections.

The underwriting discount per share is equal to the public offering price per share of common stock less the amount paid by the underwriter to us per share of common stock. These amounts are shown assuming either no exercise or full exercise by the underwriter of the underwriter's over-allotment option:

		Total Fees	
	Fee Per Share	**Without Exercise of Over-Allotment Option**	**With Full Exercise of Over-Allotment Option**
Underwriting Discount	$	$	$

We estimate that the total expenses of this offering, which will be paid by us, excluding the underwriting discount, will be approximately $430,000.

We have agreed to indemnify the underwriter against some specified types of liabilities, including liabilities under the Securities Act, and to contribute to payments the underwriter may be required to make in respect of these liabilities.

We and certain of our executive officers have agreed not to offer, sell, contract to sell or otherwise dispose of, or to engage in certain hedging and derivative transactions with respect to, our common stock for a period of 60 days after the date of this prospectus supplement, without first obtaining the written consent of Deutsche Bank Securities Inc. This consent may be given at any time without public notice. The 60 day lock-up period will automatically be extended if (1) during the last 17 days of the 60 day lock-up period we issue an earnings release or material news or a material event relating to us occurs, or (2) prior to the expiration of the 60 day lock-up period we announce that we will release earnings results during the 16-day period following the last day of the 60 day lock-up period. Such period will continue until the expiration of the 18-day period beginning on the issuance of the news release or the occurrence of the material news or material event, as applicable, unless the underwriter waives, in writing, such extension.

The European Union's prospectus directive provides that, in relation to each member state of the European Economic Area that has implemented the prospectus directive (each, a "relevant member state"), from and including the date on which the prospectus directive is implemented in the relevant member state (the "relevant implementation date"), no offeror of securities may make an offer of securities to the public in that relevant member state prior to the publication of a prospectus in relation to such securities that has been approved by the competent authority in that relevant member state or, where appropriate, approved in another relevant member state and notified to the competent authority in that relevant member state, all in accordance with the prospectus directive, except that such offeror may, with effect from and including the relevant implementation date, make an offer of securities to the public in that relevant member state at any time:

- to legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;

- to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year, (2) a total balance sheet of more than €43,000,000 and (3) an annual net turnover of more than €50,000,000, as shown in its last annual or consolidated accounts; or

- in any other circumstances which do not require the publication by the issuer of a prospectus pursuant to article 3 of the prospectus directive.

For the purposes of the above, the expression an "offer of securities to the public" in relation to any securities in any member state means the communication in any form and by any means of sufficient information on the terms of the offer and the notes to be offered so as to enable an investor to decide to purchase or subscribe the notes, as the same may be varied in that member state by any measure implementing the prospectus directive in that member state and the expression "prospectus directive" means European Union Directive 2003/71/EC and includes any relevant implementing measure in that member state.

The underwriter has represented and agreed that (i) it has not offered or sold and, prior to the expiration of the period of six months from the closing date of this offering, will not offer or sell any shares of our common stock to persons in the United Kingdom except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995; (ii) it has complied with and will comply with all applicable provisions of the Financial Services Act 1986 with respect to anything done by it in relation to the shares of our common stock in, from or otherwise involving the United Kingdom; and (iii) it has only issued or passed on and will only issue or pass on in the United Kingdom, any document received by it in connection with the issue of the shares of our common stock to a person who is of a kind described in Article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1996 or is a person to whom such document may otherwise lawfully be issued or passed on.

No prospectus (including any amendment, supplement or replacement thereto) nor any offering material relating to the shares of common stock described in this prospectus supplement has been submitted to the clearance procedures of the Autorité des Marchés Financiers or by the competent authority of another member state of the European Economic Area and notified to the Autorité des Marchés Financiers. The shares of common stock have not been offered or sold and will not be offered or sold, directly or indirectly, to the public in

France. Neither this prospectus supplement, the accompanying prospectus nor any other materials related to the offering or information contained therein relating to the shares of common stock has been or will be released, issued, distributed or caused to be released, issued or distributed to the public in France or used in connection with any offer for subscription or sale of the shares to the public in France. Such offers, sales and distributions will be made in France only

- to qualified investors (*investisseurs qualifiés*) and/or to a restricted circle of investors (*cercle restreint d'investisseurs*), in each case investing for their own account, as defined in, and in accordance with, Articles L. 411-2, D. 411-1, D. 411-2, D. 734-1, D. 744-1, D. 754-1 and D. 764-1 of the French *Code Monétaire et Financier* and applicable regulations thereunder; or

- to investment services providers authorized to engage in portfolio management on behalf of third parties; or

- in a transaction that, in accordance with article L.411-2-II-1°-or-2°-or 3° of the French *Code monétaire et Financier* and Article 211-2 of the General Regulations (*Règlement Général*) of the *Autorité des Marchés Financiers*, does not constitute a public offer (*appel public à l'épargne*).

The shares of common stock may be resold directly or indirectly, only in compliance with Articles L.411-1, L.411-2, L.412-1 and L.621-8 through L.621-8-3 of the French *Code Monétaire et Financier*.

The underwriter does not intend to confirm sales to any account over which it exercises discretionary authority.

In connection with this offering, the underwriter may purchase and sell shares of our common stock in the open market. These transactions may include stabilizing transactions, short sales and purchases to cover positions created by short sales and stabilizing transactions.

Short sales involve the sale by the underwriter of a greater number of shares than it is required to purchase in this offering. Covered short sales are sales made in an amount not greater than the underwriter's over-allotment option to purchase additional shares in this offering. The underwriter may close out any covered short position by either exercising its over-allotment option or purchasing shares in the open market. In determining the source of shares to close out the covered short position, the underwriter will consider, among other things, the price of shares available for purchase in the open market as compared to the price at which they may purchase shares through the over-allotment option.

Naked short sales are sales in excess of the over-allotment option. The underwriter must close out any naked short position by purchasing shares in the open market. A naked short position is more likely to be created if the underwriter is concerned there may be downward pressure on the price of shares in the open market prior to the completion of this offering.

Stabilizing transactions consist of various bids for or purchases of our common stock made by the underwriter in the open market prior to the completion of this offering.

Purchases to cover a short position and stabilizing transactions may have the effect of preventing or slowing a decline in the market price of our common stock. Additionally, these purchases may stabilize, maintain or otherwise affect the market price for our common stock. As a result, the price of our common stock may be higher than the price that might otherwise exist in the open market. These transactions may be effected on the Nasdaq Global Select Market, in the over-the-counter market or otherwise.

In the ordinary course of business, the underwriter or its affiliates have engaged and may in the future engage in various financing, commercial banking and investment banking services with, and provide financial advisory services to, us and our affiliates, for which they have received or may receive customary fees and expenses.

This offering is being conducted in compliance with Rule 2810 of the Conduct Rules of the National Association of Securities Dealers, Inc.

The principal business address of Deutsche Bank Securities Inc. is 60 Wall Street, New York, NY 10005.

LEGAL MATTERS

The validity of the issuance of the common stock offered hereby will be passed upon for us by Cooley Godward Kronish LLP, Reston, Virginia. The validity of the shares of common stock offered hereby will be passed upon for the underwriter by Bass, Berry & Sims PLC, Memphis, Tennessee.

EXPERTS

The financial statements as of September 30, 2006 and 2005 and for each of the three years in the period ended September 30, 2006 and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) as of September 30, 2006 included in the accompanying prospectus have been so included in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

ADDITIONAL INFORMATION

We have filed with the SEC a Registration Statement on Form N-2 under the Securities Act of 1933, as amended, with respect to the securities offered by this prospectus supplement. This prospectus supplement and the accompanying prospectus, which are a part of the registration statement, do not contain all of the information in the registration statement, including amendments, exhibits and schedules thereto. Statements in this prospectus supplement and the accompanying prospectus about the contents of any contract or other document are not necessarily complete and in each instance we refer you to the copy of the contract or other document filed, or incorporated by reference, as an exhibit to the registration statement, and each such statement is qualified in all respects by this reference.

We also file reports, proxy statements and other information with the SEC under the Securities Exchange Act of 1934, as amended. Such reports, proxy statements and other information, as well as the registration statement of which this prospectus supplement and the accompanying prospectus are a part and the exhibits and schedules thereto, can be inspected at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. Information about the operation of the public reference facilities may be obtained by calling the SEC at 1-202-551-8090. The SEC maintains a web site that contains reports, proxy statements and other information regarding registrants, including us, that file such information electronically with the SEC. The address of the SEC's web site is http://www.sec.gov. Copies of such material may also be obtained from the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates. Our common stock is listed on The Nasdaq Global Select Market and our corporate website is located at http://www.gladstonecapital.com. The information contained on, or accessible through, our website is not a part of this prospectus supplement.

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

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

FORWARD-LOOKING STATEMENTS

All statements contained herein, other than historical facts, may constitute "forward-looking statements." These statements may relate to, among other things, future events or our future performance or financial condition.

These statements may relate to, among other things, future events or our future performance or financial condition. In some cases, you can identify forward-looking statements by terminology such as "may," "might," "believe," "will," "provided," "anticipate," "future," "could," "growth," "plan," "intend," "expect," "should," "would," "if," "seek," "possible," "potential," "likely" or the 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) adverse changes in interest rates; (2) our failure or inability to establish or maintain referral arrangements with leveraged buyout funds and venture capital funds to generate loan opportunities; (3) the loss of one or more of our executive officers, in particular David Gladstone, Terry Lee Brubaker, or George Stelljes III; (4) our inability to extend, refinance, or maintain our credit facilities on terms reasonably acceptable to us, if at all, in future equity capital resources; (5) our inability to successfully securitize our loan portfolio on terms reasonably acceptable to us, if at all; (6) the decision of our competitors to aggressively seek to make senior and subordinated loans to small and medium-sized businesses on terms more favorable than we intend to provide; and (7) those factors listed under the caption "Risk Factors" in the accompanying prospectus. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this prospectus supplement.

INTERIM 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, future events or our future performance or financial condition. In some cases, you can identify forward-looking statements by terminology such as "may," "might," "believe," "will," "provided," "anticipate," "future," "could," "growth," "plan," "intend," "expect," "should," "would," "if," "seek," "possible," "potential," "likely" or the 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) adverse changes in interest rates; (2) our failure or inability to establish or maintain referral arrangements with leveraged buyout funds and venture capital funds to generate loan opportunities; (3) the loss of one or more of our executive officers, in particular David Gladstone, Terry Lee Brubaker, or George Stelljes III; (4) our inability to extend, refinance or maintain our credit facilities on terms reasonably acceptable to us, if at all in future equity capital resources; (5) our inability to successfully securitize our loan portfolio on terms reasonably acceptable to us, if at all; (6) the decision of our competitors to aggressively seek to make senior and subordinated loans to small and medium-sized businesses on terms more favorable than we intend to provide; and (7) those factors listed under the caption "Risk Factors" of the Annual Report on Form 10-K as filed with the Securities and Exchange Commission on December 6, 2006 and our Quarterly Report on Form 10-Q as filed with the Securities and Exchange Commission on May 2, 2007. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date hereof.

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

Overview

We were incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001. Our investment objectives are to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, second lien notes, and senior subordinated notes of established private businesses that are backed by leveraged buyout funds, venture capital funds or others, with a particular emphasis on second lien and senior subordinated notes. In addition, we may acquire existing loans, which meet this profile, from leveraged buyout funds, venture capital funds and others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants, or other equity instruments that we may receive when we extend loans. We operate as a closed-end, non-diversified management investment company, and have elected to be treated as a business development company under the Investment Company Act of 1940, as amended (the "1940 Act").

We seek to invest in small and medium-sized businesses that meet certain criteria, including some or all of the following: (1) the potential for growth in cash flow, (2) adequate assets for loan collateral, (3) experienced management teams with a significant ownership interest in the borrower, (4) profitable operations based on the borrower's cash flow,

(5) reasonable capitalization of the borrower (usually by buyout funds or venture capital funds) and (6) the potential to realize appreciation and gain liquidity in our equity position, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering by the borrower or by exercise of our right to require the borrower to buy back its warrants. We lend to borrowers that need funds to, among other things, effect a change of control, restructure their balance sheets, or finance growth, including acquisitions.

Our loans typically range from $5 million to $15 million, although this investment size may vary proportionately as the size of our capital base changes, generally mature in no more than seven years and accrue interest at fixed or variable rates. Some of our loans may contain a provision that calls for some portion of the interest payments to be deferred and added to the principal balance so that the interest is paid, together with the principal, at maturity. This form of deferred interest is often called "paid in kind" or "PIK" interest, and, when earned, we record PIK interest as interest income and add the PIK interest to the principal balance of the loans. We seek to avoid PIK interest with all potential investments under review. We currently do not hold any investments with PIK and, therefore, there was no PIK accrued on our balance sheet as of June 30, 2007.

Because the majority of our portfolio loans consist of term debt of private companies who typically cannot or will not expend the resources to have their debt securities rated by a credit rating agency, we expect that most of the debt securities we acquire will be unrated. We cannot accurately predict what ratings these loans might receive if they were in fact rated, and thus cannot determine whether or not they could be considered "investment grade" quality.

To the extent possible, our loans generally are collateralized by a security interest in the borrower's assets. Interest payments are generally made monthly or quarterly (except to the extent of any PIK interest) with amortization of principal generally being deferred for several years. The principal amount of the loans and any accrued but unpaid interest generally become due at maturity at five to seven years. When we receive a warrant to purchase stock in a borrower in connection with a loan, the warrant will typically have an exercise price equal to the fair value of the portfolio company's common stock at the time of the loan and entitle us to purchase a modest percentage of the borrower's stock.

Original issue discounts ("OID") arise when we extend a loan receive an equity interest in the borrower at the same time. To the extent that the price paid for the equity is not at market value, we must allocate part of the price paid for the loan, to the value of the equity. Then the amount allocated to the equity, the OID, must be amortized over the life of the loan. As with PIK interest, the amortization of OID also produces income that must be recognized for purposes of satisfying the distribution requirements for a regulated investment company ("RIC") under Subchapter M of the Internal Revenue Code of 1986, as amended (the "Code"), whereas the cash is received, if at all, when the equity instrument is sold. We seek to avoid OID and to date do not hold any investments with OID.

In addition, as a business development company under the 1940 Act, we are required to make available significant managerial assistance to our portfolio companies. Our investment adviser, Gladstone Management Corporation (the "Adviser") provides these services on our behalf through its officers who are also our officers. In addition, our Adviser provides other services to our portfolio companies, for which it receives fees, in connection with our investments. The fees for these services are generally paid to the Adviser in part at the time a prospective portfolio company signs a non-binding term sheet with us (as further described in the following paragraph), with the remainder paid at the closing of the investment. These fees are generally non-recurring, however in some instances they may have a recurring component

which is also paid to the Adviser. Fees for certain of these services are credited 50% against the base management fee payable to the Adviser pursuant to the terms of our advisory agreement, which has the effect of reducing our expenses to the extent of any such credits. The specific other services the Adviser provides vary by portfolio company, but generally include a broad array of services to the portfolio companies such as investment banking services, arranging bank financing, arranging equity financing, structuring financing from multiple lenders and investors, reviewing existing credit facilities, restructuring existing investments, raising equity and debt capital, turnaround management, merger and acquisition services and recruiting new management personnel. To date the Adviser has not charged for managerial assistance services, however, if the Adviser does receive fees for such managerial assistance, the Adviser will credit the managerial assistance fees to the base management fee due from us to the Adviser.

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

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

During the nine months ended June 30, 2007, we extended, directly or through participations or acquisitions, approximately $253.7 million of new loans to a total of 52 companies. This includes an acquisition of approximately $63.3 million in senior debt with 16 different borrowers in June 2007. Also, during the nine months ended June 30, 2007, four borrowers repaid their loans ahead of contractual maturity, one borrower refinanced its investment and we sold or were repaid in full on twenty four syndicated loans of approximately $90.8 million, and we received scheduled contractual principal repayments of approximately $9.0 million, for total principal repayments of approximately $99.8 million. Since our initial public offering in August 2001, we have made 227 different loans to, or investments in, 120 companies for a total of approximately $760.2 million, before giving effect to principal repayments on investments and divestitures.

These prospective loans are subject to, among other things, the satisfactory completion of our due diligence investigation of each borrower, acceptance of terms and structure and attainment of necessary consents. With respect to each prospective loan, we will only agree to provide the loan if, among other things, the results of our due diligence investigations are satisfactory, the terms and conditions of the loan are acceptable and all necessary consents are received. Our management has initiated its due diligence investigations of the potential borrowers, however we cannot assure you that we will not discover facts in the course of

completing our due diligence that would render a particular investment imprudent or that any of these loans will actually be made.

Our Investment Adviser and Administrator

Our Adviser is led by a management team which has extensive experience in our lines of business. Our Adviser is controlled by David Gladstone, our chairman and chief executive officer. Mr. Gladstone is also the chairman and chief executive officer of our Adviser. Terry Lee Brubaker, our vice chairman, chief operating officer, secretary and director, is a member of the board of directors of our Adviser and its vice chairman and chief operating officer. George Stelljes III, our president, chief investment officer and director, is a member of the board of directors of our Adviser and its president and chief investment officer. Harry Brill, our chief financial officer, is also the chief financial officer of our Adviser. Our Adviser also has a wholly-owned subsidiary, Gladstone Administration, LLC (the "Administrator"), which employs our chief financial officer, chief compliance officer, controller, treasurer and their respective staffs.

Our Adviser and Administrator also provide investment advisory and administrative services to our affiliates, Gladstone Commercial Corporation, a publicly traded real estate investment trust; Gladstone Investment Corporation, a publicly traded business development company; and Gladstone Land Corporation, an agricultural real estate company owned by Mr. Gladstone. All of our directors and executive officers serve as either directors or executive officers, or both, of Gladstone Commercial Corporation and Gladstone Investment Corporation. In the future, our Adviser may provide investment advisory and administrative services to other funds, both public and private, of which it is the sponsor.

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

Investment Advisory and Management Agreement

On December 2, 2005, our stockholders approved a proposal to enter into an amended and restated investment advisory agreement (the "Amended Advisory Agreement") with the Adviser and an administration agreement (the "Administration Agreement") between us and our Administrator, both of which became effective on October 1, 2006. The Amended Advisory Agreement replaced the original advisory agreement (the "Initial Advisory Agreement"), which terminated on September 30, 2006. We will continue to pay our direct expenses including, but not limited to, directors' fees, legal and accounting fees, stockholder related expenses, and directors and officers insurance under the Amended Advisory Agreement.

Pursuant to the Initial Advisory Agreement, we paid the Adviser an annual advisory fee of 1.25% of our total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.3125%, and an annual administrative fee of 0.75% of our total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.1875%, for a total annual base management fee of 2%. This fee was then directly reduced by the amount of loan servicing fees paid to the Adviser and any other fees received by the Adviser from our borrowers and potential borrowers.

Under the Amended Advisory Agreement, we pay the Adviser an annual base management fee of 2% of our average gross assets, which is defined as total assets less cash and cash equivalents pledged to creditors calculated as of the end of the two most recently completed fiscal quarters and also consists of a two-part incentive fee.

The first part of the incentive fee is an income-based incentive fee which 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 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% 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 incentive fee that will be determined and payable in arrears as of the end of each fiscal year (or upon termination of the Amended Advisory Agreement, as of the termination date), commencing on October 1, 2006, and will equal 20% of our realized capital gains as of the end of the fiscal year. In determining the capital gains 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 unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in our portfolio.

The Adviser's board of directors has agreed to voluntarily waive 1.5% of the annual 2.0% base management fee to 0.5% for senior syndicated loans for the three and nine months ended June 30, 2007.

In addition to the base management and incentive fees under the Amended Advisory Agreement, certain fees received by the Adviser from our portfolio companies were credited against the investment advisory fee under the Initial Advisory Agreement, and will continue to be paid to the Adviser and credited under the Amended Advisory Agreement.

The Adviser services our loan portfolio pursuant to a loan servicing agreement with Gladstone Business Loan, LLC ("Business Loan") in return for a 1.5% annual fee, based on the monthly aggregate outstanding loan balance of the loans pledged under our credit facility. Effective in April 2006, the Adviser's board of directors voted to reduce the portion of the 1.5% annual fee to 0.5% for senior syndicated loans. This fee directly reduces the amount of fee payable under both the Initial and Amended Advisory Agreements.

Administration Agreement

Under the Administration Agreement, we pay separately for administrative services. The Administration Agreement provides for payments equal to our allocable portion of the Administrator's overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent for employees of the Administrator, and our allocable portion of the salaries and benefits expenses of our chief financial officer, controller, chief compliance officer, treasurer and their respective staffs. Our allocable portion of expenses is derived by multiplying our Administrator's total expenses by the percentage of

our average total assets (the total assets at the beginning and end of each quarter) in comparison to the average total assets of all companies managed by our Adviser.

Off-Balance Sheet Arrangements

We do not have any significant off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Securities and Exchange Commission ("SEC") Regulation S-K as of June 30, 2007.

Recent Accounting Pronouncements

In May 2005, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 154, *"Accounting Changes and Error Corrections,"* a replacement of APB Opinion No. 20, *"Accounting Changes,"* and SFAS No. 3, *"Reporting Accounting Changes in Interim Financial Statements"* and changes the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 applies to all voluntary changes in accounting principle and also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. SFAS No. 154 requires retrospective application to prior periods' financial statements of changes in accounting principle. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. We adopted the provisions of SFAS No. 154, as applicable, on October 1, 2006.

In February 2006, the FASB issued SFAS No. 155, *"Accounting for Certain Hybrid Financial Instruments, an amendment of FASB statements No. 133 and 140"* ("SFAS No. 155"). SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) as long as the entire instrument is valued on a fair value basis. The statement also resolves and clarifies other specific SFAS No. 133 and SFAS No. 140 related issues. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. We adopted SFAS No. 155 on October 1, 2006 and have not realized a material impact of the financial statements since all investments are valued on a fair value basis.

In June 2006, the FASB issued FASB Interpretation No. 48, *"Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109,"* which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, *"Accounting for Income Taxes."* This Statement shall be effective as of the beginning of an entity's first fiscal year that begins after December 15, 2006. We will adopt this Interpretation effective October 1, 2007, and are currently evaluating the impact of this pronouncement on the consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"* ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP, and expands disclosures about fair value measurements. SFAS No. 157 applies broadly to securities and other types of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within that fiscal year. We will be required to adopt SFAS No. 157 on October 1, 2008 and are currently evaluating the impact of this pronouncement on the consolidated financial statements.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108 ("SAB 108"). SAB 108 addresses how the effects of prior year uncorrected misstatements should be

considered when quantifying misstatements in current year financial statements and requires registrants to consider the effect of all carry over and reversing effects of prior year misstatements when quantifying errors in current year financial statements. SAB 108 does not change the SEC's previous guidance in SAB No. 99, *"Materiality,"* on evaluating the materiality of misstatements. A registrant applying the new guidance for the first time that identifies material errors in existence at the beginning of the first fiscal year ending after November 15, 2006, may correct those errors through a one-time cumulative effect adjustment to beginning-of-year retained earnings. The cumulative effect alternative is available only if the application of the new guidance results in a conclusion that a material error exists as of the beginning of the first fiscal year ending after November 15, 2006, and those misstatements were determined to be immaterial based on a proper application of the registrant's previous method for quantifying misstatements. The adoption of SAB 108 did not have an impact on the consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *"The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115,"* which is effective for fiscal years beginning after November 15, 2007. This pronouncement permits an entity to choose to measure many financial instruments and certain other items at fair value at specified election dates. Subsequent unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. We are currently evaluating the potential impact of this pronouncement on the consolidated financial statements.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported consolidated amounts of assets and liabilities, and 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. Our accounting policies are more fully described in the "Notes to Consolidated Financial Statements" contained elsewhere in this prospectus supplement. 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 investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

General Valuation Policy: Using procedures established by our Board of Directors, we value our investment portfolio each quarter. We carry our investments at fair value, as determined in good faith by or under the direction of our Board of Directors. Securities that are publicly traded, if any, are valued at the closing price of the exchange or securities market on which they are listed on the valuation date. Securities that are not traded on a public exchange or securities market, but for which a limited market exists and that have been rated by a nationally recognized statistical rating organizations, ("NRSRO"), (such as certain participations in syndicated loans) are valued at the indicative bid price offered by the respective originating syndication agent's desk on or near the valuation date.

Debt and equity securities that are not publicly traded, for which a limited market does not exist, or for which a limited market exists but that have not been rated by a NRSRO (or

for which we have various degrees of trading restrictions) are valued at fair value as determined in good faith by or under the direction of our Board of Directors. In making the good faith determination of the value of these securities, we start with the cost basis of the security, which includes the amortized OID and PIK interest, if any. We then apply the methods set out below in *"Valuation Methods."* Members of our Adviser's portfolio management team prepare the valuations of our investments in portfolio companies using the most recent portfolio company financial statements and forecasts. These individuals also consult with portfolio company senior management and ownership to obtain further updates on the portfolio company's performance, including information such as industry trends, new product development, and other operational issues. Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly from the values that would have been obtained had a ready market for the securities existed, and the differences could be material. Additionally, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. There is no single standard for determining fair value in good faith, as fair value depends upon circumstances of each individual case. In general, fair value is the amount that we might reasonably expect to receive upon the current sale of the security.

At June 30, 2007, we engaged Standard & Poor's Securities Evaluations, Inc. ("SPSE") to submit opinions of value for most of our loan securities. We request that SPSE also evaluate and assign values to success fees (conditional interest included in some loan securities) when we determine that the probability of receiving a success fee on a given loan is above 6-8%, a threshold of significance. We may also submit paid in kind ("PIK") interest to SPSE for valuation when it is determined the PIK interest is likely to be received. SPSE will only evaluate the debt portion of our investments for which we specifically request evaluation, and may decline to make requested evaluations for any reason at its sole discretion. We also add any amortized original issue discount ("OID") interest to the fair value, unless adverse factors lead to a determination of a lesser valuation. Upon completing our collection of data with respect to the investments (including the information described under *"Credit Information,"* the risk ratings of the loans described under *"Loan Grading and Risk Rating"* and the factors described under *"Valuation Methods"*), this valuation data is forwarded along to SPSE for review and analysis. SPSE makes its independent assessment of the data that we have assembled and assesses its independent data to form an opinion as to what they consider to be the market values for the securities. With regard to its work, SPSE has issued the following paragraph:

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

SPSE opinions of value are submitted to our Board of Directors along with our Adviser's supplemental assessment and recommendation regarding valuation of each of these investments. Our Adviser generally accepts the opinion of value given by SPSE, however, in certain limited circumstances, such as when our Adviser may learn new information regarding an investment between the time of submission to SPSE and the date of the Board

assessment, our Adviser's conclusions as to value may differ from the opinion of value delivered by SPSE. Our Board of Directors then reviews whether our Adviser has followed its established procedures for determinations of fair value, and votes whether to accept the recommended valuation of our investment portfolio. Our Adviser and our management recommended, and the Board of Directors voted to accept, the opinions of value delivered by SPSE on the loans in our portfolio as denoted on the schedule of investments as of June 30, 2007 and September 30, 2006, included in our consolidated financial statements.

Because there is a delay between when we close an investment and when the investment can be evaluated by SPSE, new loans are not valued immediately by SPSE; rather, management makes its own determination about the value of these investments in accordance with our valuation policy. Because SPSE does not provide values for our equity securities, our Adviser determines the fair value of these investments using valuation policies approved by our Board of Directors.

Credit Information: Our Adviser monitors a wide variety of key credit statistics that provide information regarding our portfolio companies to help us assess credit quality and portfolio performance. If we held a controlled or affiliate investment, we and our Adviser would participate in periodic board meetings of such portfolio companies and also require them to provide annual audited and monthly unaudited financial statements. Using these statements and board discussions, our Adviser would calculate and evaluate the credit statistics.

Loan Grading and Risk Rating: As part of our valuation procedures we risk rate all of our investments in debt securities. For syndicated loans that have been rated by a NRSRO (as defined in Rule 2a-7 under the 1940 Act), we use the NRSRO's risk rating for such security. For all other debt securities, we use a proprietary risk rating system. Our risk rating system uses a scale of 0 to 10, with 10 being the lowest probability of default. This system is used to estimate the probability of default on debt securities and the probability of loss if there is a default. These types of systems are referred to as risk rating systems and are used by banks and rating agencies. The risk rating system covers both qualitative and quantitative aspects of the business and the securities we hold.

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

equivalent to a BBB from a NRSRO, however, no assurance can be given that a 10 on our scale is equal to a BBB on a NRSRO scale.

Company's ystem	First NRSRO	Second NRSRO	Gladstone Capital's Description (a)
>10	Baa2	BBB	Probability of Default (PD during the next ten years is 4% and the Expected Loss (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 here are for a ten year term debt security. If the company's debt security is less than ten years then the probability of default is adjusted to a lower percentage for the shorter period which may move the security higher on our risk rating scale.

The above scale gives an indication of the probability of default and the magnitude of the loss if there is a default. Our policy is to stop accruing interest on an investment if we determine that interest is no longer collectible. Currently, our investment in MCA Communications LLC is on non-accrual, the investment is currently not accruing interest nor is it paying any past due interest. Additionally, we do not risk rate our equity securities.

The following table lists the risk ratings for all non-syndicated loans in our portfolio at June 30, 2007 and September 30, 2006, representing approximately 76% and 73%, respectively, of all loans in our portfolio:

Rating	June 30, 2007	Sept. 30, 2006
Average	**7.1**	**7.2**
Weighted Average	**7.0**	**7.2**
Highest	**9.0**	**9.0**
Lowest	**4.0**	**6.0**

The following table lists the risk ratings for syndicated loans in our portfolio that are not currently rated by an NRSRO at June 30, 2007 and September 30, 2006, representing approximately 6% and 17%, respectively, of all loans in our portfolio:

Rating	June 30, 2007	Sept. 30, 2006
Average	**6.0**	**6.1**
Weighted Average	**6.0**	**6.3**
Highest	**6.0**	**8.0**
Lowest	**6.0**	**4.0**

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

portfolio that are currently rated by an NRSRO at June 30, 2007 and September 30, 2006, representing approximately 18% and 10%, respectively, of all loans in our portfolio:

Rating	June 30, 2007	Sept. 30, 2006
Average	**CCC+/Caa1**	**CCC+/Caa1**
Weighted Average	**CCC+/Caa1**	**CCC+/Caa1**
Highest	**B/B3**	**B-/B3**
Lowest	**CCC/Caa2**	**CCC/Caa1**

Valuation Methods: We determine the value of publicly-traded debt securities based on the closing price for the security on the exchange or securities market on which it is listed on the valuation date. We value debt securities that are not publicly traded, but for which a limited market for the security exists, such as certain participations in syndicated loans, at the indicative bid price offered by the respective originating syndication agent's trading desk on or near the valuation date. At June 30, 2007, none of the debt securities in our portfolio were publicly traded and there was a limited market for 31 debt securities in our portfolio. At September 30, 2006, none of the debt securities in our portfolio were publicly traded and there was a limited market for 9 debt securities in our portfolio.

Debt securities that are issued to portfolio companies where we have an equity, or equity-like interest that are not publicly traded, for which there is no market, or for which there is a market but the securities have not been rated by a NRSRO, are valued at cost, if there is adequate total enterprise value determined when valuing our equity holdings in the borrower. Fair values are discounted for any shortfall of total enterprise value over the total debt outstanding for the borrower. At June 30, 2007, for our debt investment in Clinton Aluminum Holdings LLC, where we hold a warrant, we solicited and were provided an opinion of value by SPSE. Prospectively, in accordance with our valuation policies, due to its accompanying equity-like security, the debt securities for this investment will not be assessed by SPSE.

Debt securities that are not publicly traded and that are issued to portfolio companies where we have no equity or equity-like securities, for which there is no market, or for which there is a market but have not been rated by a NRSRO, we begin with the risk rating designation of the security as described above. Using this risk rating designation, we seek to determine the value of the security as if we currently intended to sell the security and consider some or all of the following factors:

- the cost basis and the type of the security;
- the nature and realizable value of the collateral;
- the portfolio company's ability to make payments and discounted cash flow;
- reports from portfolio company senior management and board meetings;
- reported values of similar securities of the portfolio company or comparable companies; and
- changes in the economy affecting the portfolio company.

We value convertible debt, equity, success or exit fees or other equity-like securities for which there is a market based on the market prices for such securities, even if that market is not robust. At June 30, 2007 and September 30, 2006, there was no market for any of the equity securities we owned. To value equity securities for which no market exists, we use the same information we would use for a debt security valuation described above, except risk-rating, as well as standard valuation techniques used by major valuation firms to value

the equity securities of private companies. These valuation techniques also include discounted cash flow of the expected sale price in the future, valuation of the securities based on recent sales to third parties in comparable transactions, or a review of similar companies that are publicly traded and the market multiple of their equity securities. In gathering the sales to third parties of similar securities, we may reference industry statistics and use outside experts. At June 30, 2007 and September 30, 2006, we had $146,124 and $37,000, respectively, invested, at cost, in equity securities compared to our debt portfolio with a cost basis of $369,829,274 and $216,165,986, respectively.

At June 30, 2007, we had total unrealized depreciation of $4,288,673, which was mainly comprised of unrealized deprecation of $1,375,000 on our senior subordinated term debt investment in Visual Edge Technology, Inc., unrealized depreciation of $1,022,250, on the aggregate of our investments in LocalTel, Inc. and unrealized depreciation of $282,750 on our senior term debt investment in It's Just Lunch International, LLC. Unrealized appreciation of $3,262,522 was primarily composed of unrealized appreciation of $2,935,858 on our warrants in Finn Corporation. In the aggregate, we recorded net unrealized depreciation of $1,026,151 on our total investment portfolio as of June 30, 2007.

At September 30, 2006, we had total unrealized appreciation of $2,015,198, which was mainly comprised of unrealized appreciation of $672,431 on our warrants of Finn Corporation, unrealized appreciation of $607,625 on our senior term debt in Mistras Holding Corporation and unrealized appreciation of $148,287 on our senior subordinated term debt investment in Xspedius Communications, LLC. This unrealized appreciation was offset by unrealized depreciation of $575,434, most notably composed of unrealized depreciation of $131,367 on our senior subordinated term debt investment in Consolidated Bedding, Inc. and unrealized depreciation of $115,750 on our senior term debt in LocalTel Inc. In the aggregate, we recorded net unrealized appreciation of $1,439,764 on our total investment portfolio as of September 30, 2006.

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 are required to distribute to stockholders at least 90% of our investment company taxable income, as defined by the Code. We have a policy to pay out as a dividend up to 100% of that amount.

In an effort to avoid certain excise taxes imposed on RICs, we currently intend to 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% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and net capital gains for preceding years that were not distributed during such years.

Revenue Recognition

Interest Income Recognition

Interest income is recorded on the accrual basis to the extent that such amounts are expected to be collected. We will stop accruing interest on investments and write off any previously accrued and uncollected interest when it is determined that interest is no longer collectible. Conditional interest or a success fee is recorded when earned upon full repayment of a loan investment.

Paid in Kind Interest

In the future, we may hold loans in our portfolio which contain a PIK interest provision. The PIK interest, computed at the contractual rate specified in each loan agreement, is added to the principal balance of the loan and recorded as interest income. To maintain our status as a RIC, this non-cash source of income must be paid out to stockholders in the form of dividends, even though we have not yet collected the cash.

Results of Operations

Comparison of the Three Months Ended June 30, 2007 to the Three Months Ended June 30, 2006

Investment Income

Investment income for the three months ended June 30, 2007 was $9,201,279, as compared to $6,522,816 for the three months ended June 30, 2006.

Interest income from our investments in debt securities of private companies was $8,911,643 for the three months ended June 30, 2007, as compared with $5,775,522 for the three months ended June 30, 2006. This increase consisted of approximately $88.5 million of net new investments. As a result of repayments by Allied Extruders LLC, and SCPH Holdings during the three months ended June 2007, we recorded success fees of approximately $515,000. In June 2007, we purchased a senior debt portfolio of approximately $63.3 million to 16 different lenders, which is included in the net new investments described above

The annualized weighted average yield on our portfolio for the three months ended June 30, 2007 was 11.8%; there was no PIK interest accrued during the three months ended June 30, 2007. The annualized weighted average yield on our portfolio for the three months ended June 30, 2006 was 11.7% (with and without giving effect to PIK interest).

Interest income from invested cash and cash equivalents for the three months ended June 30, 2007 was $109,269, as compared to $8,178 for the three months ended June 30, 2006. Interest income increased from the prior year due to the amount of cash that was held in interest bearing accounts and the interest earned on our custodial account prior to disbursement.

For the three months ended June 30, 2007 and June 30, 2006, we recorded $132,795 and $108,877, respectively, in interest income from loans to our employees in connection with the exercise of employee stock options. The increase is the result of additional loans issued in connection with employee stock option exercises during the fourth quarter of the previous fiscal year.

For the three months ended June 30, 2007, we recorded $47,572 of prepayment fees and other income, as compared to $630,239 for the three months ended June 30, 2006. The income for both periods consisted of prepayment penalty fees received upon the full repayment of certain loan investments ahead of contractual maturity and prepayment fees received upon the early unscheduled principal repayments which, in both instances, were based on a percentage of the outstanding principal amount of the loan at the date of prepayment.

Operating Expenses

Operating expenses, prior to credit from the Adviser for fees earned and voluntary waivers to the base management fees and incentive fees, for the three months ended June 30, 2007 were $5,205,300, as compared to $2,277,508 for the three months ended

June 30, 2006. Operating expenses for the three months ended June 30, 2007 reflected a significant increase in interest expense and management fees, prior to credits, as well as the addition of the incentive and administration fees, prior to credits, under the Amended Advisory and Administration Agreements.

Loan servicing fees of $897,634 were incurred for the three months ended June 30, 2007, as compared to $693,965 for the three months ended June 30, 2006. These fees were incurred in connection with a loan servicing agreement between Business Loan and our Adviser, which is based on the size of the portfolio. These fees were reduced against the amount of the base management fee due to our Adviser.

For the three months ended June 30, 2007, we incurred a base management fee of $727,259, after reductions for loan servicing fees received by our Adviser of $897,634, less credits for fees received by our Adviser of $530,875 and a $139,261 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee of $57,123 as compared to the three months ended June 30, 2006, in which we incurred a base management fee of $334,814 after reductions for loan servicing fees received by our Adviser of $693,965, less credits for fees received by our Adviser of $539,000 and a $3,774 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management credit of $207,960. The base management fee is computed quarterly as described under *"Investment Advisory and Management Agreement."* Effective April 1, 2007, the board of our Adviser reduced the amount of credit for fees received by our Adviser from 100% of the fees received to 50% of the fees received, therefore the three months ended June 30, 2007 reflects the reduced credit for fees received by our Adviser. The gross base management fee before the reduction for loan servicing fees for the three months ended June 30, 2007 and June 30, 2006, was $1,624,893 and $1,028,779, respectively, increased in the current period due to the growth of the investment portfolio as compared to the same period of the prior year.

Effective October 1, 2006, the income based incentive fee became effective and as such we recorded a gross incentive fee of $1,166,529, which was reduced by a voluntary waiver issued by our Adviser's board of directors of $1,038,752, which resulted in a net incentive fee of $127,777, which is recorded in fees due to Adviser on our consolidated statements of assets and liabilities at June 30, 2007. There was no incentive fee recorded for the three months ended June 30, 2006, as the Amended Advisory Agreement was not in effect.

Effective October 1, 2006, the Administration Agreement became effective in which we provide payments equal to our allocable portion of our Administrator's overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent for employees of our Administrator, and our allocable portion of the salaries and benefits expenses of our chief financial officer, chief compliance officer and controller and their respective staffs. We incurred an administration fee of $186,895 for the three months ended June 30, 2007. There was no administration fee recorded during the three months ended June 30, 2006, as the Administration Agreement was not in effect.

Professional fees, consisting primarily of legal and audit fees, for the three months ended June 30, 2007 were $148,609, as compared to $166,405 for the three months ended June 30, 2006. The decrease is due to the reimbursement of certain legal fees at the time of the investment funding.

Amortization of deferred financing costs, in connection with our line of credit, was $72,133 for the three months ended June 30, 2007 and $36,036 for the three months ended June 30, 2006. The increase is due to the amortization of additional fees incurred with our line of credit which were not in place during the prior year period.

Interest expense for the three months ended June 30, 2007 was $1,762,249, as compared to $702,449 for the three months ended June 30, 2006. This increase is primarily a result of increased borrowings under our line of credit during the three months ended June 30, 2007, which borrowings were partially used to finance our increased investments, borrowings remaining outstanding for longer periods of time and an increase in the interest rates on our borrowings.

Stockholder related costs for the three months ended June 30, 2007 were $39,434, as compared to $28,371 for the three months ended June 30, 2006. Stockholder related costs include such recurring items as transfer agent fees, NASDAQ listing fees, SEC filing fees and annual report printing fees. These fees increased during the three months ended June 30, 2007 due to additional filing fees as compared to the prior year.

Directors' fees for the three months ended June 30, 2007 were $56,250, as compared to $27,500 for the three months ended June 30, 2006 due to the increase in annual stipend fees and their related monthly amortization.

Insurance expense for the three months ended June 30, 2007 was $66,246, as compared to $50,589 for the three months ended June 30, 2006. The increase was primarily the result of an increase in the amortization of our directors and officers insurance policy premiums.

There was no stock option compensation expense recorded for the three months ended June 30, 2007 as there was no longer a stock option plan in effect. Stock option compensation expense for the three months ended June 30, 2006 was $202,296 and was the result of the adoption of the SFAS No. 123 (revised 2004) "*Share-based Payment.*"

Other expenses were $82,062 for the three months ended June 30, 2007, as compared to $35,083 for the three months ended June 30, 2006. The expenses primarily represent direct expenses such as travel related specifically to our portfolio companies, loan evaluation services for our portfolio companies, press releases and backup servicer expenses.

Net Realized Gain (Loss) on Sale of Investments

During the three months ended June 30, 2007, we sold or were repaid in full on eleven syndicate loan investments for a net loss of $5,021, as compared to a realized net loss of $100,850 as a result of the repayment in full of syndicate investments that contained unamortized premiums during the three months ended June 30, 2006.

Realized Gain on Settlement of Derivative

During the three months ended June 30, 2007, we received interest rate cap agreement payments of $8,405 as a result of the one month LIBOR exceeding 5% as compared to $1,367 during the three months ended June 30, 2006.

Net Unrealized Depreciation on Derivative

During the three months ended June 30, 2007, we recorded net unrealized depreciation of $264 due to a decrease in the fair market value of our interest rate cap agreement, as compared to unrealized appreciation of $41,486 during the three months ended June 30, 2006.

Net Unrealized Appreciation on Investments

For the three months ended June 30, 2007, we recorded net unrealized appreciation on investments of $256,613, as compared to net unrealized appreciation of $812,991, for the three months ended June 30, 2006. The unrealized appreciation is mainly attributable to the

increase in fair value on our portfolio due to the repayment in full of certain underperforming investments, most notably Consolidated Bedding, Inc.

Net Increase in Net Assets from Operations

Overall, we realized a net increase in net assets resulting from operations of $5,964,600 for the three months ended June 30, 2007. Based on a weighted-average of 13,561,511 basic and diluted shares outstanding, our net increase in net assets from operations per weighted-average common share for the three months ended June 30, 2007 was $0.44, basic and diluted.

For the three months ended June 30, 2006, we realized a net increase in net assets resulting from operations of $5,543,076. Based on a weighted-average of 11,337,291 (basic) and 11,570,425 (diluted) shares outstanding, our net increase in net assets from operations per weighted-average common share for the three months ended June 30, 2006 was $0.49 (basic) and $0.48 (diluted).

Comparison of the Nine months ended June 30, 2007 to the Nine months ended June 30, 2006

Investment Income

Investment income for the nine months ended June 30, 2007 was $26,078,775, as compared to $19,553,835 for the nine months ended June 30, 2006.

Interest income from our investments in debt securities of private companies was $25,064,702 for the nine months ended June 30, 2007 as compared with $18,497,893 for the nine months ended June 30, 2006, which included $63,217 of PIK interest. This increase consisted of net new investments of approximately $153.9 million for the nine months ended June 30, 2007, as compared to net new investments of approximately $2.8 million for the nine months ended June 30, 2006. As a result of a refinancing by Badanco Acquisition Corp. and a full repayment by Mistras Holdings Corp., Allied Extruders LLC, and SCPH Holdings we recorded success fees of approximately $2,250,000 during the nine months ended June 30, 2007. In June 2007, we purchased a senior debt portfolio of approximately $63.3 million to 16 different lenders, which is included in the net new investments described above.

The annualized weighted average yield on our portfolio for the nine months ended June 30, 2007 was 12.3%; there was no PIK interest accrued during the nine months ended June 30, 2007. The annualized weighted average yield on our portfolio for the nine months ended June 30, 2006 was 12.3% (with and without giving effect to PIK interest).

Interest income from invested cash and cash equivalents for the nine months ended June 30, 2007 was $178,183, as compared to $21,714 for the nine months ended June 30, 2006. Interest income increased from the prior year due to the amount of cash that was held interest bearing accounts and the interest earned on our custodial account prior to disbursement.

For the nine months ended June 30, 2007 and June 30, 2006, we recorded $403,917 and $323,003, respectively, in interest income from loans to our employees in connection with the exercise of employee stock options. The increase is the result of additional loans issued in connection with employee stock option exercises during the fourth quarter of the previous fiscal year.

For the nine months ended June 30, 2007, we recorded $431,973 of prepayment fees and other income, as compared to $711,225 for the nine months ended June 30, 2006. The income

for both periods consisted of prepayment penalty fees received upon the full repayment of certain loan investments ahead of contractual maturity and prepayment fees received upon the early unscheduled principal repayments which, in both instances, were based on a percentage of the outstanding principal amount of the loan at the date of prepayment.

Operating Expenses

Operating expenses, prior to credit from the Adviser for fees earned and voluntary waivers to the base management and incentive fees, for the nine months ended June 30, 2007 were $14,168,785, as compared to $6,835,060 for the nine months ended June 30, 2006. Operating expenses for the nine months ended June 30, 2007 reflected a significant increase in interest expense and management fees, prior to credits, as well as the addition of the incentive and administration fees, prior to credits, under the Amended Advisory and Administration Agreements.

Loan servicing fees of $2,377,409 were incurred for the nine months ended June 30, 2007, as compared to $2,144,024 for the nine months ended June 30, 2006. These fees were incurred in connection with a loan servicing agreement between Business Loan and our Adviser, which is based on the size of the portfolio. These fees were reduced against the amount of the base management fee due to our Adviser.

For the nine months ended June 30, 2007, we incurred a base management fee of $1,806,075 after reductions for loan servicing fees received by our Adviser of $2,377,409, less credits for fees received by our Adviser of $1,616,875 and a $369,161 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee credit of $179,961, as compared to the nine months ended June 30, 2006, in which we incurred a base management fee of $955,894 after reductions for loan servicing fees received by our Adviser of $2,144,024, less credits for fees received by our Adviser of $1,762,000 and a $3,774 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management credit of $809,880. The base management fee is computed quarterly as described under *"Investment Advisory and Management Agreement."* Effective April 1, 2007, the board of our Adviser reduced the amount of credit for fees received by our Adviser from 100% of the fees received to 50% of the fees received, therefore, the three months ended June 30, 2007 reflect the reduced credit for fees received by our Adviser. The gross base management fee before the reduction for loan servicing fees for the nine months ended June 30, 2007 and June 30, 2006, was $4,183,484 and $3,099,918, respectively, which increased in the current period due to the growth of the investment portfolio as compared to the same period of the prior year and fewer credits for fees received by our Adviser.

Effective October 1, 2006, the income based incentive fee became effective and as such we recorded a gross incentive fee of $3,474,007, which was reduced by a voluntary waiver issued by our Adviser's board of directors of $2,696,124, which resulted in a net incentive fee of $777,883, which is recorded in fees due to Adviser on our consolidated statements of assets and liabilities at June 30, 2007. There was no incentive fee recorded for the nine months ended June 30, 2006, as the Amended Advisory Agreement was not in effect.

Effective October 1, 2006, the Administration Agreement became effective in which we provide payments equal to our allocable portion of our Administrator's overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent for employees of our Administrator, and our allocable portion of the salaries and benefits expenses of our chief financial officer, chief compliance officer and controller and their respective staffs. We incurred an administration fee of $481,746 for the nine months ended

June 30, 2007. There was no administration fee recorded during the nine months ended June 30, 2006, as the Administration Agreement was not in effect.

Professional fees, consisting primarily of legal and audit fees, for the nine months ended June 30, 2007 were $368,610, as compared to $399,758 for the nine months ended June 30, 2006. The slight decrease is due to the reimbursement of certain legal fees at the time of investment funding.

Amortization of deferred financing costs, in connection with our line of credit, was $198,633 for the nine months ended June 30, 2007 and $94,572 for the nine months ended June 30, 2006. The increase is due to the amortization of additional fees incurred with our line of credit which were not in place during the prior year period.

Interest expense for the nine months ended June 30, 2007 was $4,693,525, as compared to $2,302,693 for the nine months ended June 30, 2006. This increase is primarily a result of increased borrowings under our line of credit during the nine months ended June 30, 2007, which borrowings were partially used to finance our increased investments, borrowings remaining outstanding for longer periods of time and an increase in the interest rates on our borrowings.

Stockholder related costs for the nine months ended June 30, 2007 were $190,450, as compared to $273,170 for the nine months ended June 30, 2006. Stockholder related costs include such recurring items as transfer agent fees, NASDAQ listing fees, SEC filing fees and annual report printing fees. These fees decreased during the nine months ended June 30, 2007 since there were no special proxy solicitation or stock option termination notices filed as there were during the nine months ended June 30, 2006.

Directors' fees for the nine months ended June 30, 2007 were $167,470, as compared to $81,712 for the nine months ended June 30, 2006 due to the increase in annual stipend fees and their related monthly amortization.

Insurance expense for the nine months ended June 30, 2007 was $191,338, as compared to $151,956 for the nine months ended June 30, 2006. The increase is primarily the result of an increase in the amortization of our directors and officers insurance policy premiums.

There was no stock option compensation expense recorded for the nine months ended June 30, 2007 as there was no longer a stock option plan in effect. Stock option compensation expense for the nine months ended June 30, 2006 was $279,618 and was the result of the adoption of the SFAS No. 123 (revised 2004) "*Share-based Payment*."

Other expenses were $219,552 for the nine months ended June 30, 2007, as compared to $151,663 for the nine months ended June 30, 2006. The expenses primarily represent direct expenses such as travel related specifically to our portfolio companies, loan evaluation services for our portfolio companies, press releases and backup servicer expenses.

Income Tax Expense

During the nine months ended June 30, 2006, Gladstone Capital Corporation recorded approximately $50,000 in connection with penalties incurred on misclassified revenue on its fiscal year 2004 corporate tax return.

Net Realized Gain (Loss) on Sale of Investments

During the nine months ended June 30, 2007, we sold or were repaid in full on 24 syndicate loan investments for a net gain of $81,498, as compared to an aggregate net loss of $903,945, which was composed of $1,180,595 loss from the sale of two investments and a net

gain of $276,650 from the sale and repayments of syndicate investments during the nine months ended June 30, 2006.

Realized Gain on Settlement of Derivative

During the nine months ended June 30, 2007, we received interest rate cap agreement payments of $31,198 as a result of the one month LIBOR exceeding 5%, as compared to $1,367 received during the nine months ended June 30, 2006.

Net Unrealized (Depreciation) Appreciation on Derivative

During the nine months ended June 30, 2007, we recorded net unrealized depreciation of $25,877 due to a decrease in the fair market value of our interest rate cap agreement, as compared to unrealized appreciation of $65,252 during the nine months ended June 30, 2006.

Net Unrealized (Depreciation) Appreciation on Investments

For the nine months ended June 30, 2007, we recorded net unrealized depreciation on investments of $2,465,915, as compared to net unrealized appreciation of $5,769,820, for the nine months ended June 30, 2006. The unrealized depreciation is mainly attributable to the depreciated fair value on certain investments, most notably unrealized depreciation on Its Just Lunch International LLC, LocalTel, Inc. and Visual Edge Technology, Inc., partially offset by appreciation of our warrants in Finn Corporation.

Net Increase in Net Assets from Operations

Overall, we realized a net increase in net assets resulting from operations of $14,213,054 for the nine months ended June 30, 2007. Based on a weighted-average of 12,701,845 basic and diluted shares outstanding, our net increase in net assets from operations per weighted-average common share for the nine months ended June 30, 2007 was $1.12, basic and diluted.

For the nine months ended June 30, 2006, we realized a net increase in net assets resulting from operations of $19,366,806. Based on a weighted-average of 11,317,437 (basic) and 11,549,054 (diluted) shares outstanding, our net increase in net assets from operations per weighted-average common share for the nine months ended June 30, 2006 was $1.71 (basic) and $1.68 (diluted).

Liquidity and Capital Resources

At June 30, 2007, we had investments in debt securities of, or loans to, 59 private companies, totaling approximately $370.0 million (cost basis) of total assets.

During the nine months ended June 30, 2007 and June 30, 2006, the following investment activity occurred:

Quarter Ended	New Investments	Principal Repayments	Net Gain/(Loss) on Disposal
June 30, 2007	$ 126,086,654	$ 37,572,621	$ (5,021)
March 31, 2007	75,330,167	38,263,017	84,205
December 31, 2006	52,311,008	23,967,229	2,314
	$ 253,727,829	$ 99,802,867	$ 81,498
June 30, 2006	$ 39,916,834	$ 44,358,944	$ (100,850)
March 31, 2006	38,471,109	24,815,067	377,500
December 31, 2005	26,688,457	38,702,066	(1,180,595)
	$ 105,076,400	$ 107,876,077	$ (903,945)

The following table summarizes the contractual principal amortization and maturity of our investment portfolio by fiscal year:

Fiscal Year Ended September 30,	Amount
2007	$ 8,358,133
2008	9,922,956
2009	26,109,512
2010	43,759,511
2011	94,200,816
Thereafter	187,624,470
	$ 369,975,398

Net cash used in operating activities for the nine months ended June 30, 2007, consisting primarily of the items described in *"Results of Operations"* and the investment activity described above, was approximately $136.6 million as compared to net cash provided by operating activities of approximately $17.8 million for the nine months ended June 30, 2006. Net cash provided by investing activities consisted of $300,941 and $129,943 for the nine months ended June 30, 2007 and June 30, 2006, respectively, and consisted of the principal repayments of employee loans. Net cash provided by financing activities for the nine months ended June 30, 2007 was approximately $139.1 million and mainly consisted of an offering of common stock for net proceeds of approximately $45.7 million, borrowings on our line of credit of approximately $277.8 million, offset by repayments on line of credit borrowings of approximately $166.6 million, and approximately $16.0 million for the payment of dividends. Net cash used in financing activities was approximately $18.0 million for the nine months ended June 30, 2006 and consisted primarily of net repayments on our line of credit of approximately $5.2 million and the payment of dividends of approximately $13.8 million.

During the nine months ended June 30, 2007, cash and cash equivalents increased from approximately $732,000 to approximately $3.5 million.

In order to qualify as a RIC and to 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 dividends of $0.14 per common share for July, August, September, October, November and December 2006 and January, February, March, April, May and June 2007 and $0.135 per

common share for January, February, March, April, May and June 2006, and October, November and December 2005. In July 2007, our Board of Directors declared a monthly dividend of $0.14 per common share for each of July, August, and September 2007.

We anticipate continuing to borrow funds and, from time to time issuing additional equity securities, to obtain additional capital to make further investments. On May 2, 2007, we completed a public offering of 2,000,000 shares of our common stock, at a price of $24.25 per share, under a shelf registration statement on Form N-2 (File No. 333-100385), and pursuant to the terms set forth in a prospectus dated April 16, 2007, as supplemented by a final prospectus dated April 27, 2007. Net proceeds of the offering, after underwriting discounts and offering expenses were approximately $45,669,292 and were used to repay outstanding borrowings under our line of credit. In May 2007, we filed with the SEC a new shelf registration statement on Form N-2 (File No. 333-143027) (the "Registration Statement") which the SEC declared effective on July 5, 2007 that would permit us to issue, through one or more transactions, up to an aggregate of $300 million in securities, consisting of common stock, preferred stock and/or debt securities. On July 24, 2007, we completed an offering of 400,000 shares of our common stock, at a price of $20.41 per share, under the Registration Statement, and pursuant to the terms set forth in a prospectus dated July 5, 2007, as supplemented by a final prospectus dated July 24, 2007. Net proceeds from the offering, after offering expenses, were approximately $8,149,000 and were used to repay outstanding borrowings under our line of credit. After the offering, we had the capacity to issue up to an aggregate of approximately $291.8 million in securities under the Registration Statement.

Revolving Credit Facilities

Through our wholly-owned subsidiary, Business Loan, we have a $220 million revolving credit facility (the "DB Facility") with Deutsche Bank AG, as administrative agent, which is scheduled to mature on May 23, 2008. Pursuant to the DB Facility, Business Loan has pledged the loans it holds to secure future advances by certain institutional lenders. Interest rates charged on the advances under the DB Facility will be based on LIBOR, the Prime Rate or the Federal Funds Rate, depending on market conditions, and will adjust periodically. As of June 30, 2007, our outstanding principal balance under the DB Facility was approximately $161.2 million at an interest rate of approximately 5.3%. Available borrowings are subject to various constraints imposed by Deutsche Bank AG, based on the aggregate loan balance pledged by Business Loan, which varies as loans are added and repaid, regardless of whether such repayments are early prepayment or are made as contractually required. At June 30, 2007, the remaining borrowing capacity available under the DB Facility was approximately $58.8 million.

The DB Facility contains covenants that, among other things, require Business Loan to maintain its status as a separate entity; prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions); and restrict material changes to our credit and collection policies. The DB Facility also restricts some of the terms and provisions (including interest rates, terms to maturity and payments schedules) and limits the borrower and industry concentrations of loans that are eligible to secure advances. As of June 30, 2007, Business Loan was in compliance with all of the DB Facility covenants. We currently intend to securitize all of the loans held by Business Loan and to use the proceeds from the securitization to pay down any amounts then outstanding under the revolving credit facility. However, there can be no assurance that we will be able to successfully securitize any of these loans on terms acceptable to us, if at all.

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

as custodian. Deutsche Bank AG is also the trustee of the account and once a month remits the collected funds to us. For the nine months ended June 30, 2007, the amount due from custodian decreased by $457,261.

Our Adviser, services the loans pledged under the DB Facility. As a condition to this servicing arrangement, we executed a performance guaranty pursuant to which we guaranteed that our Adviser would comply fully with all of its obligations under the facility. The performance guaranty requires us to maintain a minimum net worth of $100 million and to maintain "asset coverage" with respect to "senior securities representing indebtedness" of at least 200%, in accordance with Section 18 of the 1940 Act. As of June 30, 2007, we were in compliance with our covenants under the performance guaranty.

The DB facility is available for general corporate purposes.

Contractual Obligations

As of June 30, 2007, we were a party to signed and non-binding term sheets for two loan originations for an aggregate of $15.0 million. To date, these investments have not yet funded and we expect to fund these potential investments as follows:

		Payment Due by Period			
Contractual Obligations	**Total**	**Less than 1 Year**	**1-3 Years**	**3-5 Years**	**More than 5 Years**
Investments	15,000,000	15,000,000			
Total	$ 15,000,000	$ 15,000,000	$	$	$

INTERIM CONSOLIDATED FINANCIAL STATEMENTS
GLADSTONE CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES
(Unaudited)

	June 30, 2007	September 30, 2006
ASSETS		
Investments at fair value (Cost 6/30/2007: $369,975,398; 9/30/2006: $216,202,986)	$ 368,949,247	$ 217,642,750
Cash and cash equivalents	3,491,495	731,744
Interest receivable investments in debt securities	2,221,606	1,394,942
Interest receivable employees	32,739	37,396
Due from custodian	3,129,891	3,587,152
Deferred financing fees	246,333	145,691
Prepaid assets	186,643	226,747
Due from employees		1,803,283
Other assets	352,796	213,510
TOTAL ASSETS	$ 378,610,750	$ 225,783,215
LIABILITIES		
Accounts payable	$ 5,160	$ 4,072
Interest payable	516,780	247,530
Administration fee due to Administrator	186,895	
Fees due to Adviser (Refer to Notes 4 and 5)	404,240	240,363
Borrowings under line of credit	161,188,000	49,993,000
Withholding taxes payable		1,803,283
Accrued expenses and deferred liabilities	854,322	721,287
Funds held in escrow	202,433	203,193
TOTAL LIABILITIES	163,357,830	53,212,728
NET ASSETS	$ 215,252,920	$ 172,570,487
ANALYSIS OF NET ASSETS		
Common stock, $0.001 par value, 50,000,000 shares authorized and 14,249,683 and 12,305,008 shares issued and outstanding, respectively	$ 14,250	$ 12,305
Capital in excess of par value	225,449,718	181,270,565
Notes receivable employees	(9,947,366)	(10,248,308)
Net unrealized appreciation on investments	(1,026,151)	1,439,764
Unrealized depreciation on derivative	(279,593)	(253,716)
Realized loss on sale of investments	(780,197)	(861,695)
Realized gain on settlement of derivative	46,212	15,014
Accumulated undistributed net investment income	1,776,047	1,196,558
TOTAL NET ASSETS	$ 215,252,920	$ 172,570,487
NET ASSETS PER SHARE	$ 15.11	$ 14.02

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

GLADSTONE CAPITAL CORPORATION

CONSOLIDATED SCHEDULE OF INVESTMENTS

AS OF JUNE 30, 2007

(UNAUDITED)

Company (1)	Industry	Investment (2)	Cost	Fair Value
Access Television Network, Inc. AccessTV PIN Acquisition LLC Product Information Network Venture	Service-cable airtime (infomercials)	Line of Credit (7)(8) (12.3% Due 3/2009)	$	$
		Senior Term Debt (7) (12.3% Due 3/2009)	2,979,835	2,948,401
ActivStyle Acquisition Co. ActivStyle, Inc.	Service-medical products distribution	Line of Credit (5)(9) (9.6%, Due 7/2009)	450,000	448,313
		Senior Term Debt (5) (9.6%, Due 7/2011)	2,960,000	2,956,300
		Senior Term Debt (3)(5) (11.8%, Due 7/2011)	2,500,000	2,496,875
Advanced Homecare Management, Inc.	Service-home health nursing services	Senior Subordinated Term Debt (5)(6) (11.9%, Due 12/2013)	6,300,000	6,300,000
Allison Publications, LLC D. Magazine Partners, L.P. Allison Media, Inc. City Newspapers, LP City Newspapers, Management, LLC	Service-publisher of consumer oriented magazines	Senior Term Debt (7) (10.3%, Due 12/2011)	8,014,728	7,933,000
Anitox Acquisition Company Anitox Holding, Inc.	Manufacturing-preservatives for animal feed	Senior Real Estate Term Debt (8.8%, Due 1/2012)	3,412,939	3,360,000
		Line of Credit (10) (9.6%, Due 1/2010)		
		Senior Term Debt (5) (9.6%, Due 1/2012)	2,750,000	2,746,563
		Senior Term Debt (3)(5) (11.8%, Due 1/2012)	2,750,000	2,746,563
Badanco Acquisition Corp.	Service-luggage design and distribution	Senior Subordinated Term Debt (5) (12.1%, Due 7/2012)	9,701,250	9,701,250
Bresnan Communications, LLC	Service-telecommunications	Senior Term Debt (6) (7.3%, Due 9/2013)	3,001,880	2,992,500
		Senior Subordinated Term Debt (6) (9.9%, Due 3/2014)	1,510,393	1,505,625
CCS, LLC	Service-cable tv franchise owner	Senior Term Debt (7) (12.3%, Due 7/2007)	3,455,580	3,424,146
CHG Companies, Inc. CHG Medical Staffing, Inc.	Service-healthcare staffing	Letter of Credit (5)(6) (7.9%, Due 12/2012)	400,000	404,000
		Senior Term Debt (5)(6) (7.8%, Due 12/2012)	1,596,000	1,605,975
		Senior Subordinated Term Debt (5)(6) (11.3%, Due 12/2012)	500,000	503,125
Chinese Yellow Pages Company	Service-publisher of Chinese language directories	Line of Credit (7)(11) (12.3%, Due 9/2010)	150,071	150,071
		Senior Term Debt (7) (12.3%, Due 9/2010)	1,235,008	1,222,435

Clinton Holdings, LLC Clinton Aluminum Acquisition, LLC Metal Transportation, LLC Clinton Distribution Center, LLC	Distribution-aluminum sheets and stainless steel	Senior Subordinated Term Debt (5) (12.6%, Due 1/2013)	$ 15,500,000	$ 15,519,375
		Common Stock Warrants	109,124	125,864
CMI Acquisition, LLC (d/b/a Triangle Metal Industries) TMC Acquisition, LLC	Service-recycling	Senior Subordinated Term Debt (7) (12.3%, Due 11/2012)	6,500,000	6,500,000
Community Media Corporation	Service-publisher of free weekly newspapers	Senior Term Debt (7) (10.8%, Due 7/2007)	2,572,497	2,547,350
Country Road Communications LLC Country Road Management, Inc.	Service-telecommunications	Senior Subordinated Term Debt (5)(6) (13.2%, Due 7/2013)	5,965,833	6,030,000
Defiance Acquisition Corporation	Manufacturing-trucking parts	Senior Term Debt (3)(5) (13.3%, Due 4/2010)	6,325,000	6,317,094
Doe & Ingalls Management LLC	Distributor-specialty chemicals	Senior Term Debt (5) (8.8%, Due 11/2010)	4,100,000	4,110,250
Doe & Ingalls of North Carolina Operating LLC Doe & Ingalls of Florida Operating LLC Doe & Ingalls of Virginia Operating LLC Doe & Ingalls of Maryland Operating LLC		Senior Term Debt (3)(5) (9.8%, Due 11/2010)	4,466,250	4,471,833
Emdeon Business Services, Inc.	Service-healthcare technology solutions	Senior Term Debt (6) (7.6%, Due 11/2013)	2,440,341	2,450,020
		Senior Subordinated Term Debt (6) (10.4%, Due 5/2014)	2,013,460	2,020,000
Express Courier International, Inc.	Service-ground delivery and logistics	Line of Credit (12) (9.6%, Due 6/2009)		
		Senior Term Debt (5) (9.6%, Due 6/2011)	4,347,500	4,347,500
		Senior Term Debt (3)(5) (11.8%, Due 6/2011)	3,950,000	3,950,000
Finn Corporation	Manufacturing-landscape equipment	Common Stock Warrants	37,000	2,972,858
Florida Cable, Inc. Lakepointe Limited Partnership	Service-cable and internet system operator	Senior Term Debt (7) (11.8%, Due 7/2010)	5,906,391	5,849,810
FR X Ohmstede Holdings, LLC	Service & Manufacturing-heat exchangers	Senior Term Debt (6) (7.9%, Due 8/2013)	2,739,130	2,756,250
FR X Ohmstede Acquisitions Co.		Senior Subordinated Term Debt (6) (12.4%, Due 8/2014)	3,011,190	3,015,000

Global Materials Technologies, Inc.	Manufacturing-steel wool products and metal fibers	Senior Term Debt (3)(5) (14.3%, Due 11/2009)	$ 5,150,000	$ 4,944,000
GTM Holdings, Inc. Gold Toe Investment Corp.	Manufacturing-socks	Senior Term Debt (6) (8.1%, Due 10/2013)	497,500	499,988
		Senior Subordinated Term Debt (6) (11.4%, Due 4/2014)	500,000	505,000
Greatwide Logistics Services, Inc.	Service-logistics and transportation	Senior Term Debt (6) (8.6%, Due 12/2013)	3,980,000	3,880,500
		Senior Subordinated Term Debt (6) (11.9%, Due 6/2014)	4,000,000	3,840,000
Harrington Holdings, Inc. Harrington Acquisition Corp.	Service-healthcare products distribution	Senior Term Debt (6) (7.8%, Due 1/2014)	2,493,750	2,506,219
		Senior Subordinated Term Debt (6) (11.4%, Due 1/2014)	5,000,000	5,025,000
Heartland Communications Group, LLC Heartland Comm. License, LLC Heartland Comm. Houghton License, LLC Tu-Mar Broadcasting, Inc.	Service-radio station operator	Line of Credit (7)(13) (11.8%, Due 5/2008)	9,856	9,856
		Senior Term Debt (7) (11.8%, Due 5/2011)	4,873,531	4,823,237
International Junior Golf	Service-golf training	Line of Credit (5)(14) (9.6%, Due 5/2010)	500,000	499,375
		Senior Term Debt (5) (9.6%, Due 5/2012)	2,650,000	2,646,688
		Senior Term Debt (3)(5) (11.8%, Due 5/2012)	2,500,000	2,493,750
It's Just Lunch International, LLC	Service-dating service	Line of Credit (5)(15) (9.3%, Due 6/2009)	550,000	514,250
		Senior Term Debt (5) (9.6%, Due 6/2011)	3,300,000	3,085,500
		Senior Term Debt (3)(5)(15) (11.8%, Due 6/2011)	500,000	467,500
John Henry Holdings, Inc. Multi Packaging Solutions, Inc.	Manufacturing-packaging products	Senior Subordinated Term Debt (6) (12.3%, Due 6/2011)	8,000,000	8,000,000
Kinetek Acquisition Corp.	Manufacturing-custom engineered motors & controls	Senior Term Debt (6) (7.8%, Due 11/2013)	1,498,218	1,492,500
		Senior Subordinated Term Debt (6) (10.8%, Due 5/2014)	1,509,209	1,507,500
KMBQ Corporation	Service-AM/FM radio broadcaster	Line of Credit (7)(16) (13.3%, Due 3/2010)	150,000	150,000
		Senior Term Debt (7) (13.3%, Due 3/2010)	1,825,404	1,806,543

LocalTel, Inc.	Service-yellow pages publishing	Line of Credit (5)(17) (9.8%, Due 6/2009)	$ 1,275,000	$ 1,096,500
		Senior Term Debt (5) (9.8%, Due 6/2011)	2,687,500	2,311,250
		Senior Term Debt (3)(5) (12.3%, Due 6/2011)	2,750,000	2,282,500
Macfadden Performing Arts Media, LLC	Service-magazine publisher	Line of Credit (7) (11.3%, Due 6/2009)	515,979	515,979
		Senior Term Debt (7) (11.3%, Due 6/2009)	6,775,441	6,700,000
MCA Communications, LLC MCA Internet, LLC	Service-internet-based data publisher	Line of Credit (7) (non-accrual, Due 9/2006)	798,349	792,063
Meteor Holding Corporation	Manufacturing-bar code scanning and data	Senior Term Debt (6) (8.3%, Due 12/2013)	2,354,100	2,364,281
Metrologic Instruments, Inc.	capture	Senior Subordinated Term Debt (6) (11.6%, Due 12/2013)	1,500,000	1,509,375
Multi-Ag Media LLC HFW Communications, Inc. Dairy Radio, LLC DPW Publishing, Inc. Phoenix Data Processing, LLC	Service-dairy magazine publisher/information database	Senior Term Debt (7) (12.3%, Due 12/2009)	2,643,911	2,618,764
Newhall Holdings, Inc. (d/b/a Newhall Laboratories) Golden Sun, Inc.	Service-distributor of personal care products and supplements	Line of Credit (7)(20) (8.8%, Due 5/2010)		
		Senior Term Debt (3)(7) (9.1%, Due 5/2012)	4,500,000	4,500,000
		Senior Term Debt (3)(7) (11.3%, Due 5/2012)	4,500,000	4,500,000
Northern Contours Northern Contours of Kentucky, Inc. Norcon Holding LLC Norcon Lewis LLC	Manufacturing-veneer and laminate components	Senior Subordinated Term Debt (5) (12.3%, Due 5/2010)	7,000,000	7,008,750
Pinnacle Treatment Centers, Inc.	Service-Addiction treatment centers	Line of Credit (21) (9.6%, Due 12/2009)		
		Senior Term Debt (5) (9.6%, Due 12/2011)	2,500,000	2,496,875
		Senior Term Debt (3)(5) (12.3%, Due 12/2011)	4,500,000	4,494,375
Precision Acquisition Group Holdings, Inc. Precision Asset Acquisition Company, LLC	Manufacturing-consumable components for the aluminum industry	Equipment Note (5)(22) (9.8%, Due 10/2011)	591,228	591,228
		Senior Term Debt (5) (9.8%, Due 10/2010)	5,000,000	5,012,500
		Senior Term Debt (3)(5) (11.8%, Due 10/2010)	4,200,000	4,210,500

PROFITSystems Acquisition Co.	Service-design and develop ERP software	Line of Credit (23) (9.6%, Due 7/2009)	$	$
PROFITSystems, Inc.		Senior Term Debt (5) (9.6%, Due 7/2011)	2,875,000	2,878,594
		Senior Term Debt (3)(5) (11.8%, Due 7/201)	2,900,000	2,903,625
Puerto Rico Cable Acquisition Company, Inc.	Service-telecommunications	Senior Subordinated Term Debt (5)(6) (11.6%, Due 1/2012)	7,802,222	7,755,841
Reading Broadcasting, Inc.	Service-television station operator	Senior Term Debt (7) (12.8%, Due 12/2011)	7,087,084	7,017,930
RCS Management Holding Co.	Service-healthcare supplies	Senior Term Debt (3)(5) (9.8%, Due 1/2011)	3,000,000	2,910,000
		Senior Term Debt (4)(5) (12.3%, Due 1/2011)	3,000,000	2,895,000
RedPrairie Holding, Inc. RedPrairie Corporation	Service-design and develop supply chain	Senior Term Debt (6) (8.4%, Due 7/2012)	4,457,500	4,457,500
Blue Cube Software, Inc.	software	Senior Subordinated Term Debt (6) (11.9%, Due 1/2013)	3,000,000	3,000,000
RiskMetrics Group Holdings, LLC	Service-develop risk and wealth management	Senior Term Debt (6) (7.6%, Due 1/2014)	1,995,000	1,999,988
	solutions	Senior Subordinated Term Debt (6) (10.9%, Due 7/2014)	500,000	505,000
SCI Cable, Inc.	Service-cable, internet, voice provider	Senior Term Debt (7) (14.3%, Due 10/2008)	2,485,032	2,459,885
SCS Acquisition Corp. (d/b/a Specialty Coatings	Service-chemically treated equipment	Senior Term Debt (5)(17) (9.3%, Due 12/2011)	5,442,311	5,442,311
Systems)	distribution	Senior Term Debt (3)(5)(17) (11.3%, Due 12/2011)	6,531,250	6,531,250
Sunburst Media-Louisiana, LLC	Service-radio station operator	Senior Term Debt (7) (12.0%, Due 6/2011)	7,875,441	7,800,000
Sunshine Media Holdings	Service-publisher regional B2B trade	Credit Facility (5)(24) (9.3%, Due 5/2010)	600,000	598,500
	magazines	Senior Term Debt (5) (9.3%, Due 5/2012)	17,000,000	16,978,750
		Senior Term Debt (3)(5) (11.8%, Due 5/2012)	10,000,000	9,975,000
Thibaut Acquisition Co.	Service-design and disbribute wall covering	Credit Facility (5)(25) (9.8%, Due 1/2011)	500,000	499,375
		Senior Term Debt (5) (9.8%, Due 1/2011)	2,887,500	2,887,500
		Senior Term Debt (3)(5) (12.3%, Due 1/2011)	3,000,000	3,000,000
U.S. HealthCare Communications, LLC	Service-magazine publisher/operator	Senior Term Debt (7) (11.3%, Due 4/2011)	2,244,182	2,219,035

Viapack, Inc. P&O Packaging Acquisition LLC	Manufacturing-polyethylene film	Senior Real Estate Term Debt (9.8%, Due 3/2011)	$ 975,000	$ 975,000
		Senior Term Debt (3)(5)(19) (11.3%, Due 3/2011)	4,223,438	4,202,320
Visual Edge Technology, Inc. Graphic Enterprises, Inc. Copeco, Inc.	Service-office equipment distribution	Senior Subordinated Term Debt (5) (13.3%, Due 8/2011)	5,000,000	3,625,000
Wesco Holdings, Inc. Wesco Aircraft Hardware Corp.	Service-aerospace parts and distribution	Senior Term Debt (6) (7.6%, Due 9/2013)	2,478,317	2,466,436
		Senior Subordinated Term Debt (6) (11.1%, Due 3/2014)	2,271,494	2,289,375
West Coast Yellow Pages, Inc.	Service-directory publisher	Senior Term Debt (7) (13.8%, Due 8/2010)	1,624,251	1,605,390
Westlake Hardware, Inc. WHI Holding Corp.	Retail-hardware and variety	Senior Subordinated Term Debt (5) (12.6%, Due 1/2011)	15,000,000	14,925,000
Winchester Electronics	Manufacturing-high bandwidth connectors and cables	Senior Term Debt (5) (9.1%, Due 6/2012)	2,000,000	2,002,500
		Senior Subordinated Term Debt (5) (12.3%, Due 6/2012)	10,000,000	10,012,500
WP Evenflo Group Holdings Inc. WP Evenflo Acquisition, Inc.	Manufacturing-infant and juvenile products	Senior Term Debt (6) (7.8%, Due 2/2013)	1,990,000	1,999,950
		Senior Subordinated Term Debt (6) (11.3%, Due 2/2014)	2,000,000	2,000,000
Total:			**$ 369,975,398**	**$ 368,949,247**

(1) We do not "Control," and are not an "Affiliate" of, any of our portfolio companies, each as defined in the Investment Company Act of 1940, as amended (the "1940 Act"). In general, under the 1940 Act, we would "Control" a portfolio company if we owned 25% or more of its voting securities and would be an "Affiliate" of a portfolio company if we owned 5% or more of its voting securities.

(2) Percentage represents interest rates in effect at June 30, 2007 and due date represents the contractual maturity date.

(3) Last Out Tranche of senior debt, meaning if the company is liquidated then the holder of the Last Out Tranche is paid after the senior debt.

(4) Last Out Tranche of senior debt, meaning if the company is liquidated then the holder of the Last Out Tranche is paid after the senior debt, however the debt is junior to another Last Out Tranche.

(5) Fair value was based on opinions of value submitted by Standard & Poor's Securities Evaluations, Inc.

(6) Marketable securities, such as syndicated loans, are valued based on the indicative bid price, as of June 29, 2007, from the respective originating syndication agent's trading desk.

(7) Investment valued at cost due to recent acquisition.

(8) Availability under the Access TV credit facility totals $500,000. There were no borrowings outstanding as of June 30, 2007.

(9) Availability under the ActivStyle credit facility totals $1,500,000. Borrowings of $450,000 were outstanding at June 30, 2007.

(10) Availability under the Anitox credit facility totals $3,000,000. There were no borrowings outstanding at June 30, 2007.

(11) Availability under the Chinese Yellow Pages credit facility totals $950,000. Borrowings of $150,071 were outstanding at June 30, 2007.

(12) Availability under the Express Courier credit facility totals $1,500,000. There were no borrowings outstanding at June 30, 2007.

(13) Availability under the Heartland credit facility totals $500,000. Borrowings of $9,856 were outstanding at June 30, 2007.

(14) Availability under the International Junior Golf credit facility totals $1,000,000. Borrowings of $500,000 were outstanding at June 30, 2007.

(15) Remaining availability under the It's Just Lunch revolving credit facility totals $200,000, borrowings of $550,000 were outstanding at June 30, 2007. The company may borrow an additional $1,750,000 of the senior term debt facility, subject to certain conditions including Gladstone Capital's approval, borrowings of $500,000 were outstanding at June 30, 2007.

(16) Availability under the KMBQ credit facility totals $200,000. Borrowings of $150,000 were outstanding at June 30, 2007.

(17) Availability under the LocalTel credit facility totals $3,000,000. Borrowings of $1,275,000 were outstanding at June 30, 2007.

(18) Availability under the MacFadden credit facility totals $1,400,000. Borrowings of $515,979 were outstanding at June 30, 2007.

(19) The MCA credit facility was matured as of June 30, 2007. The investment is currently not income producing.

(20) Availability under the Newhall credit facility totals $4,000,000. There were no borrowings outstanding as of June 30, 2007.

(21) Availability under the Pinnacle credit facility totals $500,000. There were no borrowings outstanding at June 30, 2007.

(22) Precision may borrow up to $1,000,000 for purposes of acquiring equipment. Borrowings of $591,228 were outstanding at June 30, 2007.

(23) Availability under the ProfitSystems credit facility totals $1,250,000. There were no borrowings outstanding at June 30, 2007.

(24) Availability under the Sunshine credit facility totals $3,000,000. Borrowings of $600,000 were outstanding at June 30, 2007.

(25) Availability under the Thibaut credit facility totals $500,000. Borrowings of $500,000 were outstanding at June 30, 2007.

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

GLADSTONE CAPITAL CORPORATION

CONSOLIDATED SCHEDULE OF INVESTMENTS

AS OF SEPTEMBER 30, 2006

Company (1)	Industry	Investment (2)	Cost	Fair Value
ActivStyle Acquisition Co. ActivStyle, Inc.	Service-medical products distribution	Line of Credit (16) (9.6%, Due 7/2009)	$	$
		Senior Term Debt (5) (9.6%, Due 7/2011)	3,200,000	3,200,000
		Senior Term Debt (3)(5) (11.8%, Due 7/2011)	2,500,000	2,500,000
Advanced Homecare Management, Inc.	Service-home health nursing services	Senior Subordinated Term Debt (5)(6) (11.33%, Due 12/2013)	5,000,000	5,000,000
Allied Extruders, LLC P&O Packaging Acquisition LLC	Manufacturing-polyethylene film	Senior Real Estate Term Debt (9.8%, Due 3/2011)	1,000,000	1,000,000
		Senior Term Debt (3)(5) (11.3%, Due 3/2011)	8,000,000	8,030,000
Badanco Acquisition Corp.	Manufacturing-luggage	Senior Term Debt (5) (10.8%, Due 2/2010)	5,145,019	5,157,881
		Senior Term Debt (3)(5) (13.8%, Due 2/2010)	8,585,125	8,628,051
Benetech, Inc.	Service & Manufacturing-dust management systems for the coal and electric utility industries	Senior Term Debt (5) (10.3%, Due 5/2009)	2,112,500	2,144,187
		Senior Term Debt (3)(5) (13.3%, Due 5/2009)	3,046,875	3,107,813
Bresnan Communications, LLC	Service-telecommunications	Senior Term Debt (6) (7.2%, Due 9/2013)	1,002,115	997,500
		Senior Subordinated Term Debt (9.9%, Due 3/2014)	1,511,554	1,533,750
Consolidated Bedding, Inc.	Manufacturing-mattresses	Senior Subordinated Term Debt (5) (14.4%, Due 3/2009)	2,438,359	2,306,991
Country Road Communications LLC Country Road Management, Inc.	Service-telecommunications	Senior Subordinated Term Debt (5)(6) (13.3%, Due 7/2013)	5,961,594	6,015,000
Defiance Stamping Company	Manufacturing-trucking parts	Senior Term Debt (3)(5) (13.3%, Due 4/2010)	6,325,000	6,332,906
Doe & Ingalls Management LLC Doe & Ingalls of North Carolina Operating LLC Doe & Ingalls of Florida Operating LLC Doe & Ingalls of Virginia Operating LLC	Distributor-specialty chemicals	Senior Term Debt (5) (9.8%, Due 11/2010)	4,700,000	4,723,500
		Senior Term Debt (3)(5) (13.3%, Due 11/2010)	4,500,000	4,516,875
Express Courier International, Inc.	Service-ground delivery and logistics	Line of Credit (7) (9.6%, Due 6/2009)		
		Senior Term Debt (5) (9.6%, Due 6/2011)	4,700,000	4,700,000
		Senior Term Debt (3)(5) (11.8%, Due 6/2011)	3,950,000	3,950,000

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Finn Corporation	Manufacturing-landscape equipment	Common Stock Warrants	37,000	709,431
FR X Ohmstede Holdings, LLC FR X Ohmstede Acquisitions Co.	Service & Manufacuring-heat exchangers	Senior Term Debt (6) (8.5%, Due 8/2013)	3,000,000	3,026,250
		Senior Subordinated Term Debt (6) (12.5%, Due 8/2014)	3,012,369	3,030,000
Global Materials Technologies, Inc.	Manufacturing-steel wool products and metal fibers	Senior Term Debt (3)(5) (14.3%, Due 11/2009)	5,300,000	5,233,750
It's Just Lunch International, LLC	Service-dating service	Line of Credit (12)(5) (9.2%, Due 6/2009)	200,000	199,500
		Senior Term Debt (13)(5) (9.6%, Due 6/2011)	3,300,000	3,291,750
		Senior Term Debt (3)(14) (11.8%, Due 6/2011)		
John Henry Holdings, Inc. Multi Packaging Solutions, Inc.	Manufacturing-packaging products	Senior Subordinated Term Debt (6) (12.5%, Due 6/2011)	8,000,000	8,000,000
LocalTel, Inc.	Service-yellow pages publishing	Line of Credit (5)(15) (9.8%, Due 6/2009)	350,000	343,000
		Senior Term Debt (5) (9.8%, Due 6/2011)	2,687,500	2,633,750
		Senior Term Debt (3)(5) (12.3%, Due 6/2011)	2,750,000	2,695,000
Mistras Holdings Corp.	Service & Manufacturing nondestructive testing instruments, systems and services	Senior Term Debt (3)(5) (11.5%, Due 8/2008)	9,499,999	9,737,499
		Senior Term Debt (4)(5)(18) (12.5%, Due 8/2008)	5,250,001	5,620,124
Network Solutions LLC	Service-internet domain registry and host	Senior Term Debt (6) (10.4%, Due 1/2012)	4,464,358	4,499,747
Northern Contours Northern Contours of Kentucky, Inc. Norcon Holding LLC Norcon Lewis LLC	Manufacturing-veneer and laminate components	Senior Subordinated Term Debt (5) (12.3%, Due 5/2010)	7,000,000	7,017,500
PROFITSystems Acquisition Co. PROFITSystems, Inc.	Service-design and develop ERP software	Line of Credit (17) (9.6%, Due 7/2009)		
		Senior Term Debt (5) (9.6%, Due 7/2011)	3,100,000	3,100,000
		Senior Term Debt (5) (11.8%, Due 7/201) (3)	2,900,000	2,900,000
Puerto Rico Cable Acquisition Company, Inc.	Service-telecommunications	Senior Subordinated Term Debt (5)(6) (11.6%, Due 1/2012)	7,813,274	7,775,183
QCE, LLC (d/b/a Quiznos Corp.)	Service-restaurant franchisor	Senior Term Debt (6) (7.6%, Due 5/2013)	3,010,713	2,977,538
		Senior Term Debt (3)(6) (11.1%, Due 11/2013)	3,045,560	3,033,750

RCS Management Holding Co.	Service-healthcare supplies	Senior Term Debt (3)(5) (9.8%, Due 1/2011)	3,000,000	3,003,750
		Senior Term Debt (4)(5) (12.3%, Due 1/2011)	3,000,000	3,003,750
RedPrairie Holding, Inc. RedPrairie Corporation Blue Cube Software, Inc.	Service-design and develop supply chain software	Senior Term Debt (6) (8.4%, Due 7/2012)	3,990,000	3,990,000
		Senior Subordinated Term Debt (6) (11.9%, Due 1/2013)	2,000,000	2,005,000
SCPH Holdings, Inc. Sea Con Phoenix, Inc. Phoenix Optix, Inc.	Manufacturing-underwater and harsh environment components	Credit Facility (8) (9.8%, Due 2/2007)		
		Senior Term Debt (5) (10.3%, Due 2/2010)	2,625,000	2,631,563
		Senior Term Debt (3)(5) (13.3%, Due 2/2010)	2,887,500	2,898,328
SCS Acquisition Corp.	Service-chemically treated equipment distribution	Senior Term Debt (3)(5)(9) (9.3%, Due 12/2011)	6,250,000	6,257,812
		Senior Term Debt (3)(5)(10) (11.3%, Due 12/2011)	6,568,750	6,576,961
Thibaut Acquisition Co.	Design and Disbtribution-wall coverings	Credit Facility (11) (9.8%, Due 1/2011)		
		Senior Term Debt (5) (9.8%, Due 1/2011)	3,325,000	3,325,000
		Senior Term Debt (3)(5) (12.3%, Due 1/2011)	3,000,000	3,000,000
Visual Edge Technology, Inc. Graphic Enterprises, Inc. Copeco, Inc.	Service-office equipment distribution	Senior Subordinated Term Debt (5) (13.3%, Due 8/2011)	5,000,000	4,987,500
Westlake Hardware, Inc. WHI Holding Corp.	Retail-hardware and variety	Senior Subordinated Term Debt (5) (12.6%, Due 1/2011)	15,000,000	14,981,250
Winchester Electronics	Manufacturing-high bandwidth connectors and cables	Senior Term Debt (3)(5) (12.3%, Due 6/2012)	6,000,000	6,007,500
Xspedius Communications LLC	Service-telecommunications	Senior Subordinated Term Debt (5) (15.8%, Due 3/2010)	5,157,821	5,306,110
Total:			**$ 216,202,986**	**$ 217,642,750**

(1) We do not "Control," and are not an "Affiliate" of, any of our portfolio companies, each as defined in the Investment Company Act of 1940, as amended (the "1940 Act"). In general, under the 1940 Act, we would "Control" a portfolio company if we owned 25% or more of its voting securities and would be an "Affiliate" of a portfolio company if we owned 5% or more of its voting securities.

(2) Percentage represents interest rates in effect at September 30, 2006 and due date represents the contractual maturity date.

(3) Last Out Tranche of senior debt, meaning if the company is liquidated then the holder of the Last Out Tranche is paid after the senior debt.

(4) Last Out Tranche of senior debt, meaning if the company is liquidated then the holder of the Last Out Tranche is paid after the senior debt, however the debt is junior to another Last Out Tranche.

(5) Fair value was based on opinions of value submitted by Standard & Poor's Securities Evaluations, Inc.

(6) Marketable securities, such as syndicated loans, are valued based on the indicative bid price, as of September 30, 2006 from the respective originating syndication agent's trading desk.

(7) Availability under the credit facility totals $1,500,000. There were no borrowings outstanding at September 30, 2006.

(8) Availability under the credit facility totals $500,000. There were no borrowings outstanding at September 30, 2006.

(9) Availability under the debt facility totals $7,500,000. The outstanding balance of the debt facility was $6,250,000 at September 30, 2006.

(10) Availability under the debt facility totals $7,500,000. The outstanding balance of the debt facility was $6,568,750 at September 30, 2006.

(11) Availability under the credit facility totals $1,000,000. There were no borrowings outstanding at September 30, 2006.

(12) Availability under the credit facility totals $750,000. Borrowings of $200,000 were outstanding at September 30, 2006.

(13) The company may borrow an additional $500,000 under the senior term debt facility, subject to certain conditions including Gladstone Capital's approval.

(14) The company may borrow an additional $2,250,000 under the senior term debt facility, subject to certain conditions including Gladstone Capital's approval.

(15) Availability under the credit facility totals $3,000,000. Borrowings of $350,000 were outstanding at September 30, 2006.

(16) Availability under the credit facility totals $1,500,000. There were no borrowings outstanding at September 30, 2006

(17) Availability under the credit facility totals $1,250,000. There were no borrowings outstanding at September 30, 2006

(18) Includes a success fee with a fair value of $742,000 and no cost basis.

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

GLADSTONE CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended June 30,	
	2007	**2006**
INVESTMENT INCOME		
Interest income investments	$ 8,911,643	$ 5,775,522
Interest income cash and cash equivalents	109,269	8,178
Interest income notes receivable from employees	132,795	108,877
Prepayment fees and other income	47,572	630,239
Total investment income	9,201,279	6,522,816
EXPENSES		
Interest expense	1,762,249	702,449
Loan servicing (Refer to Notes 4 and 5)	897,634	693,965
Base management fee (Refer to Note 4)	727,259	334,814
Incentive fee (Refer to Note 4)	1,166,529	
Administration fee (Refer to Note 4)	186,895	
Professional fees	148,609	166,405
Amortization of deferred financing fees	72,133	36,036
Stockholder related costs	39,434	28,371
Directors fees	56,250	27,500
Insurance expense	66,246	50,589
Stock option compensation		202,296
Other expenses	82,062	35,083
Expenses before credit from Adviser	5,205,300	2,277,508
Credit to base management and incentive fees from Adviser (Refer to Note 4)	(1,708,888)	(542,774)
Total expenses net of credits to base management and incentive fees	3,496,412	1,734,734
NET INVESTMENT INCOME	5,704,867	4,788,082
REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS:		
Realized loss on sale of investments	(5,021)	(100,850)
Realized gain on settlement of derivative	8,405	1,367
Unrealized (depreciation) appreciation on derivative	(264)	41,486
Net unrealized appreciation on investments	256,613	812,991
Net gain on investments	259,733	754,994
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS	$ 5,964,600	$ 5,543,076
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS PER COMMON SHARE:		
Basic	$ 0.44	$ 0.49
Diluted	$ 0.44	$ 0.48
WEIGHTED AVERAGE SHARES OF COMMON STOCK OUTSTANDING:		
Basic	13,561,511	11,337,291

	Three Months Ended June 30,	
Diluted	13,561,511	11,570,425

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

GLADSTONE CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Nine Months Ended June 30,	
	2007	**2006**
INVESTMENT INCOME		
Interest income investments	$ 25,064,702	$ 18,497,893
Interest income cash and cash equivalents	178,183	21,714
Interest income notes receivable from employees	403,917	323,003
Prepayment fees and other income	431,973	711,225
Total investment income	26,078,775	19,553,835
EXPENSES		
Interest expense	4,693,525	2,302,693
Loan servicing (Refer to Notes 4 and 5)	2,377,409	2,144,024
Base management fee (Refer to Note 4)	1,806,075	955,894
Incentive fee (Refer to Note 4)	3,474,007	
Administration fee (Refer to Note 4)	481,746	
Professional fees	368,610	399,758
Amortization of deferred financing fees	198,633	94,572
Stockholder related costs	190,450	273,170
Directors fees	167,470	81,712
Insurance expense	191,338	151,956
Stock option compensation		279,618
Other expenses	219,522	151,663
Expenses before credit from Adviser	14,168,785	6,835,060
Credit to base management and incentive fees from Adviser (Refer to Note 4)	(4,682,160)	(1,765,774)
Total expenses net of credits to base management and incentive fees	9,486,625	5,069,286
NET INVESTMENT INCOME BEFORE INCOME TAXES	16,592,150	14,484,549
Income tax expense		50,237
NET INVESTMENT INCOME	16,592,150	14,434,312
REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS:		
Net realized gain (loss) on sale of investments	81,498	(903,945)
Realized gain on settlement of derivative	31,198	1,367
Unrealized (depreciation) appreciation on derivative	(25,877)	65,252
Net unrealized (depreciation) appreciation on investments	(2,465,915)	5,769,820
Net (loss) gain on investments	(2,379,096)	4,932,494
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS	$ 14,213,054	$ 19,366,806
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS PER		

	Nine Months Ended June 30,	
COMMON SHARE:		
Basic	$ 1.12	$ 1.71
Diluted	$ 1.12	$ 1.68
WEIGHTED AVERAGE SHARES OF COMMON STOCK OUTSTANDING:		
Basic	12,701,845	11,317,437
Diluted	12,701,845	11,549,054

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

GLADSTONE CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
(UNAUDITED)

	Nine Months Ended June 30,	
	2007	**2006**
Operations:		
Net investment income	$ 16,592,150	$ 14,434,312
Net realized gain (loss) on sale of investments	81,498	(903,945)
Realized gain on settlement of derivative	31,198	1,367
Unrealized (depreciation) appreciation on derivatives	(25,877)	65,252
Net unrealized (depreciation) appreciation on investments	(2,465,915)	5,769,820
Net increase in net assets from operations	14,213,054	19,366,806
Capital transactions:		
Issuance of common stock under shelf offering	46,075,000	
Distributions to stockholders	(16,012,661)	(13,751,539)
Shelf offering costs	(405,708)	
Repayment of principal on employee notes	300,941	129,943
Stock option compensation		279,618
Issuance of common stock under stock option plan		1,150,245
Stock surrendered in settlement of withholding tax	(1,488,193)	
Increase (decrease) in net assets from capital share transactions	28,469,379	(12,191,733)
Total increase in net assets	42,682,433	7,175,073
Net assets at beginning of year	172,570,487	151,610,683
Net assets at end of period	$ 215,252,920	$ 158,785,756

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

GLADSTONE CAPITAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Nine Months Ended June 30,	
	2007	**2006**
CASH FLOWS FROM OPERATING ACTIVITIES		
Net increase in net assets resulting from operations	$ 14,213,054	$ 19,366,806
Adjustments to reconcile net increase in net assets resulting from operations to net cash (used in) provided by operating activities:		
Purchase of investments	(253,727,829)	(105,076,400)
Principal repayments on investments	99,802,867	107,876,077
Net amortization of premiums and discounts	29,872	(144,501)
Amortization of deferred financing fees	198,633	94,572
Stock compensation expense		279,618
Realized loss on investments	122,680	1,329,458
Unrealized depreciation (appreciation) on derivative	25,877	(65,252)
Change in net unrealized depreciation (appreciation) on investments	2,465,915	(5,769,820)
(Increase) decrease in interest receivable	(822,007)	276,230
Decrease in funds due from custodian	457,261	130,150
Decrease in prepaid assets	40,102	105,902
Increase in due from affiliate		(207,960)
Increase in other assets	(165,163)	(27,845)
Increase in accounts payable	1,088	23,449
Increase in interest payable	269,250	4,685
Increase (decrease) in accrued expenses and deferred liabilities	133,035	(125,298)
Increase (decrease) in fees due to affiliate	163,877	(209,924)
Increase in administration fee due to Gladstone Administration	186,895	
(Decrease) increase in funds held in escrow	(760)	40
Increase in investment balance due to payment in kind interest		(74,701)
Net cash (used in) provided by operating activities	(136,605,353)	17,785,286
CASH FLOWS FROM INVESTING ACTIVITIES		
Receipt of principal on notes receivable employees	300,941	129,943
Net cash provided by investing activities	300,941	129,943
CASH FLOWS FROM FINANCING ACTIVITIES		
Net proceeds from issuance of common shares	45,669,292	
Borrowings from the lines of credit	277,800,000	113,090,000
Repayments on the lines of credit	(166,605,000)	(118,278,064)
Distributions paid	(16,012,661)	(13,751,539)
Exercise of employee stock options		1,150,245
Deferred financing fees	(299,275)	(173,333)
Withholding tax obligation settlement	(1,488,193)	
Net cash provided by (used in) financing activities	139,064,163	(17,962,691)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS (1)	2,759,751	(47,462)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	731,744	503,776

	Nine Months Ended June 30,	
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 3,491,495	$ 456,314
CASH PAID DURING PERIOD FOR INTEREST	$ 4,424,275	$ 2,298,008
NON-CASH FINANCING ACTIVITIES		
Notes receivable issued in exchange for common stock associated with the exercise of employee stock options	$	$ 199,980

(1) Cash and cash equivalents consist of demand deposits and highly liquid investments with original maturities of three months or less when purchased.

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

GLADSTONE CAPITAL CORPORATION
FINANCIAL HIGHLIGHTS
(UNAUDITED)

	Three Months Ended June 30,	
	2007	**2006**
Per Share Data (1)		
Net asset value at beginning of period	$ 13.82	$ 13.84
Income from investment operations:		
Net investment income (2)	0.42	0.42
Realized gain (loss) on sale of investments (2)		(0.01)
Net unrealized (loss) gain on investments (2)	0.02	0.07
Net unrealized gain on derivatives (2)		0.01
Total from investment operations	0.44	0.49
Less distributions:		
Distributions from net investment income	(0.42)	(0.41)
Total distributions	(0.42)	(0.41)
Issuance of common stock under shelf offering	1.50	
Offering costs and underwriting discount	(0.23)	
Issuance of common stock under stock option plan		0.10
Repayment of principal on notes receivable		0.01
Dilutive effect of share issuance		(0.08)
Net asset value at end of period	$ 15.11	$ 13.95
Per share market value at beginning of period	$ 23.68	$ 21.55
Per share market value at end of period	21.46	21.39
Total return (3)(4)	(7.69)%	1.11%
Shares outstanding at end of period	14,249,683	11,384,363
Ratios/Supplemental Data		
Net assets at end of period	$ 215,252,920	$ 158,785,756
Average net assets (5)	$ 197,994,217	$ 156,053,816
Ratio of expenses to average net assets annualized (6)	10.52%	5.83%
Ratio of net expenses to average net assets annualized (7)	7.06%	4.45%
Ratio of net investment income to average net assets annualized	11.53%	12.27%

(1) Based on actual shares outstanding at the end of the corresponding period.

(2) Based on weighted average basic per share data.

(3) Total return equals the increase or decrease of the ending market value over the beginning market value plus monthly dividends divided by the monthly beginning market value, assuming monthly dividend reinvestment.

(4) Amounts were not annualized.

(5)

Average net assets are computed using the average of the balance of net assets at the end of each month of the reporting period.

(6)
Ratio of expenses to average net assets is computed using expenses before credits from Adviser to the base management and incentive fees and including income tax expense.

(7)
Ratio of net expenses to average net assets is computed using total expenses net of credits from Adviser to the base management and incentive fees and including income tax expense.

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

GLADSTONE CAPITAL CORPORATION
FINANCIAL HIGHLIGHTS
(UNAUDITED)

	Nine Months Ended June 30,	
	2007	**2006**
Per Share Data (1)		
Net asset value at beginning of period	$ 14.02	$ 13.41
Income from investment operations:		
Net investment income (2)	1.31	1.28
Realized loss on sale of investments (2)		(0.08)
Net unrealized (loss) gain on investments (2)	(0.19)	0.51
Total from investment operations	1.12	1.71
Less distributions:		
Distributions from net investment income	(1.26)	(1.22)
Total distributions	(1.26)	(1.22)
Issuance of common stock under shelf offering	1.50	
Offering costs and underwriting discount	(0.23)	
Issuance of common stock under stock option plan		0.10
Repayment of principal on notes receivable	0.02	0.01
Stock surrendered to settle withholding tax obligation	(0.06)	
Dilutive effect of share issuance		(0.06)
Net asset value at end of period	$ 15.11	$ 13.95
Per share market value at beginning of period	$ 22.01	$ 22.55
Per share market value at end of period	21.46	21.39
Total return (3)(4)	2.92%	0.35%
Shares outstanding at end of period	14,249,683	11,384,363
Ratios/Supplemental Data		
Net assets at end of period	$ 215,252,920	$ 158,785,756
Average net assets (5)	$ 179,127,176	$ 153,804,303
Ratio of expenses to average net assets annualized (6)	10.55%	5.97%
Ratio of net expenses to average net assets annualized (7)	7.06%	4.44%
Ratio of net investment income to average net assets annualized	12.35%	12.51%

(1) Based on actual shares outstanding at the end of the corresponding period.

(2) Based on weighted average basic per share data.

(3) Total return equals the increase or decrease of the ending market value over the beginning market value plus monthly dividends divided by the monthly beginning market value, assuming monthly dividend reinvestment.

(4)

Amounts were not annualized.

(5) Average net assets are computed using the average of the balance of net assets at the end of each month of the reporting period.

(6) Ratio of expenses to average net assets is computed using expenses before credits from Adviser to the base management and incentive fees and including income tax expense.

(7) Ratio of net expenses to average net assets is computed using total expenses net of credits from Adviser to the base management and incentive fees and including income tax expense.

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

GLADSTONE CAPITAL CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2007
(UNAUDITED)

Note 1. Organization

Gladstone Capital Corporation (the "Company") was incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001. The Company is a closed-end, non-diversified management investment company that has elected to be treated as a business development company, or BDC, under the Investment Company Act of 1940, as amended (the "1940 Act"). In addition, the Company has elected to be treated for tax purposes as a regulated investment company ("RIC") under the Internal Revenue Code of 1986, as amended (the "Code"). The Company's investment objectives are to achieve a high level of current income by investing in debt and equity securities of established private businesses.

Gladstone Business Loan LLC ("Business Loan"), a wholly-owned subsidiary of the Company, was established on February 3, 2003 for the purpose of holding the Company's portfolio of loan investments. Gladstone Capital Advisers, Inc. is also a wholly-owned subsidiary.

Gladstone SSBIC Corporation ("Gladstone SSBIC"), a wholly-owned subsidiary of the Company, was established on November 21, 2006 for the purpose of holding a license to operate as a Specialized Small Business Investment Company. Gladstone SSBIC acquired this license in February 2007. This will enable the Company, through this subsidiary, to make investments in accordance with the United States Small Business Administration guidelines for specialized small business investment companies.

The financial statements of the subsidiaries are consolidated with those of the Company.

The Company is externally managed by Gladstone Management Corporation (the "Adviser"), an unconsolidated affiliate of the Company.

Note 2. Summary of Significant Accounting Policies

Unaudited Interim Financial Statements

Interim financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information and pursuant to the requirements for reporting on Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain disclosures accompanying annual financial statements prepared in accordance with GAAP are omitted. In the opinion of management, all adjustments, consisting solely of normal recurring accruals, necessary for the fair statement of financial statements for the interim periods have been included. The current period's results of operations 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 the Company's Form 10-K for the fiscal year ended September 30, 2006, as filed with the Securities and Exchange Commission (the "SEC") on December 6, 2006.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and

disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year presentation with no effect to net increase in net assets resulting from operations.

Investment Valuation

The Company carries its investments at fair value, as determined by its Board of Directors. Securities that are publicly traded are valued at the closing price on the valuation date. Securities for which a limited market exists, such as certain participations in syndicated loans, are valued at the indicative bid price on or near the valuation date from the respective originating syndication agent's trading desk. Debt and equity securities that are not publicly traded, or for which a limited market does not exist, are valued at fair value. The Company's Board of Directors has established a valuation policy and consistently applied valuation procedures used to determine the fair value of these securities quarterly.

The procedures for the determination of value of the Company's debt securities that that are not publicly traded and that are issued to portfolio companies where the Company has no equity, or equity-like securities, rely on the opinions of value submitted to us by Standard & Poor's Securities Evaluations, Inc. ("SPSE"). The Company may also submit paid in kind ("PIK") interest to SPSE for valuation when it is determined the PIK interest is likely to be received. SPSE will only evaluate the debt portion of the Company's investments for which the Company specifically requests evaluation, and may decline to make requested evaluations for any reason at its sole discretion. SPSE opinions of value are submitted to the Board of Directors along with the Adviser's supplemental assessment and recommendation regarding valuation of each of these investments. Lastly, the Company adds any amortized original issue discount ("OID") interest to the fair value, unless adverse factors lead to a determination of a lesser valuation.

The fair value of convertible debt, equity, success or exit fees or other equity-like securities is determined based on the collateral, the enterprise value of the issuer, the issuer's ability to make payments, the earnings of the issuer, recent sales to third parties of similar securities, the comparison to publicly traded securities, discounted cash flow or other pertinent factors. In gathering the sales to third parties of similar securities, the Company may reference industry statistics and use outside experts.

Debt securities that are issued to portfolio companies where the Company has equity, or equity-like securities are valued at cost, if there is adequate total enterprise value determined when valuing the Company's equity securities of the portfolio company. Fair values are discounted for any shortfall of total enterprise value over the total debt outstanding for the borrower.

The Board of Directors then reviews whether the Adviser has followed its established procedures for determinations of fair value, and votes whether or not to accept the recommended valuation of the Company's investment portfolio.

Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly from the values that would have resulted had a ready market for the securities existed, and the differences could be material. Additionally, changes in the market

environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuation currently assigned. Because there is a delay between when the Company closes an investment and when the investment can be evaluated by SPSE, new investments are not valued immediately by SPSE; rather, the Adviser makes its own determination about the recommended value of these investments in accordance with the Company's valuation policy without the input of SPSE during the specific quarter in which the investment is made. Because SPSE does not currently perform independent valuations of mortgage loans or equity securities for the Company, the Adviser also determines a recommendation for the fair value of these investments, if any, without the input of SPSE. The Adviser considers a number of qualitative and quantitative factors in current market conditions when performing valuations. The Board of Directors then determines whether or not to accept the Adviser's recommendations for the aggregate valuation of the Company's portfolio of investments. The Board of Directors is ultimately responsible for setting the fair value and disclosure of investments in the financial statements.

Interest Income Recognition

Interest income, adjusted for amortization of premiums and accretion of discounts, is recorded on the accrual basis to the extent that such amounts are expected to be collected. The Company stops accruing interest on its investments when it is determined that interest is no longer collectible. At June 30, 2007, one investment was on non-accrual. Conditional interest or a success fee is recorded when earned upon full repayment of a loan investment.

Paid in Kind Interest

The Company seeks to avoid PIK interest, however, the Company had one loan in its portfolio that contained a PIK provision during the six months ended March 31, 2006 and no loans with PIK provisions for the remainder of fiscal year 2006. A PIK provision requires the borrower to accrue a payment to the Company but the borrower does not have to pay that interest until the loan is paid in full. The PIK interest is added to the principal balance of the loan and recorded as income to the Company even though the cash has not been received. To maintain the Company's status as a RIC (as discussed in Note 10), this non-cash source of income must be paid out to stockholders in the form of cash dividends, even though the Company has not yet collected the cash. The Company recorded no PIK interest income for the three and nine months ended June 30, 2007 and $63,217, respectively, for the nine months ended June 30, 2006, there were no PIK loans in the Company's portfolio during the three months ended June 30, 2006.

Services Provided to Portfolio Companies

The 1940 Act requires that a business development company make available managerial assistance to its portfolio companies by providing significant guidance and counsel concerning the management, operations, or business objectives and policies of the respective portfolio company. The Company provides these and other services to its portfolio companies through its Adviser. Currently, neither the Company nor the Adviser charges a fee for managerial assistance.

The Adviser receives fees for other services it provides to portfolio companies. These other fees are typically non-recurring, are recognized as revenue when earned and are generally paid directly to the Adviser by the borrower or potential borrower upon closing of the investment. The services the Adviser provides to portfolio companies vary by investment, but generally include a broad array of services, such as investment banking services,

arranging bank and equity financing, structuring financing from multiple lenders and investors, reviewing existing credit facilities, restructuring existing investments, raising equity and debt capital, turnaround management, merger and acquisition services and recruiting new management personnel. When the Adviser receives fees for these services, fifty percent of certain of those fees are credited to the base management fees due to the Adviser from the Company. Any services of this nature subsequent to the closing would typically generate a separate fee at the time of completion.

The Adviser also receives fees for monitoring and reviewing portfolio company investments. These fees are recurring and are generally paid annually or quarterly in advance to the Adviser throughout the life of the investment. Fees of this nature are recorded as revenue by the Adviser when earned and are not credited against the base management fees.

While the Adviser receives all fees in connection with the Company's investments, such fees received by the Adviser, with the exception of monitoring and review fees, are credited to the Company as a reduction of the advisory fee payable under the advisory agreement between the Company and the Adviser. Prior to April 1, 2007, these fees were entirely credited against the advisory fee payable and starting on April 1, 2007, these fees were credited at 50% against the advisory fee payable. For the three and nine months ended June 30, 2007, the Adviser received $1,061,750 and $2,147,750, respectively, of such fees, of which $530,875 and $1,616,875, respectively, were credited against the base management fee payable for the three and nine months ended June 30, 2007, as compared to $539,000 and $1,762,000, respectively, for the three and nine months ended June 30, 2006 and the advisory fee payable by the Company to the Adviser was reduced by these amounts. None of these fees were for managerial assistance even though the Adviser provided managerial assistance to many of the Company's portfolio companies.

Cash and Cash Equivalents

Cash and cash equivalents consist of demand deposits and highly liquid investments with original maturities of three months or less when purchased. Cash and cash equivalents are carried at cost which approximates fair value as of June 30, 2007 and September 30, 2006.

Realized Gain or Loss and Unrealized Appreciation or Depreciation of Portfolio Investments

Realized gain or loss is recognized when an investment is disposed of and is computed as the difference between the Company's cost basis in the investment at the disposition date and the net proceeds received from such disposition. Unrealized appreciation or depreciation displays the difference between the fair market value of the investment and the cost basis of such investment.

Federal and State Income Taxes

The Company intends to continue to qualify for treatment as a RIC under Subchapter M of the Code. As a RIC, the Company is not subject to federal or state income tax on the portion of its taxable income and gains distributed to stockholders. To qualify as a RIC, the Company is required to distribute to its stockholders at least 90% of its investment company taxable income, as defined by the Code and, as such, no income tax provisions have been recorded for the individual companies of Gladstone Capital Corporation and Gladstone Business Loan LLC.

During the nine months ended June 30, 2006, Gladstone Capital Corporation recorded approximately $50,000 in connection with penalties incurred on misclassified revenue on its fiscal year 2004 corporate tax return.

Recent Accounting Pronouncements

In May 2005, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 154, *"Accounting Changes and Error Corrections,"* a replacement of APB Opinion No. 20, *"Accounting Changes,"* and SFAS No. 3, *"Reporting Accounting Changes in Interim Financial Statements"* and changed the requirements for the accounting for and reporting of a change in accounting principle. SFAS No. 154 applies to all voluntary changes in accounting principle and also applies to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. SFAS No. 154 requires retrospective application to prior periods' financial statements of changes in accounting principle. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The Company adopted the provisions of SFAS No. 154, as applicable, on October 1, 2006.

In February 2006, the FASB issued SFAS No. 155, *"Accounting for Certain Hybrid Financial Instruments, an amendment of FASB statements No. 133 and 140"* ("SFAS No. 155"). SFAS No. 155 allows financial instruments that have embedded derivatives to be accounted for as a whole (eliminating the need to bifurcate the derivative from its host) as long as the entire instrument is valued on a fair value basis. The statement also resolves and clarifies other specific SFAS No. 133 and SFAS No. 140 related issues. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company adopted SFAS No. 155 on October 1, 2006 and has not realized a material impact of the financial statements since all investments are valued on a fair value basis.

In June 2006, the FASB issued FASB Interpretation No. 48, *"Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109,"* which clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, *"Accounting for Income Taxes."* This Statement shall be effective as of the beginning of an entity's first fiscal year that begins after December 15, 2006. The Company will adopt this Interpretation effective October 1, 2007. The Company is currently evaluating the impact of this pronouncement on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *"Fair Value Measurements"* ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP, and expands disclosures about fair value measurements. SFAS No. 157 applies broadly to securities and other types of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within that fiscal year. The Company will be required to adopt SFAS No. 157 on October 1, 2008 and is currently evaluating the impact of this pronouncement on its consolidated financial statements.

In September 2006, the SEC issued Staff Accounting Bulletin No. 108 ("SAB 108"). SAB 108 addresses how the effects of prior year uncorrected misstatements should be considered when quantifying misstatements in current year financial statements and requires registrants to consider the effect of all carry over and reversing effects of prior year misstatements when quantifying errors in current year financial statements. SAB 108 does not change the SEC's previous guidance in SAB No. 99, *"Materiality,"* on evaluating the materiality of misstatements. A registrant applying the new guidance for the first time that identifies material errors in existence at the beginning of the first fiscal year ending after November 15, 2006, may correct those errors through a one-time cumulative effect adjustment

to beginning-of-year retained earnings. The cumulative effect alternative is available only if the application of the new guidance results in a conclusion that a material error exists as of the beginning of the first fiscal year ending after November 15, 2006, and those misstatements were determined to be immaterial based on a proper application of the registrant's previous method for quantifying misstatements. The adoption of SAB 108 did not have an impact on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *"The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115"* which is effective for fiscal years beginning after November 15, 2007. This pronouncement permits an entity to choose to measure many financial instruments and certain other items at fair value at specified election dates. Subsequent unrealized gains and losses on items for which the fair value option has been elected will be reported in earnings. The Company is currently evaluating the potential impact of this pronouncement on its consolidated financial statements.

Note 3. Investments

Investments at fair value consisted of the following industry classifications as of June 30, 2007 and September 30, 2006:

	June 30, 2007			September 30, 2006		
Industry Classification	**Fair Value**	**% of Total Investments**	**% of Net Assets**	**Fair Value**	**% of Total Investments**	**% of Net Assets**
Aerospace & Defense	$ 4,755,812	1.3%	2.2%	$ 5,529,891	2.5%	3.2%
Automobile	6,442,958	1.8%	3.0%	6,332,906	2.9%	3.7%
Broadcasting (TV, Radio & Cable)	36,289,808	9.8%	16.9%			
Cargo Transport	16,018,000	4.3%	7.4%	8,650,000	4.0%	5.0%
Chemicals, Plastics & Rubber	25,732,964	7.0%	12.0%	31,105,148	14.3%	18.0%
Diversified/Conglomerate Manufacturing	3,999,950	1.1%	1.9%			
Electronics	32,128,375	8.7%	14.9%	33,360,123	15.4%	19.3%
Entertainment				3,491,250	1.6%	2.0%
Farming & Agriculture	11,825,984	3.2%	5.5%	709,431	0.3%	0.4%
Finance	2,504,988	0.7%	1.2%			
Healthcare, Education & Childcare	39,512,077	10.7%	18.4%	16,707,500	7.7%	9.7%
Home & Office Furnishings	17,020,625	4.6%	7.9%	20,636,991	9.5%	12.0%
Leisure, Amusement & Movies	9,707,063	2.6%	4.5%			
Machinery	9,814,228	2.7%	4.6%			
Mining, Steel, Iron & Non-precious Metals	26,963,375	7.3%	12.5%	5,233,750	2.4%	3.0%
Oil & Gas	5,771,250	1.6%	2.7%	6,056,250	2.8%	3.5%
Personal, Food and Miscellaneous Services				6,011,288	2.8%	3.5%
Personal & Nondurable Consumer Products	9,000,000	2.4%	4.2%			
Printing, Publishing & Broadcasting	85,830,553	23.3%	39.9%	16,203,000	7.4%	9.4%
Retail Stores	14,925,000	4.0%	6.9%	14,981,250	6.9%	8.7%
Telecommunications				23,596,040	10.8%	13.7%
Textiles & Leather	10,706,237	2.9%	5.0%	13,785,932	6.3%	8.0%
Utilities				5,252,000	2.4%	3.0%
Total	$ 368,949,247	100.0%		$ 217,642,750	100.0%	

The investments at fair value consisted of the following geographic regions of the United States at June 30, 2007 and September 30, 2006:

	June 30, 2007		September 30, 2006	
Geographic Region	**Fair Value**	**% of Total Investments**	**Fair Value**	**% of Total Investments**
Midwest	$ 163,405,522	44.3%	$ 99,413,970	45.7%
West	72,358,060	19.6%	15,502,538	7.1%
Mid-Atlantic	57,231,151	15.5%	53,044,805	24.4%
Southeast	50,493,423	13.7%	24,697,113	11.3%
Northeast	17,705,250	4.8%	17,209,141	7.9%
US Territory	7,755,841	2.1%	7,775,183	3.6%
	$ 368,949,247	100.0%	$ 217,642,750	100.0%

The geographic region depicts the location of the headquarters for the Company's portfolio companies. A portfolio company may have a number of other locations in other geographic regions.

Note 4. Related Party Transactions

Loans to Employees

The Company provided loans to employees of the Adviser for the exercise of options under the Amended and Restated 2001 Equity Incentive Plan (the "2001 Plan"), which has since been terminated and is no longer in operation. The loans require the quarterly payment of interest at the market rate in effect at the date of issue, have varying terms not exceeding ten years and have been recorded as a reduction of net assets. The loans are evidenced by full recourse notes that are due upon maturity or 60 days following termination of employment, and the shares of common stock purchased with the proceeds of the loan are posted as collateral. No new loans were issued during the three and nine months ended June 30, 2007 and the Company received $300,941 of principal repayments during the nine months ended June 30, 2007. During the nine months ended June 30, 2006, the Company issued one loan to an employee for $199,980 and received principal repayments of $129,943 in connection with the full repayment of one loan and a partial repayment on another loan. The Company recognized interest income from all employee stock option loans of $132,795 and $403,917, respectively, for the three and nine months ended June 30, 2007, as compared to $108,877 and $323,003, respectively, for the three and nine months ended June 30, 2006.

Investment Advisory and Management and Administration Agreements

The Company is externally managed by the Adviser, which is controlled by our chairman and chief executive officer, under a contractual investment advisory agreement. On October 1, 2006, the Company entered into an amended and restated investment advisory agreement (the "Amended Advisory Agreement"). Prior to October 1, 2006, the relationship was governed by the initial advisory agreement (the "Initial Advisory Agreement").

Terms of the Amended Advisory Agreement

Under the Amended Advisory Agreement, the Company pays the Adviser an annual base management fee of 2% of its average gross assets, which is defined as total assets less cash and cash equivalents pledged to creditors calculated as of the end of the two most recently completed fiscal quarters and also consists of a two-part incentive fee.

The first part of the incentive fee is an income-based incentive fee which rewards the Adviser if the Company's quarterly net investment income (before giving effect to any incentive fee) exceeds 1.75% of the Company's net assets (the "hurdle rate"). The Company pays the Adviser an income incentive fee with respect to its pre-incentive fee net investment income in each calendar quarter as follows:

- no incentive fee in any calendar quarter in which its pre-incentive fee net investment income does not exceed the hurdle rate (7% annualized);

- 100% of 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 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 incentive fee that is determined and payable in arrears as of the end of each fiscal year (or upon termination of the Amended Advisory Agreement, as of the termination date) and equals 20% of the Company's realized capital gains as of the end of the fiscal year. In determining the capital gains incentive fee payable to the Adviser, the Company calculates the cumulative aggregate realized capital gains and cumulative aggregate realized capital losses since the Company's inception, and the aggregate unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in its portfolio.

The Adviser's board of directors voluntarily waived, for the fiscal quarter ended June 30, 2007, the annual 2.0% base management fee to 0.5% for senior syndicated loan participations and also waived a portion of the incentive fee due.

In addition to the base management and incentive fees under the Amended Advisory Agreement, certain fees received by the Adviser from the Company's portfolio companies were credited against the investment advisory fee under the Initial Advisory Agreement, and will continue to be paid to the Adviser and credited under the Amended Advisory Agreement. Effective April 1, 2007, 50% of certain of the fees received by the Adviser are credited against the base management fee. In addition, the Company will continue to pay its direct expenses including, but not limited to, directors' fees, legal and accounting fees, stockholder related expenses, and directors and officers insurance under the Amended Advisory Agreement.

For the three months ended June 30, 2007, the Company recorded a base management fee of $727,259, after reductions for loan servicing fees paid to the Adviser of $897,634, less a 50% credit of $530,875 for fees received by the Adviser and a $139,261 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee of $57,123 as compared to a base management fee of $334,814, after reductions for loan servicing fees paid to the Adviser of $693,965, less a credit of $539,000 for fees received by the Adviser and a $3,774 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee credit of $207,960 for the three months ended June 30, 2006. For the nine months ended June 30, 2007, the Company recorded a base management fee of $1,806,075, after reductions for loan servicing fees paid to the Adviser of $2,377,409, less a credit of $1,616,875 for fees received by the Adviser and a $369,161 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee credit of $179,961 as compared to a base management fee of $955,894, after reductions for loan servicing fees paid to the Adviser of $2,144,024, less a credit of $1,762,000 for fees received by the Adviser and a $3,774 fee reduction for the waiver of the 2% fee on senior syndicated loans to 0.5%, for a net base management fee credit of $809,880 for the

nine months ended June 30, 2006. The Company also recorded a gross incentive fee of $1,166,529 and $3,474,007, for the three and nine months ended June 30, 2007, respectively, offset by a credit from a voluntary waiver issued by the Adviser's board of directors of $1,038,752 and $2,696,124, for the three and nine months ended June 30, 2007, respectively, for a net incentive fee of $127,777 and $777,883, for the three and nine months ended June 30, 2007, respectively. There was no incentive fee in effect at June 30, 2006. As of June 30, 2007, the Company owed $57,123 of unpaid base management fee due to the Adviser and owed $127,777 of unpaid incentive fees to the Adviser, presented in the net fees due to Adviser in the accompanying consolidated statements of assets and liabilities. The credits to the base management fee and incentive fee are reflected on the consolidated statement of operations as credits to base management and incentive fees. 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.

Terms of the Initial Advisory Agreement

As compensation for its services, under the Initial Advisory Agreement, the Company paid the Adviser an annual advisory fee of 1.25% of total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.3125%, and an annual administrative fee of 0.75% of total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.1875%, for a total annual management fee of 2.0% (0.50% quarterly) of total assets (as reduced by cash and cash equivalents pledged to creditors). The Company also paid all of its direct expenses including, but not limited to, directors' fees, legal and accounting fees, stockholder related expenses, and directors and officers insurance.

Loan Servicing and Portfolio Company Fees

The Adviser also services the loans held by Business Loan, in return for which it receives a 1.5% annual fee based on the monthly aggregate outstanding balance of the loans pledged under the Company's line of credit. Since the Company owns these loans, all loan servicing fees paid to the Adviser have been and continue to be treated as reductions directly against the 2% management fee, under both the Initial and Amended Advisory Agreements. Effective in April 2006, the Adviser's board of directors voluntarily agreed to a waiver of the annual servicing fee rate for senior syndicated loans that, on a temporary basis, reduced the annual servicing fee rate on these loans to 0.5%. For the three and nine months ended June 30, 2007, these loan servicing fees totaled $897,634 and $2,377,409, respectively, as compared to the loan servicing fees for the three and nine months ended June 30, 2006 of $693,965 and $2,144,024, respectively, all of which were deducted against the 2% base management fee in order to derive the base management fee which is presented as the line item base management fee in the consolidated statements of operations. At June 30, 2007, the Company owed $219,339 of unpaid loan servicing fees to the Adviser, which are netted and recorded in fees due to Adviser. At September 30, 2006, the Company owed $214,608 in loan servicing fees to the Adviser, recorded in fees due to Adviser in the consolidated statements of assets and liabilities. Under the Initial and Amended Advisory Agreements, the Adviser has also provided and continues to provide managerial assistance and other services to the Company's portfolio companies and may receive fees for services other than managerial assistance services.

Administration Agreement

On October 1, 2006, the Company entered into an administration agreement (the "Administration Agreement") with Gladstone Administration, LLC (the "Administrator"), a wholly-owned subsidiary of the Adviser. Under the Administration Agreement, the Company pays separately for administrative services. The Administration Agreement provides for payments equal to the Company's allocable portion of the Administrator's overhead expenses in performing its obligations under the Administration Agreement, including, but not limited to, rent for employees of the Administrator, and the allocable portion of salaries and benefits expenses of the Company's chief financial officer, controller, chief compliance officer, treasurer and their respective staffs. The Company recorded an administration fee of $186,895 and $481,746, respectively, for the three and nine months ended June 30, 2007. The administration fee was not in effect during the three and nine months ended June 30, 2006.

Sale of Investments to Affiliate

During the three and nine months ended June 30, 2007, the Company sold to its affiliate, Gladstone Investment Corporation ("Gladstone Investment"), certain of its investments in syndicated loan participations at market value totaling approximately $9.7 million and approximately $22.1 million, respectively. An independent broker was engaged to execute these transactions between the Company and Gladstone Investment. The independent broker accepted the quotes from the respective agent bank for each syndicated loan and then executed these transactions between the Company and Gladstone Investment. The cumulative effect of these transactions, net of any unamortized premiums or discounts associated with the loans, resulted in a realized net gain of $26,965 and $83,182, respectively, for the three and nine months ended June 30, 2007. The sales that occurred during the three months ended June 30, 2007 were all initiated during the three months ended March 31, 2007.

Note 5. Line of Credit

Through Business Loan, the Company has a $220 million revolving credit facility (the "DB Facility") with Deutsche Bank AG, as administrative agent, pursuant to which Business Loan pledges the loans it holds to secure future advances by certain institutional lenders. The interest rate charged on the advances under the DB Facility is based on the London Interbank Offered Rate ("LIBOR"), the Prime Rate or the Federal Funds Rate, depending on market conditions, and adjusts periodically. The DB Facility is in effect through May 23, 2008. As of June 30, 2007, the outstanding principal balance under the DB Facility was $161,188,000 at an interest rate of approximately 5.3%. Available borrowings are subject to various constraints imposed under the credit agreement, based on the aggregate loan balance pledged by Business Loan, which varies as loans are added and repaid, regardless of whether such repayments are early prepayment or are made as contractually required. At June 30, 2007, the remaining borrowing capacity available under the DB Facility was approximately $58.8 million.

The DB Facility contains covenants that require Business Loan to maintain its status as a separate entity; prohibit certain significant corporate transactions (such as mergers, consolidations, liquidations or dissolutions); and restrict material changes to the Company's credit and collection policies. The DB Facility also restricts some of the terms and provisions (including interest rates, terms to maturity and payments schedules) and limits the borrower and industry concentrations of loans that are eligible to secure advances. As of June 30, 2007, Business Loan was in compliance with all of the facility covenants.

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

as custodian. Deutsche Bank AG is also the trustee of the account and once a month remits the collected funds to the Company. At June 30, 2007, the amount due from custodian was $3,129,891 and at September 30, 2006, the amount due from custodian was $3,587,152.

The Adviser also services the loans pledged under the DB Facility. As a condition to this servicing arrangement, the Company executed a performance guaranty pursuant to which it guaranteed that the Adviser would comply fully with all of its obligations under the DB Facility. The performance guaranty requires that the Company maintain a minimum net worth of $100 million and maintain "asset coverage" with respect to "senior securities representing indebtedness" of at least 200%, in accordance with Section 18 of the 1940 Act. As of June 30, 2007, the Company was in compliance with all covenants under the performance guaranty.

Note 6. Interest Rate Cap Agreement

Pursuant to the DB Facility, the Company has an interest rate cap agreement that effectively limits the interest rate on a portion of the borrowings under the line of credit.

The use of a cap involves risks that are different from those associated with ordinary portfolio securities transactions. Cap agreements may be considered to be illiquid. Although the Company will not enter into any such agreements unless it believes that the other party to the transaction is creditworthy, the Company does bear the risk of loss of the amount expected to be received under such agreements in the event of default or bankruptcy of the agreement counterparty.

In February 2004, the Company entered into an interest rate cap agreement with a notional amount of $35.0 million at a cost of $304,000. The interest rate cap agreement's current notional amount is $8.8 million and it has a current fair value of $24,407 which is recorded in other assets on the Company's consolidated balance sheet at June 30, 2007. At September 30, 2006, the interest rate cap agreement had a fair market value of $50,284. The Company records changes in the fair market value of the interest rate cap agreement monthly based on the current market valuation at month end as unrealized depreciation or appreciation on derivative on the Company's consolidated statement of operations. The interest rate cap agreement expires in February 2009. The agreement provides that the Company's floating interest rate or cost of funds on a portion of the portfolio's borrowings will be capped at 5% when the LIBOR rate is in excess of 5%. During the three and nine months ended June 30, 2007, the Company recorded $8,405 and $31,198, respectively, as compared to $1,367 for the three and nine months ended June 30, 2006 of income from the interest rate cap agreement recorded as a realized gain on the settlement of derivative on the Company's consolidated statements of operations.

Note 7. Common Stock Transactions

As of June 30, 2006 and June 30, 2007, 50,000,000 shares of $0.001 par value common stock were authorized and 11,384,363 and 14,249,683 shares were outstanding, respectively.

Transactions in common stock were as follows:

	Common Stock	
	Shares	**Amount**
Balance at September 30, 2005	11,303,510	$ 11,304
Issuance of Common Stock Under Stock Option Plan	80,853	81
Balance at June 30, 2006	11,384,363	$ 11,385
Balance at September 30, 2006	12,305,008	$ 12,305
Issuance of Common Stock Under Shelf Offering	2,000,000	2,000
Issuance of Common Stock Under Stock Option Plan	5,000	5
Stock surrendered for settlement of withholding tax	(60,325)	(60)
Balance at June 30, 2007	14,249,683	$ 14,250

In May 2007, the Company completed a public offering of 2,000,000 shares of its common stock at $24.25 per share, less an underwriting discount of $1.21 per share or 5%. In October 2006, 5,000 shares of common stock were issued as a result of an option exercise which took place on the last business day of the prior fiscal year. These shares were issued by the transfer agent at the start of the current fiscal year and during the nine months ended June 30, 2007, 60,325 shares of stock were surrendered to the Company from certain optionees who exercised non-qualified stock options during the third and fourth quarters of fiscal year 2006 in order to satisfy settlement of withholding taxes that were paid by the Company with respect to the shares underlying the exercise of such options.

Note 8. Stock Options

There were no stock options outstanding at June 30, 2007. Prior to its termination on September 30, 2006, the Company had authorized 2,000,000 shares of capital stock for the issuance of options under the 2001 Plan to employees and directors. Options granted under the 2001 Plan originally could have been exercised during a term not to exceed ten years from the date of grant. Only employees of the Company and its affiliates were eligible to receive incentive stock options and both employees and non-employee directors were eligible to receive nonstatutory stock options under the 2001 Plan. Options granted under the 2001 Plan were either incentive stock options or nonstatutory stock options. The option exercise price was equal to the market price on the date of the grant. In connection with the externalization of the Company's management, all of the Company's officers and employees became direct employees of the Adviser, as of October 1, 2004. However, these individuals continued to be eligible to receive stock options under the 2001 Plan. Effective October 1, 2004, the Company accounted for any options granted to employees of the Adviser, who qualify as leased employees of the Company under FASB Interpretation No. 44, *"Accounting for Certain Transactions Involving Stock Compensation, an Interpretation of APB Opinion No. 25."*

On October 1, 2005, the Company adopted SFAS No. 123 (revised 2004) "*Share-based Payment"* ("SFAS No. 123(R)") using the modified prospective approach. Under the modified prospective approach, stock-based compensation expense was recorded for the unvested portion of previously issued awards that remained outstanding at October 1, 2005 using the same estimate of the grant date fair value and the same attribution method previously used to determine the pro forma disclosure under SFAS No. 123. SFAS No. 123(R) also requires that all share-based payments to employees after October 1, 2005, including employee stock options, be recognized in the financial statements as stock-based compensation expense based on the fair value on the date of grant.

For the three and nine months ended June 30, 2006, the Company recorded stock option compensation expense for the cost of stock options issued under the 2001 Plan of $202,296 and $279,618, respectively. The Company's expensing of stock options decreased both basic and diluted net increase to net assets resulting from operations per share by $0.02 for the three and nine months ended June 30, 2006, respectively. Additionally, SFAS No. 123(R) states that any potential tax benefits associated with incentive stock options should be recognized only at the time of settlement if those options settle through a disqualifying disposition. Thus, the related stock-based compensation expense must be treated as a permanent difference until that time which, in turn, results in an increase to the Company's effective tax rate. The Company did not record tax benefits associated with the expensing of stock options since the Company intends to qualify as a RIC under Subchapter M of the Code and as such the Company is not subject to federal income tax on the portion of its taxable income and gains distributed to stockholders, provided that at least 90% of the taxable income is distributed.

Note 9. Increase in Net Assets Per Share Resulting from Operations

The following table sets forth the computation of basic and diluted net increase in net assets per share resulting from operations for the three and nine months ended June 30, 2007 and June 30, 2006:

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2007	**2006**	**2007**	**2006**
Numerator for basic and diluted net increase in net assets resulting from operations per share	$ 5,964,600	$ 5,543,076	$ 14,213,054	$ 19,366,806
Denominator for basic weighted average shares	13,561,511	11,337,291	12,701,845	11,317,437
Dilutive effect of stock options		233,134		231,617
Denominator for diluted weighted average shares	13,561,511	11,570,425	12,701,845	11,549,054
Basic net increase in net assets resulting from operations per share	$ 0.44	$ 0.49	$ 1.12	$ 1.71
Diluted net increase in net assets resulting from operations per share	$ 0.44	$ 0.48	$ 1.12	$ 1.68

There were no stock options outstanding at June 30, 2007. There were 1,224,645 options outstanding to purchase common stock at June 30, 2006. Of these, 336,000 options were not included in the computation of diluted earnings per share for the three and nine months ended June 30, 2006, because the options' exercise prices were greater than the average market price of the common shares for the period and, therefore, were anti-dilutive.

Note 10. Dividends

The Company is required to pay out as a dividend 90% of its ordinary income and short-term capital gains for each taxable year in order to maintain its status as a RIC under Subtitle A, Chapter 1 of Subchapter M of the Code. It is the policy of the Company to pay out as a dividend up to 100% of those amounts. The amount to be paid out as a dividend is determined by the Board of Directors each quarter and is based on the annual earnings estimated by the management of the Company. Based on that estimate, three monthly dividends are declared each quarter. At year-end the Company may pay a bonus dividend, in addition to the monthly dividends, to ensure that it has paid out at least 90% of its ordinary

income and realized net short-term capital gains for the year. Long-term capital gains are composed of success fees, prepayment fees and gains from the sale of securities held for one year or more. The Company intends to retain long-term capital gains from the sale of securities, if any, and not pay them out as dividends, however, the Board of Directors may decide to declare and pay out capital gains during any fiscal year. If the Company decides to retain long-term capital gains, the portion of the retained capital gains will be subject to 35% tax. The tax characteristics of all dividends will be reported to stockholders on Form 1099 at the end of each calendar year. The following table lists the per share dividends paid for the nine months ended June 30, 2007 and 2006:

Fiscal Year	Record Date	Payment Date	Dividend per Share
2007	June 21, 2007	June 29, 2007	$ 0.14
	May 22, 2007	May 31, 2007	$ 0.14
	April 20, 2007	April 30, 2007	$ 0.14
	March 22, 2007	March 30, 2007	$ 0.14
	February 20, 2007	February 28, 2007	$ 0.14
	January 23, 2007	January 31, 2007	$ 0.14
	December 20, 2006	December 29, 2006	$ 0.14
	November 21, 2006	November 30, 2006	$ 0.14
	October 23, 2006	October 31, 2006	$ 0.14
		Total	$ 1.26
2006	June 22, 2006	June 30, 2006	$ 0.135
	May 22, 2006	May 31, 2006	$ 0.135
	April 20, 2006	April 28, 2006	$ 0.135
	March 23, 2006	March 31, 2006	$ 0.135
	February 20, 2006	February 28, 2006	$ 0.135
	January 19, 2006	January 31, 2006	$ 0.135
	December 21, 2005	December 30, 2005	$ 0.135
	November 21, 2005	November 30, 2005	$ 0.135
	October 21, 2005	October 31, 2005	$ 0.135
		Total	$ 1.215

Note 11. Contractual Obligations

As of June 30, 2007, the Company was a party to signed and non-binding term sheets for two loan originations for an aggregate of $15.0 million. The Company expects to fund these potential investments as follows:

		Payment Due by Period			
Contractual Obligations	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Investments	15,000,000	15,000,000			
Total	$ 15,000,000	$ 15,000,000	$	$	$

All prospective investments are subject to, among other things, the satisfactory completion of the Company's due diligence investigation of each borrower, acceptance of terms and structure and receipt of necessary consents. With respect to each prospective loan, the Company will only agree to provide the loan if, among other things, the results of its due diligence investigations are satisfactory, the terms and conditions of the loan are acceptable

and all necessary consents are received. The Company has initiated its due diligence investigations of the potential borrowers, however there can be no guarantee that facts will not be discovered in the course of completing the due diligence that would render a particular investment imprudent or that any of these investments will actually be made.

As of July 31, 2007, the above mentioned investments had not yet funded.

Note 12. Subsequent Events

In July 2007, the Company's Board of Directors declared the following monthly cash dividends:

Fiscal Year	Record Date	Payment Date	Dividend per Share
2007	July 23, 2007	July 31, 2007	$ 0.14
	August 23, 2007	August 31, 2007	$ 0.14
	September 20, 2007	September 28, 2007	$ 0.14

On July 24, 2007, the Company completed an offering of 400,000 shares of its common stock, at a price of $20.41 per share, under a shelf registration statement on Form N-2 (File No. 333-143027), and pursuant to the terms set forth in a prospectus dated July 5, 2007, as supplemented by a final prospectus dated July 24, 2007. Net proceeds of the offering, after offering expenses, were approximately $8,149,000 and were used to repay outstanding borrowings under the Company's line of credit.

On July 26, 2007, a loan to an employee, and the shares pledged as collateral under the loan under a separate pledge agreement, were cancelled due to an event of default which was triggered by a stop loss provision in the employee's promissory note and pledge agreement. The provision specified that in the event that the aggregate value of the shares pledged under the note, as determined by the intra-day price of the shares on Nasdaq, became less than or equal to the aggregate outstanding principal amount of the note, the note would become immediately due and collectible through cancellation of the shares under the terms of the pledge agreement. The Company cancelled 37,109 shares which, in turn, cancelled via a non-cash transaction the remaining outstanding principal of the note of approximately $716,711.

PROSPECTUS

GLADSTONE CAPITAL CORPORATION

$300,000,000

COMMON STOCK
DEBT SECURITIES

We may offer, from time to time, up to $300 million aggregate initial offering price of our common stock, $0.001 par value per share, or debt securities, which we refer to in this prospectus collectively as our Securities, in one or more offerings. The Securities may be offered at prices and on terms to be set forth in one or more supplements to this prospectus. In the case of our common stock, the offering price per share, less any underwriting commissions or discounts, will not be less than the net asset value per share of our common stock at the time we make the offering. You should read this prospectus and the applicable prospectus supplement carefully before you invest in our Securities.

Our Securities may be offered directly to one or more purchasers, including existing stockholders in a rights offering, through agents designated from time to time by us, or to or through underwriters or dealers. The prospectus supplement relating to the offering will identify any agents or underwriters involved in the sale of our Securities, and will disclose any applicable purchase price, fee, commission or discount arrangement between us and our agents or underwriters or among our underwriters or the basis upon which such amount may be calculated. See "Plan of Distribution." We may not sell any of our Securities through agents, underwriters or dealers without delivery of a prospectus supplement describing the method and terms of the offering of such Securities. Our common stock is traded on The Nasdaq Global Select Market under the symbol "GLAD." As of July 3, 2007, the last reported sales price for our common stock was $21.24.

This prospectus contains information you should know before investing, including information about risks. Please read it before you invest and keep it for future reference. This prospectus may not be used to consummate sales of securities unless accompanied by a prospectus supplement.

An investment in our Securities involves certain risks, including, among other things, risks relating to investments in securities of small, private and developing businesses. We describe some of these risks in the section entitled "Risk Factors," which begins on page 9. Shares of closed-end investment companies frequently trade at a discount to their net asset value and this may increase the risk of loss of purchasers of our Securities. You should carefully consider these risks together with all of the other information contained in this prospectus and any prospectus supplement before making a decision to purchase our Securities.

The Securities being offered have not been approved or disapproved by the Securities and Exchange Commission or any state securities commission nor has the Securities and Exchange Commission or any state securities commission passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense. July 5, 2007

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

PROSPECTUS SUMMARY

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

GLADSTONE CAPITAL CORPORATION

General

We were incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001. Our investment objectives are to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, second lien notes, and senior subordinated notes of established private businesses that are backed by leveraged buyout funds, venture capital funds or others, with a particular emphasis on second lien and senior subordinated notes. In addition, we may acquire existing loans, which meet this profile, from leveraged buyout funds, venture capital funds and others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants, or other equity instruments that we may receive when we extend loans. We operate as a closed-end, non-diversified management investment company, and have elected to be treated as a business development company under the Investment Company Act of 1940, as amended, which we refer to in this prospectus as the 1940 Act.

We seek to invest in small and medium-sized businesses that meet certain criteria, including some or all of the following: (1) the potential for growth in cash flow, (2) adequate assets for loan collateral, (3) experienced management teams with a significant ownership interest in the borrower, (4) profitable operations based on the borrower's cash flow, (5) reasonable capitalization of the borrower (usually by buyout funds or venture capital funds) and (6) the potential to realize appreciation and gain liquidity in our equity position, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering by the borrower or by exercise of our right to require the borrower to buy back its warrants. We lend to borrowers that need funds to, among other things, effect a change of control, restructure their balance sheets, or finance growth, including acquisitions. Our loans typically range from $5 million to $15 million, although this investment size may vary proportionately as the size of our capital base changes, generally mature in no more than seven years and accrue interest at fixed or variable rates.

Our Investment Adviser and Administrator

Our Adviser, is our affiliate and investment adviser and is led by a management team which has extensive experience in our lines of business. All of our directors and executive officers serve as either directors or executive officers, or both, of Gladstone Commercial, a publicly traded real estate investment trust; Gladstone Investment, a publicly traded business development company; our Adviser; and our Administrator. Our Adviser also has a wholly-owned subsidiary, our Administrator, which employs our chief financial officer, chief compliance officer, controller, treasurer and their respective staffs.

Our Adviser and our Administrator also provide investment advisory and administrative services to our affiliates Gladstone Commercial, Gladstone Investment and Gladstone Land Corporation, an agricultural real estate company owned by Mr. Gladstone. In the future, our Adviser may provide

investment advisory and administrative services to other funds, both public and private, of which it is the sponsor.

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

Our Investment Objectives and Our Strategy

We seek to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, senior subordinated notes and junior subordinated notes, of established private businesses that are backed by leveraged buyout funds, venture capital funds or others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants or other equity instruments that we may receive when we make loans. There can be no assurance that we will realize our investment objectives. We seek to invest primarily in three categories of debt of private companies:

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

Senior Notes. We seek to invest a portion of our assets in senior notes of borrowers. Using its assets and cash flow as collateral, the borrower typically uses senior notes to cover a substantial portion of the funding needed to operate. Senior lenders are exposed to the least risk of all providers of debt because they command a senior position with respect to scheduled interest and principal payments. However, unlike senior subordinated and junior subordinated lenders, these senior lenders typically do not receive any stock, warrants to purchase stock of the borrowers or other yield enhancements. As such, they generally do not participate in the equity appreciation of the value of the business. Senior notes may include revolving lines of credit, senior term loans, senior syndicated loans and senior last-out tranche loans.

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

THE OFFERING

We may offer, from time to time, up to $300,000,000 of our Securities, on terms to be determined at the time of the offering. Our Securities may be offered at prices and on terms to be disclosed in one or more prospectus supplements. In the case of the offering of our common stock, the offering price per share less any underwriting commissions or discounts will not be less than the net asset value per share of our common stock at the time of the offering.

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

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

The Nasdaq Global Select Market Symbol	GLAD
Use of Proceeds	Unless otherwise specified in a prospectus supplement, we intend to use the net proceeds from the sale of our Securities for general corporate purposes. We expect the proceeds to be used first to pay down existing short-term debt, then to make investments in small and medium sized businesses in accordance with our investment objectives, and any remaining proceeds to be used for other general corporate purposes. See "Use of Proceeds."
Dividends and Distributions	We have paid monthly dividends to the holders of our common stock and generally intend to continue to do so. The amount of the monthly dividends is determined by our Board of Directors on a quarterly basis and is based on our estimate of our annual investment company taxable income and net short-term taxable capital gains. See "Price Range of Common Stock and Distributions." Certain additional amounts may be deemed as distributed to stockholders for income tax purposes. Other types of securities will likely pay distributions in accordance with their terms.
Taxation	We intend to continue to elect to be treated for federal income tax purposes as a regulated investment company, which we refer to as a RIC. Accordingly, we generally will pay no corporate-level federal income taxes on any ordinary income or capital gains that we distribute to our stockholders. To maintain our RIC status, we must meet specified source-of-income and asset diversification requirements and distribute annually at least 90% of our taxable ordinary income and realized net short-term capital gains in excess of realized net long-term capital losses, if any, out of assets legally available for distribution. See "Price Range of Common Stock and Distributions."
Trading at a Discount	Shares of closed-end investment companies frequently trade at a discount to their net asset value. The possibility that our shares may trade at a discount to our net asset value is separate and distinct from the risk that our net asset value per share may decline. We cannot predict whether our shares will trade above, at or below net asset value.

Certain Anti-Takeover Provisions	Our Board of Directors is divided into three classes of directors serving staggered three-year terms. This structure is intended to provide us with a greater likelihood of continuity of management, which may be necessary for us to realize the full value of our investments. A staggered board of directors also may serve to deter hostile takeovers or proxy contests, as may certain provisions of Maryland law and other measures we have adopted. See "Certain Provisions of Maryland Law and of Our Articles of Incorporation and Bylaws."
Dividend Reinvestment Plan	We have a dividend reinvestment plan for our stockholders. This is an "opt in" dividend reinvestment plan, meaning that stockholders may elect to have their cash dividends automatically reinvested in additional shares of our common stock. Stockholders who do not so elect will receive their dividends in cash. Stockholders who receive distributions in the form of stock will be subject to the same federal, state and local tax consequences as stockholders who elect to receive their distributions in cash. See "Dividend Reinvestment Plan."
Management Arrangements	Gladstone Management Corporation serves as our investment adviser, and Gladstone Administration, LLC serves serve as our administrator. We have entered into a license agreement with our Adviser, pursuant to which our Adviser has agreed to grant us a non-exclusive license to use the name "Gladstone" and the Diamond G logo. For a description of our Adviser, our Administrator, the Gladstone Companies and our contractual arrangements with these companies, see "Management Certain Transactions Advisory and Administration Agreements," and "Management Certain Transactions License Agreement."

Fees and Expenses

The following table is intended to assist you in understanding the costs and expenses that an investor in this offering will bear directly or indirectly. We caution you that some of the percentages indicated in the table below are estimates and may vary. Except where the context suggests otherwise, whenever this prospectus contains a reference to fees or expenses paid by "us" or "Gladstone Capital," or that "we" will pay fees or expenses, stockholders will indirectly bear such fees or expenses as investors in Gladstone Capital. The following percentages were calculated based on net assets as of March 31, 2007.

	Current
Stockholder Transaction Expenses	
Sales load (as a percentage of offering price)	%
Dividend reinvestment plan expenses(1)	None
Estimated annual expenses (as a percentage of net assets attributable to common stock)	
Management fees(2)	3.44%
Incentive fees payable under investment advisory and management agreement (20% of realized capital gains and 20% of pre-incentive fee net investment income)(3)	2.74%
Interest Payments on Borrowed Funds(4)	4.44%
Other expenses	1.26%
Total annual expenses (estimated)(2)(5)	11.88%

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

(2) Our annual base management fee is 2.0% (0.5% quarterly) of our average gross assets, which is defined as total assets of Gladstone Capital, including investments made with proceeds of borrowings, less any uninvested cash or cash equivalents pledged to creditors. See "Management Advisory and Administration Agreements" and footnote 3 below.

(3) The incentive fee consists of two parts: an income-based fee and a capital gains-based fee. The income-based fee will be payable quarterly in arrears, and will equal 20% of the excess, if any, of our pre-incentive fee net investment income that exceeds a 1.75% quarterly (7.0% annualized) hurdle rate, subject to a "catch-up" provision measured as of the end of each calendar quarter. The "catch-up" provision requires us to pay 100% of our pre-incentive fee net investment income with respect to that portion of such income, if any, that exceeds the hurdle rate but is less than 125% of the quarterly hurdle rate (or 2.1875%) in any calendar quarter (8.75% annualized). The catch-up provision is meant to provide our Adviser with 20% of our pre-incentive fee net investment income as if a hurdle rate did not apply when our pre-incentive fee net investment income exceeds 125% of the quarterly hurdle rate in any calendar quarter (8.75% annualized). The income-based incentive fee will be computed and paid on income that may include interest that is accrued but not yet received in cash. Our pre-incentive fee net investment income used to calculate this part of the income incentive fee is also included in the amount of our gross assets used to calculate the 2% base management fee (see footnote 2 above). The quarter ended December 31, 2006 was the first quarter under our new advisory agreement and, as a result, was the first quarter in which the incentive fee was earned. For purposes of this computation, the aggregate gross amount of the December 31, 2006 and March 31, 2007 fees, exclusive of any credits, was annualized to determine the percentage the fee represents of net assets. After giving effect to credits against the incentive fee, the annualized incentive fee was 0.17% of net assets as of March 31, 2007. There can be no assurance that our Adviser will give any credits against the incentive fee in the future. The capital gains-based portion of the fee did not have an effect on the incentive fee for purposes of this calculation since we have not realized overall net capital gains to date.

Examples of how the incentive fee would be calculated (exclusive of any credits) are as follows:

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

Assuming pre-incentive fee net investment income of 2.00%, the income-based incentive fee would be as follows:
= 100% × (2.00% - 1.75%)

= 0.25%

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

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

= (100% × 0.4375%) + (20% × 0.1125%)

= 0.4375% + 0.0225%

= 0.46%

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

= 20% × (6% - 1%)

= 20% × 5%

= 1%

For a more detailed discussion of the calculation of the two-part incentive fee, see "Management Advisory and Administration Agreements."

(4) We have entered into a revolving credit facility, under which our borrowing capacity is $220 million, effective May 29, 2007. We have drawn down on this credit facility and we expect to borrow additional funds in the future up to an amount so that our asset coverage, as defined in the 1940 Act, is at least 200% after each issuance of our senior securities. Assuming that we borrowed $220 million at an interest rate of 6.07%, interest payments on borrowed funds would have been 7.89% of our net assets as of March 31, 2007.

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

Example

The following example demonstrates the projected dollar amount of total cumulative expenses that would be incurred over various periods with respect to a hypothetical investment in our Securities. In calculating the following expense amounts, we have assumed we would have no leverage and that our annual operating expenses would remain at the levels set forth in the table above. In the event that Securities to which this prospectus relates are sold to or through underwriters, a corresponding prospectus supplement will restate this example to reflect the applicable sales load.

	1 Year	3 Years	5 Years	10 Years
You would pay the following expenses on a $1,000 investment, assuming a 5% annual return	$ 89	$ 257	$ 412	$ 745

While the example assumes, as required by the Securities and Exchange Commission, which we refer to as the SEC, a 5% annual return, our performance will vary and may result in a return greater or less than 5%. Additionally, we have assumed that the entire amount of such 5% annual return would constitute ordinary income as we have not historically realized positive capital gains (computed net of all realized capital losses and unrealized capital depreciation) on our investments, nor do we expect to realize positive capital gains in the foreseeable future. Because the assumed 5% annual return is significantly below the hurdle rate of 7% (annualized) that we must achieve under the investment advisory and management agreement to trigger the payment of an income-based incentive fee, we have assumed, for purposes of the above example, that no income-based incentive fee would be payable if we realized a 5% annual return on our investments. Additionally, because we have not historically realized positive capital gains (computed net of all realized capital losses and unrealized capital depreciation) on our investments, we have assumed that we will not trigger the payment of any capital gains-based incentive fee in any of the indicated time periods. If we achieve sufficient returns on our investments, including through the realization of capital gains, to trigger an incentive fee of a material amount, our expenses, and returns to our investors after such expenses, would be higher than reflected in the example. In addition, while the example assumes reinvestment of all dividends and distributions at net asset value, participants in our dividend reinvestment plan will receive a number of shares of our common stock, determined by dividing the total dollar amount of the dividend payable to

a participant by the market price per share of our common stock at the close of trading on the valuation date for the dividend. See "Dividend Reinvestment Plan" for additional information regarding our dividend reinvestment plan.

This example and the expenses in the table above should not be considered a representation of our future expenses, and actual expenses (including the cost of debt and incentive fees, if any, and other expenses) may be greater or less than those shown. As noted in the Fees and Expenses table above, we estimate that annual incentive fees payable under the investment advisory and management agreement will be 2.74% of net assets attributable to common stock.

CONSOLIDATED SUMMARY FINANCIAL DATA
(in thousands, except per share data)

The following table summarizes our consolidated financial data. The summary financial data as of and for the years ended September 30, 2006, 2005 and 2004 is derived from our audited consolidated financial statements included in this prospectus. The summary financial data as of and for the years ended September 30, 2003 and 2002 is derived from our audited consolidated financial statements that are not included in this prospectus. The summary financial data as of and for the six months ended March 31, 2007 and 2006 is derived from our unaudited consolidated financial statements included in this prospectus. You should read this data together with our consolidated financial statements and notes thereto presented elsewhere in this prospectus and the information under "Consolidated Selected Financial Data" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" for more information.

	Year Ended September 30, 2006	Year Ended September 30, 2005	Year Ended September 30, 2004	Year Ended September 30, 2003	Year Ended September 30, 2002	Six Months Ended March 31, 2007	Six Months Ended March 31, 2006
						(unaudited)	(unaudited)
Total Investment Income	$ 26,899,846	$ 23,949,759	$ 20,395,968	$ 15,154,874	$ 10,455,703	$ 16,877,496	$ 13,031,019
Total Net Expenses	$ 7,549,266	$ 6,663,614	$ 7,103,193	$ 3,858,953	$ 2,839,102	$ 5,990,213	$ 3,384,789
Net Investment Income	$ 19,350,580	$ 17,286,145	$ 13,292,775	$ 11,295,921	$ 7,616,601	$ 10,887,283	$ 9,646,230
Net Increase in Net Assets Resulting from Operations	$ 24,430,235	$ 15,490,682	$ 10,570,290	$ 11,073,581	$ 7,616,601	$ 8,248,454	$ 13,823,730
Per Share Data:							
Net Increase in Net Assets Resulting from Operations:							
Basic	$ 2.15	$ 1.37	$ 1.05	$ 1.10	$ 0.76	$ 0.67	$ 1.22
Diluted	$ 2.10	$ 1.33	$ 1.02	$ 1.09	$ 0.75	$ 0.67	$ 1.20
Cash Distributions Declared per Share	$ 1.635	$ 1.515	$ 1.365	$ 1.10	$ 0.81	$ 0.84	$ 0.81
Statement of Assets and Liabilities Data:							
Total Assets	$ 225,783,215	$ 205,793,094	$ 215,333,727	$ 214,566,663	$ 172,922,039	$ 291,015,954	$ 217,725,319
Net Assets	$ 172,570,487	$ 151,610,683	$ 152,226,655	$ 130,802,382	$ 130,663,273	$ 169,323,895	$ 156,461,511
Other Data:							
Number of Portfolio Companies at Period End	32	28	16	11	7	51	28
Principal Amount of Loan Originations	$ 135,954,879	$ 143,794,006	$ 86,267,500	$ 47,011,278	$ 97,705,054	$ 127,641,175	$ 65,159,566
Principal Amount of Loan Repayments	$ 124,009,929	$ 88,019,136	$ 47,158,995	$ 18,005,827	$ 18,387,191	$ 62,230,246	$ 63,517,133
Total Return(1)	5.21%	5.93%	24.40%	21.74%	9.60%	11.50%	(0.75)%
Weighted Average Yield on Investments(2):							
With PIK Interest(3)	12.74%	12.36%	13.78%	13.86%	14.79%	n/a	12.56%
Without PIK Interest(3)	12.74%	12.23%	13.44%	13.14%	13.82%	12.58%	12.56%

(1) For the fiscal years ended September 30, 2006, 2005 and 2004, the total return equals the increase of the ending market value over the beginning market value plus monthly dividends divided by the monthly beginning market value. For the fiscal years ended September 30, 2003 and 2002, total return equals the increase of the ending market value over the beginning market value, plus distributions, dividend by the beginning market value.

(2) Weighted average yield on investments equals interest income on investments divided by the average investment balance throughout the year.

(3) Refer to Note 2 of the "Notes to Consolidated Financial Statements" for an explanation of PIK, or "Paid-in-Kind," interest.

ADDITIONAL INFORMATION

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

We also file reports, proxy statements and other information with the SEC under the Securities Exchange Act of 1934, as amended, which we refer to as the Exchange Act. Such reports, proxy statements and other information, as well as the registration statement and the amendments, exhibits and schedules thereto, can be inspected at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. Information about the operation of the public reference facilities may be obtained by calling the SEC at 1-202-551-8090. The SEC maintains a web site that contains reports, proxy statements and other information regarding registrants, including us, that file such information electronically with the SEC. The address of the SEC's web site is http://www.sec.gov. Copies of such material may also be obtained from the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates. Our common stock is listed on The Nasdaq Global Select Market and our corporate website is located at http://www.gladstonecapital.com. The information contained on, or accessible through, our website is not a part of this prospectus.

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

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

RISK FACTORS

You should carefully consider the risks described below and all other information provided and incorporated by reference in this prospectus (or any prospectus supplement) before making a decision to purchase our Securities. The risks and uncertainties described below are not the only ones facing us. Additional risks and uncertainties not presently known to us, or not presently deemed material by us, may also impair our operations and performance.

If any of the following risks actually occur, our business, financial condition or results of operations could be materially adversely affected. If that happens, the trading price of our Securities could decline, and you may lose all or part of your investment.

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

We have no employees. Our chief executive officer, chief operating officer, chief investment officer and chief financial officer, and the employees of our Adviser, do not spend all of their time managing our activities and our investment portfolio. We are particularly dependent upon David Gladstone, George Stelljes III and Terry Lee Brubaker in this regard. Our executive officers and the employees of our Adviser allocate some, and in some cases a material portion, of their time to businesses and activities that are not related to our business. We have no separate facilities and are completely reliant on our Adviser, which has significant discretion as to the implementation and execution of our business

strategies and risk management practices. We are subject to the risk of discontinuation of our Adviser's operations or termination of the investment advisory agreement and the risk that, upon such event, no suitable replacement will be found. We believe that our success depends to a significant extent upon our Adviser and that discontinuation of its operations could have a material adverse effect on our ability to achieve our investment objectives.

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

On December 2, 2005, our stockholders approved a proposal to enter into an amended and restated investment advisory agreement with our Advisor, which we refer to as the Amended Advisory Agreement. On October 1, 2006, the Amended Advisory Agreement became effective. The Amended Advisory Agreement entitles our Adviser to incentive compensation for each fiscal quarter in an amount equal to a percentage of the excess of our investment income for that quarter (before deducting incentive compensation, net operating losses and certain other items) above a threshold return for that quarter. Our pre-incentive fee net investment income for incentive compensation purposes excludes realized and unrealized capital losses that we may incur in the fiscal quarter, even if such capital losses result in a net loss on our statement of operations for that quarter. Thus, we may be required to pay our Adviser incentive compensation for a fiscal quarter even if there is a decline in the value of our portfolio or we incur a net loss for that quarter. For additional information on incentive compensation under the Amended Advisory Agreement with our Adviser, see "Business Investment Advisory and Administration Agreements Management services and fees under the amended and restated investment advisory agreement."

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

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

We operate in a highly competitive market for investment opportunities.

A large number of entities compete with us and make the types of investments that we seek to make in small and medium-sized privately owned businesses. We compete with a large number of private equity funds, leveraged buyout funds and venture capital funds, investment banks and other equity and non-equity based investment funds, and other sources of financing, including traditional financial services companies such as commercial banks. Many of our competitors are substantially larger and have considerably greater financial, technical and marketing resources than we do. For example, some competitors may have a lower cost of funds and access to funding sources that are not available to us. In addition, certain of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments and establish more relationships and build their market shares. Furthermore, many of our potential competitors are not subject to the regulatory restrictions that the 1940 Act imposes on us as a business development company. We cannot assure you that the competitive pressures we face will not have a material adverse effect on our business, financial condition and results of operations. Also, as a result of this

competition, we may not be able to take advantage of attractive investment opportunities from time to time and there can be no assurance that we will be able to identify and make investments that satisfy our investment objectives or that we will be able to fully invest our available capital.

Our business model is dependent upon developing and sustaining strong referral relationships with leveraged buyout funds and venture capital funds.

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

Our loans to small and medium-sized borrowers are extremely risky and you could lose all or a part of your investment.

Loans to small and medium-sized borrowers are subject to a number of significant risks including the following:

Small and medium-sized businesses may have limited financial resources and may not be able to repay the loans we make to them. Our strategy includes providing financing to borrowers that typically is not readily available to them. While we believe that this provides an attractive opportunity for us to generate profits, this may make it difficult for the borrowers to repay their loans to us upon maturity. A borrower's ability to repay its loan may be adversely affected by numerous factors, including the failure to meet its business plan, a downturn in its industry or negative economic conditions. Deterioration in a borrower's financial condition and prospects usually will be accompanied by deterioration in the value of any collateral and a reduction in the likelihood of us realizing on any guarantees we may have obtained from the borrower's management. Although we will sometimes seek to be the senior, secured lender to a borrower, in most of our loans we expect to be subordinated to a senior lender, and our interest in any collateral would, accordingly, likely be subordinate to another lender's security interest.

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

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

Small and medium-sized businesses generally have less predictable operating results. We expect that our borrowers may have significant variations in their operating results, may from time to time be parties to litigation, may be engaged in rapidly changing businesses with products subject to a substantial risk of obsolescence, may require substantial additional capital to support their operations, to finance expansion or to maintain their competitive position, may otherwise have a weak financial position or may be adversely affected by changes in the business cycle. Our portfolio companies may not meet net income, cash flow and other coverage tests typically imposed by their senior lenders. A borrower's failure to satisfy financial or operating

covenants imposed by senior lenders could lead to defaults and, potentially, foreclosure on its senior credit facility, which could additionally trigger cross-defaults in other agreements. If this were to occur, it is possible that the borrower's ability to repay our loan would be jeopardized.

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

Small and medium-sized businesses are likely to have greater exposure to economic downturns than larger businesses. We expect that our borrowers will have fewer resources than larger businesses and an economic downturn is more likely to have a material adverse effect on them. If one of our borrowers is adversely impacted by an economic downturn, its ability to repay our loan would be diminished.

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

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

When we make a subordinated loan, we may receive warrants to purchase stock issued by the borrower or other yield enhancements, such as success fees (conditional interest). Our goal is to ultimately dispose of these equity interests and realize gains upon our disposition of such interests. We expect that, over time, the gains we realize on these warrants and other yield enhancements will offset any losses we experience on loan defaults. However, any warrants we receive may not appreciate in value and, in fact, may decline in value and any other yield enhancements, such as success fees, may not be realized. Accordingly, we may not be able to realize gains from our equity interests or other yield enhancements and any gains we do recognize may not be sufficient to offset losses we experience on our loan portfolio. Because the loans we make and equity securities we receive when we make loans are not publicly traded, there will be uncertainty regarding the value of our privately held securities that could adversely affect our determination of our net asset value.

A large percentage of our portfolio investments are, and will continue to be, in the form of securities that are not publicly traded. The fair value of securities and other investments that are not publicly traded may not be readily determinable. Our Board of Directors has established a valuation policy and consistently applied valuation procedures used to determine the fair value of these securities quarterly. These procedures for the determination of value of many of our debt securities rely on the opinions of value submitted to us by Standard & Poor's Securities Evaluations, Inc., which we refer to as SPSE. SPSE will only evaluate the debt portion of our investments for which we specifically request evaluation, and SPSE may decline to make requested evaluations for any reason in its sole discretion. However, to date, SPSE has accepted each of our requests for evaluation.

Our procedures also include provisions whereby our Adviser will establish the fair value of any equity securities we may hold where SPSE is unable to provide evaluations. The types of factors that may be considered in determining the fair value of our debt and equity investments include some or all of the following: the nature and realizable value of any collateral, the portfolio company's earnings and cash flows and its ability to make payments on its obligations, the markets in which the portfolio company does business, comparison to publicly traded companies, discounted cash flow, and other relevant factors. Because such valuations, particularly valuations of private securities and private companies, are inherently uncertain, may fluctuate over short periods of time, and may be based on

estimates, our determinations of fair value may differ materially from the values that might have resulted from a readily available market for these securities.

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

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

Most of our investments presently consist of, and will continue to consist of, loans and warrants acquired in private transactions directly from borrowers or from the originators of loans to such borrowers. Substantially all of the investments we presently hold are, and the investments we expect to acquire in the future will be, subject to restrictions on resale, including, in some instances, legal restrictions, or will otherwise be less liquid than publicly traded securities. The illiquidity of our investments may make it difficult for us to quickly obtain cash equal to the value at which we record our investments if the need arises. This could cause us to miss important business opportunities. In addition, if we are required to quickly liquidate all or a portion of our portfolio, we may realize significantly less than the value at which we have previously recorded our investments. In addition, we may face other restrictions on our ability to liquidate an investment in a portfolio company to the extent that we, our Adviser, or our respective officers, employees or affiliates have material non-public information regarding such portfolio company.

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

Our business plan is dependent upon external financing which may expose us to risks associated with leverage.

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

Senior Securities. We intend to issue debt securities, other evidences of indebtedness (including borrowings under our line of credit) and possibly preferred stock, up to the maximum amount permitted by the 1940 Act. The 1940 Act currently permits us, as a business development company, to issue debt securities and preferred stock, to which we refer collectively as senior securities, in amounts such that our asset coverage, as defined in the 1940 Act, is at least 200% after each issuance of senior securities. As a result of issuing senior securities, we will be exposed to the risks associated with leverage. Although borrowing money for investments increases the potential for gain, it also increases the risk of a loss. A decrease in the value of our investments will have a greater impact on the value of our common stock to the extent that we have borrowed money to make investments. There is a possibility that the costs of borrowing could exceed the income we receive on the investments we make with such borrowed funds. In addition, our ability to pay dividends or incur additional indebtedness would be restricted if asset coverage is not at least twice our indebtedness. If the value of our assets declines, we might be

unable to satisfy that test. If this happens, we may be required to liquidate a portion of our loan portfolio and repay a portion of our indebtedness at a time when a sale may be disadvantageous. Furthermore, any amounts that we use to service our indebtedness will not be available for distributions to our stockholders.

Common Stock. Because we are constrained in our ability to issue debt for the reasons given above, we are dependent on the issuance of equity as a financing source. If we raise additional funds by issuing more common stock or debt securities convertible into or exchangeable for our common stock, the percentage ownership of our stockholders at the time of the issuance would decrease and they may experience dilution. In addition, any convertible or exchangeable securities that we issue in the future may have rights, preferences and privileges more favorable than those of our common stock.

Securitization. In addition to issuing securities to raise capital as described above, we anticipate that in the future we will securitize our loans to generate cash for funding new investments. An inability to successfully securitize our loan portfolio could limit our ability to grow our business, fully execute our business strategy and impact our profitability. Moreover, successful securitization of our loan portfolio might expose us to losses as the loans in which we do not plan to sell interests will be those that are riskier and more apt to generate losses.

A change in interest rates may adversely affect our profitability and our hedging strategy may expose us to additional risks.

We anticipate using a combination of equity and long-term and short-term borrowings to finance our lending activities. As a result, a portion of our income will depend upon the difference between the rate at which we borrow funds and the rate at which we loan these funds. Certain of our borrowings may be at fixed rates and others at variable rates. Ultimately, we expect approximately 20% of the loans in our portfolio to be at fixed rates and approximately 80% to be at variable rates determined on the basis of a benchmark prime rate. As of March 31, 2007, our portfolio had approximately 56% of the total of the loan cost value at variable rates with a floor, approximately 2% of the total loan cost value at variable rates with a floor and ceiling, 40% at variable rates without a floor or ceiling and approximately 1% of the total loan portfolio cost basis at a fixed rate. Pursuant to our initial line of credit, we agreed to enter into hedging transactions such as interest rate cap agreements, futures, options and forward contracts. To date, we hold only one interest rate cap agreement. In the event that we securitize a portion of our loan portfolio in the future, we believe that we will likely be required to enter into similar arrangements with respect to the securitized loans. While hedging activities may insulate us against adverse fluctuations in interest rates, they may also limit our ability to participate in the benefits of lower interest rates with respect to the hedged portfolio. Adverse developments resulting from changes in interest rates or hedging transactions could have a material adverse effect on our business, financial condition and results of operations.

Our credit facility imposes certain limitations on us.

We will have a continuing need for capital to finance our loans. In order to maintain RIC status, we will be required to distribute to our stockholders at least 90% of our ordinary income and short-term capital gains on an annual basis. Accordingly, such earnings will not be available to fund additional loans. Therefore, we are party to a credit agreement arranged by Deutsche Bank AG as the structuring agent. The agreement provides us with a revolving credit line facility of $220 million. In the future, borrowings outstanding on the credit line facility may be repaid with the proceeds we may receive from securitizing some or all of the loans in our portfolio for long-term funding. The line of credit facility will permit us to fund additional loans and investments as long as we are within the conditions set out in the credit agreement.

As a result of the line of credit facility, we are subject to certain limitations on the type of loan investments we make, including restrictions on geographic concentrations, sector concentrations, loan size, payment frequency and status, and average life. Our failure to satisfy these limitations could result in foreclosure by our lenders which would have a material adverse effect on our business, financial condition and results of operations.

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

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

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

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

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

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

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

Our executive officers and directors, and the officers and directors of our Adviser and our Administrator serve or may serve as officers, directors or principals of entities that operate in the same or a related line of business as we do or of investment funds managed by our affiliates. Accordingly, they may have obligations to investors in those entities, the fulfillment of which might not be in the best interests of us or our stockholders. In addition, all of our directors and executive officers serve as either directors or executive officers, or both, of Gladstone Commercial and Gladstone Investment and our Adviser and Administrator also provide investment advisory and administrative services to these affiliates as well as Gladstone Land. In the future, our Adviser and our Administrator may provide investment advisory and administrative services, as applicable, to other funds, both public and private, of which it is the sponsor. Moreover, our Adviser may establish or sponsor other investment vehicles which from time to time may have potentially overlapping investment objectives with those of ours and accordingly may invest in, whether principally or secondarily, asset classes similar to those we targeted. While our Adviser generally has broad authority to make investments on behalf of the investment vehicles that it advises, our Adviser has adopted investment allocation procedures to address these potential conflicts and intends to direct investment opportunities to the Gladstone affiliate with the investment strategy that most closely fits the investment opportunity to ensure the fair and equitable treatment of all the funds it manages. Nevertheless, the management of our Adviser may face conflicts in the allocation of investment opportunities to other entities managed by our Adviser. As a result, it is possible that we may not be given the opportunity to participate in certain investments made by other members of the Gladstone Companies or investment funds managed by investment managers affiliated with our Adviser.

In certain circumstances, we may make investments in a portfolio company in which one of our affiliates has or will have an investment, subject to satisfaction of any regulatory restrictions and, where required, to the prior approval of our Board of Directors. As of March 31, 2007, our Board of Directors has approved the following types of co-investment transactions:

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

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

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

In the course of our investing activities, we will pay management and incentive fees to our Adviser and will reimburse our Administrator for certain expenses it incurs. As a result, investors in our common stock will invest on a "gross" basis and receive distributions on a "net" basis after expenses, resulting in, among other things, a lower rate of return than one might achieve through our investors themselves making direct investments. As a result of this arrangement, there may be times when the management team of our Adviser or our Administrator has interests that differ from those of our stockholders, giving rise to a conflict.

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

On October 1, 2006, we implemented the Amended Advisory Agreement with our Adviser. In addition to providing for a base management fee based on our total assets, this agreement contemplates a quarterly incentive fee based on our pre-incentive fee net investment income and an annual incentive fee based on our capital gains, if any. Our Adviser has the ability to issue a full or partial waiver of the incentive fee for current and future periods, however our Adviser is not required to issue this waiver. If our Adviser does not issue this waiver in future quarters, it could negatively impact our earnings and may compromise our ability to maintain our current level of, or increase, distributions to our stockholders, which could have a material adverse impact on our stock price.

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

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

We may experience fluctuation in our quarterly results.

We could experience fluctuations in our quarterly operating results due to a number of factors including, among others, the interest rates payable on our debt securities, variations in and the timing of the recognition of realized and unrealized gains or losses, the level of our expenses, the degree to which we encounter competition in our markets and general economic conditions. As a result of these factors, results for any period should not be relied upon as being indicative of performance in future periods.

There is a risk that you may not receive dividends or that our dividends may not grow over time.

Our current intention is to distribute at least 90% of our ordinary income and short-term capital gains to our stockholders on a quarterly basis. We expect to retain net realized long-term capital gains to supplement our equity capital and support the growth of our portfolio, although our Board of Directors may determine in certain cases to distribute these gains. We cannot assure you that we will achieve investment results or maintain a tax status that will allow or require any specified level of cash distributions or year-to-year increases in cash distributions. Provisions of our articles of incorporation and bylaws could deter takeover attempts and adversely impact the price of our shares.

Our articles of incorporation and bylaws and the Maryland General Corporation Law contain provisions that may have the effect of discouraging, delaying or making more difficult a change in control and preventing the removal of incumbent directors. The existence of these provisions may negatively impact the price of our shares and may discourage third-party bids. These provisions may reduce any premiums paid to you for our shares. Furthermore, we are subject to Section 3-602 of the Maryland General Corporation Law which governs business combinations with interested stockholders and could delay or prevent a change in control. In addition, our Board of Directors is elected in staggered terms which makes it more difficult for a hostile bidder to acquire control of us.

The market price of our shares may fluctuate significantly.

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

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

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

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

Shares of closed-end investment companies frequently trade at a discount from net asset value. This characteristic of shares of closed-end investment companies is separate and distinct from the risk that our net asset value per share will decline. Although shares of our common stock have historically traded at a premium to net asset value, there can be no guarantee that they will continue to do so.

We could face losses and potential liability if intrusion, viruses or similar disruptions to our technology jeopardize our confidential information or that of users of our technology.

Although we have implemented, and will continue to implement, security measures, our technology platform is and will continue to be vulnerable to intrusion, computer viruses or similar disruptive problems caused by transmission from unauthorized users. The misappropriation of proprietary information could expose us to a risk of loss or litigation.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

All statements contained or incorporated by reference in this prospectus or any accompanying prospectus summary, other than historical facts, may constitute "forward-looking statements". These statements may relate to, among other things, future events or our future performance or financial condition. In some cases, you can identify forward-looking statements by terminology such as "may," "might," "believe," "will," "provided," "anticipate," "future," "could," "growth," "plan," "intend," "expect," "should," "would," "if," "seek," "possible," "potential," "likely" or the 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) adverse changes in interest rates; (2) our failure or inability to establish or maintain referral arrangements with leveraged buyout funds and venture capital funds to generate loan opportunities; (3) the loss of one or more of our executive officers, in particular David Gladstone, Terry Lee Brubaker, or George Stelljes III; (4) our inability to extend, refinance, or maintain our credit facilities on terms reasonably acceptable to us, if at all, in future equity capital resources; (5) our inability to successfully securitize our loan portfolio on terms reasonably acceptable to us, if at all; (6) the decision of our competitors to aggressively seek to make senior and subordinated loans to small and medium-sized businesses on terms more favorable than we intend to provide; and (7) those factors described in the "Risk Factors" section of this prospectus. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this prospectus.

USE OF PROCEEDS

Unless otherwise specified in any prospectus supplement accompanying this prospectus, we intend to use the net proceeds from the sale of the Securities for general corporate purposes. We expect the proceeds to be used first to pay down existing short-term debt, then to make investments in small and medium sized businesses in accordance with our investment objectives, and any remaining proceeds to be used for other general corporate purposes. Indebtedness under our credit line facility currently accrues interest at the rate of approximately 6.07% and matures on May 23, 2008. We anticipate that substantially all of the net proceeds of any offering of Securities will be utilized in the manner described above within three months of the completion of such offering. Pending such utilization, we intend to invest the net proceeds of any offering of Securities primarily in cash, cash equivalents, U.S. government securities, and other high-quality debt investments that mature in one year or less from the date of investment, consistent with the requirements for continued qualification as a RIC for federal income tax purposes.

PRICE RANGE OF COMMON STOCK AND DISTRIBUTIONS

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

Our common stock is quoted on The Nasdaq Global Select Market under the symbol "GLAD." Our common stock has historically traded at prices above its net asset value. There can be no assurance, however, that any premium to net asset value will be maintained. As of June 15, 2007, we had 80 stockholders of record. The following table sets forth the range of high and low sales prices of our common stock as reported on The Nasdaq Global Select Market (for periods prior to July 1, 2006, The Nasdaq National Market) and the dividends declared by us for the last two completed fiscal years and the current fiscal year through July 3, 2007.

	Net Asset Value Per Share(1)	Closing Price High	Closing Price Low	Premium of High to Net Asset Value(2)	Premium of Low to Net Asset Value(2)	Dividends Declared
FY 2005						
First Quarter	$ 13.58	$ 25.35	$ 22.61	$ 11.77	$ 9.03	$ 0.360
Second Quarter	$ 13.64	$ 24.80	$ 20.94	$ 11.16	$ 7.30	$ 0.360
Third Quarter	$ 13.61	$ 23.96	$ 21.18	$ 10.35	$ 7.57	$ 0.390
Fourth Quarter	$ 13.41	$ 26.00	$ 22.55	$ 12.59	$ 9.14	$ 0.405
FY 2006						
First Quarter	$ 13.74	$ 23.68	$ 20.36	$ 9.94	$ 6.62	$ 0.405
Second Quarter	$ 13.84	$ 22.42	$ 19.96	$ 8.58	$ 6.12	$ 0.405
Third Quarter	$ 13.95	$ 23.50	$ 20.79	$ 9.55	$ 6.84	$ 0.405
Fourth Quarter	$ 14.02	$ 23.08	$ 21.10	$ 9.06	$ 7.08	$ 0.420
FY 2007						
First Quarter	$ 13.88	$ 25.21	$ 21.96	$ 11.33	$ 8.08	$ 0.420
Second Quarter	$ 13.82	$ 24.24	$ 21.24	$ 10.42	$ 7.42	$ 0.420
Third Quarter	*	$ 24.60	$ 21.44	*	*	$ 0.420
Fourth Quarter (through July 3, 2007)	*	$ 21.39	$ 21.24	*	*	*

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

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

* Not available.

CONSOLIDATED SELECTED FINANCIAL DATA
(in thousands, except per share data)

The following consolidated selected financial data as of and for the years ended September 30, 2006, 2005 and 2004 is derived from our audited consolidated financial statements included in this prospectus. The consolidated selected financial data as of and for the years ended September 30, 2003 and 2002 is derived from our audited consolidated financial statements that are not included in this prospectus. The consolidated selected financial data as of and for the six months ended March 31, 2007 and 2006 is derived from our unaudited consolidated financial statements included in this prospectus. You should read this data together with our consolidated financial statements and notes thereto presented elsewhere in this prospectus and the information under "Management's Discussion and Analysis of Financial Condition and Results of Operations" for more information.

	Year Ended September 30, 2006	Year Ended September 30, 2005	Year Ended September 30, 2004	Year Ended September 30, 2003	Year Ended September 30, 2002	Six Months Ended March 31, 2007	Six Months Ended March 31, 2006
						(unaudited)	(unaudited)
Total Investment Income	$ 26,899,846	$ 23,949,759	$ 20,395,968	$ 15,154,874	$ 10,455,703	$ 16,877,496	$ 13,031,019
Total Net Expenses	$ 7,549,266	$ 6,663,614	$ 7,103,193	$ 3,858,953	$ 2,839,102	$ 5,990,213	$ 3,384,789
Net Investment Income	$ 19,350,580	$ 17,286,145	$ 13,292,775	$ 11,295,921	$ 7,616,601	$ 10,887,283	$ 9,646,230
Net Increase in Net Assets Resulting from Operations	$ 24,430,235	$ 15,490,682	$ 10,570,290	$ 11,073,581	$ 7,616,601	$ 8,248,454	$ 13,823,730
Per Share Data:							
Net Increase in Net Assets Resulting from Operations:							
Basic	$ 2.15	$ 1.37	$ 1.05	$ 1.10	$ 0.76	$ 0.67	$ 1.22
Diluted	$ 2.10	$ 1.33	$ 1.02	$ 1.09	$ 0.75	$ 0.67	$ 1.20
Cash Distributions Declared per Share	$ 1.635	$ 1.515	$ 1.365	$ 1.10	$ 0.81	$ 0.84	$ 0.81
Statement of Assets and Liabilities Data:							
Total Assets	$ 225,783,215	$ 205,793,094	$ 215,333,727	$ 214,566,663	$ 172,922,039	$ 291,015,954	$ 217,725,319
Net Assets	$ 172,570,487	$ 151,610,683	$ 152,226,655	$ 130,802,382	$ 130,663,273	$ 169,323,895	$ 156,461,511
Other Data:							
Number of Portfolio Companies at Period End	32	28	16	11	7	51	28
Principal Amount of Loan Originations	$ 135,954,879	$ 143,794,006	$ 86,267,500	$ 47,011,278	$ 97,705,054	$ 127,641,175	$ 65,159,566
Principal Amount of Loan Repayments	$ 124,009,929	$ 88,019,136	$ 47,158,995	$ 18,005,827	$ 18,387,191	$ 62,230,246	$ 63,517,133
Total Return(1)	5.21%	5.93%	24.40%	21.74%	9.60%	11.50%	(0.75)%
Weighted Average Yield on Investments(2):							
With PIK Interest(3)	12.74%	12.36%	13.78%	13.86%	14.79%	n/a	12.56%
Without PIK Interest(3)	12.74%	12.23%	13.44%	13.14%	13.82%	12.58%	12.56%

(1) For the fiscal years ended September 30, 2006, 2005 and 2004, the total return equals the increase of the ending market value over the beginning market value plus monthly dividends divided by the monthly beginning market value. For the fiscal years ended September 30, 2003 and 2002, total return equals the increase of the ending market value over the beginning market value, plus distributions, dividend by the beginning market value.

(2) Weighted average yield on investments equals interest income on investments divided by the average investment balance throughout the year.

(3) Refer to Note 2 of the "Notes to Consolidated Financial Statements" for an explanation of PIK, or "Paid-in-Kind," interest.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

We were incorporated under the General Corporation Laws of the State of Maryland on May 30, 2001. Our investment objectives are to achieve a high level of current income by investing in debt securities, consisting primarily of senior notes, second lien notes, and senior subordinated notes of established private businesses that are backed by leveraged buyout funds, venture capital funds or others, with a particular emphasis on second lien and senior subordinated notes. In addition, we may acquire existing loans, which meet this profile, from leveraged buyout funds, venture capital funds and others. We also seek to provide our stockholders with long-term capital growth through the appreciation in the value of warrants, or other equity instruments that we may receive when we extend loans. We operate as a closed-end, non-diversified management investment company, and have elected to be treated as a business development company under the 1940 Act.

We seek to invest in small and medium-sized businesses that meet certain criteria, including some or all of the following: (1) the potential for growth in cash flow, (2) adequate assets for loan collateral, (3) experienced management teams with a significant ownership interest in the borrower, (4) profitable operations based on the borrower's cash flow, (5) reasonable capitalization of the borrower (usually by buyout funds or venture capital funds) and (6) the potential to realize appreciation and gain liquidity in our equity position, if any. We anticipate that liquidity in our equity position will be achieved through a merger or acquisition of the borrower, a public offering by the borrower or by exercise of our right to require the borrower to buy back its warrants. We lend to borrowers that need funds to, among other things, effect a change of control, restructure their balance sheets, or finance growth, including acquisitions.

Our loans typically range from $5 million to $15 million, although this investment size may vary proportionately as the size of our capital base changes, generally mature in no more than seven years and accrue interest at fixed or variable rates. Some of our loans may contain a provision that calls for some portion of the interest payments to be deferred and added to the principal balance so that the interest is paid, together with the principal, at maturity. This form of deferred interest is often called "paid in kind" or PIK interest, and, when earned, we record PIK interest as interest income and add the PIK interest to the principal balance of the loans. We seek to avoid PIK interest with all potential investments under review. We currently do not hold any investments with PIK and, therefore, there was no PIK accrued on our balance sheet as of March 31, 2007.

Because the majority of our portfolio loans consist of term debt of private companies who typically cannot or will not expend the resources to have their debt securities rated by a credit rating agency, we expect that most of the debt securities we acquire will be unrated. We cannot accurately predict what ratings these loans might receive if they were in fact rated, and thus cannot determine whether or not they could be considered "investment grade" quality.

To the extent possible, our loans generally are collateralized by a security interest in the borrower's assets. Interest payments are generally made monthly or quarterly (except to the extent of any PIK interest) with amortization of principal generally being deferred for several years. The principal amount of the loans and any accrued but unpaid interest generally become due at maturity at five to seven years. When we receive a warrant to purchase stock in a borrower in connection with a loan, the warrant will typically have an exercise price equal to the fair value of the portfolio company's common stock at the time of the loan and entitle us to purchase a modest percentage of the borrower's stock.

Original issue discount, or OID, arises when we extend a loan and receive an equity interest in the borrower at the same time. To the extent that the price paid for the equity is not at market value, we must allocate part of the price paid for the loan to the value of the equity. Then the amount allocated

to the equity, the OID, must be amortized over the life of the loan. As with PIK interest, the amortization of OID also produces income that must be recognized for purposes of satisfying the distribution requirements for a RIC under Subchapter M of the Internal Revenue Code, which we refer to as the Code, whereas the cash is received, if at all, when the equity instrument is sold. We seek to avoid OID and to date do not hold any investments with OID.

In addition, as a business development company under the 1940 Act, we are required to make available significant managerial assistance to our portfolio companies. We provide these services through our Adviser, who provides these services on our behalf through its officers who are also our officers. In addition, our Adviser provides other services to our portfolio companies, for which it receives fees, in connection with our investments. The fees for these services are generally paid to our Adviser in part at the time a prospective portfolio company signs a non-binding term sheet with us (as further described in the following paragraph), with the remainder paid at the closing of the investment. These fees are generally non-recurring, however in some instances they may have a recurring component which is also paid to our Adviser. Any fees received for other services, with the exception of recurring monitoring and review fees, by our Adviser are currently credited against the base management fee payable to our Adviser pursuant to the terms of the Amended Advisory Agreement, which has the effect of reducing our expenses to the extent of any such credits. The specific other services our Adviser provides vary by portfolio company, but generally include a broad array of services to the portfolio companies such as investment banking services, arranging bank financing, arranging equity financing, structuring financing from multiple lenders and investors, reviewing existing credit facilities, restructuring existing loans, raising equity and debt capital, turnaround management, merger and acquisition services and recruiting new management personnel. To date our Adviser has not charged for managerial assistance services, however, if our Adviser does receive fees for such managerial assistance, our Adviser will credit the managerial assistance fees to the base management fee due from us to our Adviser.

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

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

During the six months ended March 31, 2007, we extended, directly or through participations, approximately $127.6 million of new loans to a total of 32 companies. Also, during the six months ended March 31, 2007, one borrower repaid its loans ahead of contractual maturity, one borrower refinanced its investment and we sold or were repaid in full on 11 syndicated loans of approximately $56.9 million, and we received scheduled contractual principal repayments of approximately $5.1 million, for total principal repayments of approximately $62.0 million. During the fiscal year ended September 30, 2006, we extended, directly or through participations, approximately $136 million of new loans to a total of 22 companies. Also, during the fiscal year ended September 30, 2006, 7 borrowers

repaid their loans ahead of contractual maturity and we sold or repaid in full on 9 syndicated loans, and sold 3 loan investments at a loss for an aggregate return of capital of approximately $20 million and we received scheduled contractual principal repayments of approximately $20 million, for total principal repayments of approximately $124 million. Since our initial public offering in August 2001, we have made approximately 220 different loans to, or investments in approximately 120 companies for a total of approximately $755.5 million, before giving effect to principal repayments on investments and divestitures.

We are continuously working toward the consummation of more loan originations and syndicated investments in an effort to grow our loan portfolio. These prospective loans are subject to, among other things, the satisfactory completion of our due diligence investigation of each borrower, acceptance of terms and structure and attainment of necessary consents. With respect to each prospective loan, we will only agree to provide the loan if, among other things, the results of our due diligence investigations are satisfactory, the terms and conditions of the loan are acceptable and all necessary consents are received. Our management has initiated its due diligence investigations of the potential borrowers, however we cannot assure you that we will not discover facts in the course of completing our due diligence that would render a particular investment imprudent or that any of these loans will actually be made.

Our Investment Adviser and Administrator

Our Adviser is led by a management team which has extensive experience in our lines of business. Our Adviser is controlled by David Gladstone, our chairman and chief executive officer. Mr. Gladstone is also the chairman and chief executive officer of our Adviser. Terry Lee Brubaker, our vice chairman, chief operating officer, secretary and director, is a member of the board of directors of our Adviser and its vice chairman and chief operating officer. George Stelljes III, our president, chief investment officer and director, is a member of the board of directors of our Adviser and its president and chief investment officer. Harry Brill, our chief financial officer, is also the chief financial officer of our Adviser. Our Adviser's wholly-owned subsidiary, our Administrator, employs our chief financial officer, chief compliance officer, controller, treasurer and their respective staffs.

Our Adviser and Administrator also provide investment advisory and administrative services to our affiliates, Gladstone Commercial, a publicly traded real estate investment trust; Gladstone Investment, a publicly traded business development company; and Gladstone Land Corporation, an agricultural real estate company owned by Mr. Gladstone. All of our directors and executive officers serve as either directors or executive officers, or both, of Gladstone Commercial and Gladstone Investment. In the future, our Adviser may provide investment advisory and administrative services to other funds, both public and private, of which it is the sponsor.

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

Investment Advisory and Management Agreements

On December 2, 2005, our stockholders approved a proposal to enter into an amended and restated investment advisory agreement, which we refer to as the Amended Advisory Agreement, with our Adviser and an administration agreement which we refer to as the Administration Agreement, with our Administrator, both of which became effective on October 1, 2006. The Amended Advisory Agreement replaced the original advisory agreement which terminated on September 30, 2006 and we

refer to as the Initial Advisory Agreement. We continue to pay our direct expenses including, but not limited to, directors fees, legal and accounting fees, and stockholder related expenses under the Amended Advisory Agreement.

Pursuant to the Initial Advisory Agreement, we paid our Adviser an annual advisory fee of 1.25% of our total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.3125%, and an annual administrative fee of 0.75% of our total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.1875%, for a total annual base management fee of 2%. This fee was then directly reduced by the amount of loan servicing fees paid to our Adviser and any other fees received by our Adviser from our borrowers and potential borrowers.

Under the Amended Advisory Agreement, we pay our Adviser an annual base management fee of 2% of our average gross assets, which is defined as total assets less cash and cash equivalents pledged to creditors calculated as of the end of the two most recently completed fiscal quarters and also consists of a two-part incentive fee.

The first part of the incentive fee is an income-based incentive fee which rewards our Adviser if our quarterly net investment income (before giving effect to any incentive fee) exceeds 1.75% of our net assets (the "hurdle rate"). We will pay our Adviser an income 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% 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).

Quarterly Incentive Fee Based on Net Investment Income

Pre-incentive fee net investment income
(expressed as a percentage of the value of net assets)

Percentage of pre-incentive fee net investment income
allocated to income-related portion of incentive fee

The second part of the incentive fee is a capital gains incentive fee that will be determined and payable in arrears as of the end of each fiscal year (or upon termination of the Amended Advisory Agreement, as of the termination date), commencing on October 1, 2006, and will equal 20% of our realized capital gains as of the end of the fiscal year. In determining the capital gains incentive fee payable to our Adviser, we will calculate the cumulative aggregate realized capital gains and cumulative aggregate realized capital losses since our inception, and the aggregate unrealized capital depreciation as of the date of the calculation, as applicable, with respect to each of the investments in our portfolio. A discussion regarding the basis for our Board of Directors' approval of the Amended Advisory

Agreement is available in our Annual Report on Form 10-K for the fiscal year ended September 30, 2006.

Our Adviser's board of directors agreed to voluntarily waive 1.5% of the annual 2.0% base management fee to 0.5% for senior syndicated loans for each of the three months ended December 31, 2006 and March 31, 2007.

In addition to the base management and incentive fees under the Amended Advisory Agreement, certain fees received by our Adviser from our portfolio companies were credited against the investment advisory fee under the Initial Advisory Agreement, and will continue to be paid to our Adviser and credited under the Amended Advisory Agreement. Our Adviser services our loan portfolio pursuant to a loan servicing agreement with Gladstone Business Loan, LLC, which we refer to as Business Loan, in return for a 1.5% annual fee, based on the monthly aggregate outstanding loan balance of the loans pledged under our credit facility. Effective in April 2006, our Adviser's board of directors voted to reduce the portion of the annual fee to 0.5% for senior syndicated loans. This fee directly reduces the amount of the fees payable under both the Initial and Amended Advisory Agreements. For the three months ended March 31, 2007 and 2006, we incurred $760,623 and $734,644, respectively, and for the six months ended March 31, 2007 and 2006 we incurred $1,479,775 and $1,450,059, respectively, in loan servicing fees.

For the three months ended March 31, 2007, the gross base management fee, based on the Amended Advisory Agreement, before reductions for loan servicing and other fees was $1,211,108, as compared to $1,087,023 for the three months ended March 31, 2006. After being reduced by loan servicing fees of $760,623 and other fees received by our Adviser of $775,000, our net base management fee was a credit of $324,516 for the three months ended March 31, 2007, as compared to reductions for loan servicing fees of $734,644 and other fees received by our Adviser of $673,000, our net base management fee was a credit of $320,621 for the three months ended March 31, 2006. For the six months ended March 31, 2007, the gross base management fee, based on the Amended Advisory Agreement, before reductions for loan servicing fees and other fees was $2,328,692. After being reduced by loan servicing fees of $1,479,775 and other fees received by our Adviser of $1,086,000, our net base management fee for the six months ended March 31, 2007 was a credit of $237,084. For the six months ended March 31, 2006, the gross base management fee, before reductions for loan servicing fees and other fees was $2,071,139. After being reduced by loan servicing fees of $1,450,059 and other fees received by our Adviser of $1,223,000, our net base management fee for the six months ended March 31, 2006 was a credit of $601,920. At March 31, 2007, $217,631 of unpaid loan servicing fees and $324,516 of base management fee due to us was recorded net in fees due from Adviser in the accompanying consolidated statement of assets and liabilities.

For the three and six months ended March 31, 2007, we recorded a gross incentive fee of $1,158,995 and $2,307,478, respectively, which was offset by a waiver voluntarily issued by our Adviser's board of directors of $1,088,378 and $1,657,372, respectively, which resulted in a net incentive fee due to our Adviser of $70,617 and $650,106, respectively, of which $70,617 is unpaid and is netted and recorded in fees due from Adviser on our consolidated statements of assets and liabilities. There was no incentive fee recorded for the three and six months ended March 31, 2006 as the Amended Advisory Agreement was not in effect.

Administration Agreement

Under the Administration Agreement, we pay separately for administrative services. The Administration Agreement provides for payments equal to our allocable portion of our Administrator's overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent for employees of our Administrator, and our allocable portion of the salaries and benefits expenses of our chief financial officer, controller, chief compliance officer, treasurer and their

respective staffs. Our allocable portion of expenses is derived by multiplying our Administrator's total allocable expenses by the percentage of our average total assets (the total assets at the beginning and end of each quarter) in comparison to the average total assets of all companies managed by our Adviser under similar agreements.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States, which we refer to as GAAP, requires management to make estimates and assumptions that affect the reported consolidated amounts of assets and liabilities, and 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. Our accounting policies are more fully described in the "Notes to Consolidated Financial Statements" contained elsewhere in the registration statement of which this prospectus is a part. 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 investments and the related amounts of unrealized appreciation and depreciation of investments recorded.

General Valuation Policy: Using procedures established by our Board of Directors, we value our investment portfolio each quarter. We carry our investments at fair value, as determined in good faith by or under the direction of our Board of Directors. Securities that are publicly traded, if any, are valued at the closing price of the exchange or securities market on which they are listed on the valuation date. Securities that are not traded on a public exchange or securities market, but for which a limited market exists and that have been rated by a nationally recognized statistical rating organizations, or NRSRO, (such as certain participations in syndicated loans) are valued at the indicative bid price offered by the syndication agent on the valuation date.

Debt and equity securities that are not publicly traded, for which a limited market does not exist, or for which a limited market exists but that have not been rated by a NRSRO (or for which we have various degrees of trading restrictions) are valued at fair value as determined in good faith by or under the direction of our Board of Directors. In making the good faith determination of the value of these securities, we start with the cost basis of the security, which includes the amortized OID and PIK interest, if any. We then apply the methods set out below in "Valuation Methods." Members of our Adviser's portfolio management team prepare the valuations of our investments in portfolio companies using the most recent portfolio company financial statements and forecasts. These individuals also consult with portfolio company senior management and ownership to obtain further updates on the portfolio company's performance, including information such as industry trends, new product development, and other operational issues. Due to the uncertainty inherent in the valuation process, such estimates of fair value may differ significantly from the values that would have been obtained had a ready market for the securities existed, and the differences could be material. Additionally, changes in the market environment and other events that may occur over the life of the investments may cause the gains or losses ultimately realized on these investments to be different than the valuations currently assigned. There is no single standard for determining fair value in good faith, as fair value depends upon circumstances of each individual case. In general, fair value is the amount that we might reasonably expect to receive upon the current sale of the security.

At March 31, 2007, we engaged Standard & Poor's Securities Evaluations, Inc., or SPSE, to submit opinions of value for most of our loan securities. We request that SPSE also evaluate and assign values to success fees (conditional interest included in some loan securities) when we determine that the

probability of receiving a success fee on a given loan is above 6-8%, a threshold of significance. Upon completing our collection of data with respect to the investments (including the information described under "Credit Information," the risk ratings of the loans described under "Loan Grading and Risk Rating" and the factors described under "Valuation Methods"), this valuation data is forwarded along to SPSE for review and analysis. SPSE makes its independent assessment of the data that we have assembled and assesses its independent data to form an opinion as to what they consider to be the market values for the securities. With regard to its work, SPSE has issued the following paragraph:

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

SPSE opinions of value are submitted to our Board of Directors along with our Adviser's supplemental assessment and recommendation regarding valuation of each of these investments. Our Adviser generally accepts the opinion of value given by SPSE, however, in certain limited circumstances, such as when our Adviser may learn new information regarding an investment between the time of submission to SPSE and the date of the Board assessment, our Adviser's conclusions as to value may differ from the opinion of value delivered by SPSE. Our Board of Directors then reviews whether our Adviser has followed its established procedures for determinations of fair value, and votes whether to accept the recommended valuation of our investment portfolio. Our Adviser and our management recommended, and the Board of Directors elected to accept, the opinions of value delivered by SPSE on the loans in our portfolio as denoted on the schedule of investments as of March 31, 2007, September 30, 2006 and September 30, 2005, included in our consolidated financial statements.

Because there is a delay between when we close an investment and when the investment can be evaluated by SPSE, new loans are not valued immediately by SPSE; rather, management makes its own determination about the value of these investments in accordance with our valuation policy. Because SPSE does not provide values for equity securities, our Adviser determines the fair value of these investments using valuation policies approved by our Board of Directors.

Credit Information: Our Adviser monitors a wide variety of key credit statistics that provide information regarding our portfolio companies to help us assess credit quality and portfolio performance. If we held a controlled or affiliate investment, we and our Adviser would participate in periodic board meetings of such portfolio companies and also require them to provide annual audited and monthly unaudited financial statements. Using these statements and board discussions, our Adviser would calculate and evaluate the credit statistics.

Loan Grading and Risk Rating: As part of our valuation procedures we risk rate all of our investments in debt securities. For syndicated loans that have been rated by a NRSRO (as defined in Rule 2a-7 under the 1940 Act), we use the NRSRO's risk rating for such security. For all other debt securities, we use a proprietary risk rating system. Our risk rating system uses a scale of 0 to 10, with 10 being the lowest probability of default. This system is used to estimate the probability of default on debt securities and the probability of loss if there is a default. These types of systems are referred to as risk rating systems and are used by banks and rating agencies. The risk rating system covers both qualitative and quantitative aspects of the business and the securities we hold.

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

Company's System	First NRSRO	Second NRSRO	Gladstone Capital's Description(a)
>10	Baa2	BBB	Probability of Default (PD during the next ten years is 4% and the Expected Loss (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 here are for a ten year term debt security. If the company's debt security is less than ten years then the probability of default is adjusted to a lower percentage for the shorter period which may move the security higher on our risk rating scale.

The above scale gives an indication of the probability of default and the magnitude of the loss if there is a default. Our policy is to stop accruing interest on an investment if we determine that interest is no longer collectible. Currently, none of our investments are on non-accrual. At March 31, 2007, no payments were past due on any of our debt securities. Additionally, we do not risk rate our equity securities.

The following table lists the risk ratings for all non-syndicated loans in our portfolio at March 31, 2007, September 30, 2006 and September 30, 2005, representing approximately 64%, 73% and 62%, respectively, of all loans in our portfolio:

Rating	Mar. 31, 2007	Sept. 30, 2006	Sept. 30, 2005
Average	**7.1**	**7.2**	**7.6**
Weighted Average	**7.0**	**7.2**	**7.6**
Highest	**10.0**	**9.0**	**9.0**
Lowest	**5.0**	**6.0**	**6.0**

The following table lists the risk ratings for syndicated loans in our portfolio that are not currently rated by an NRSRO at March 31, 2007, September 30, 2006 and September 30, 2005, representing approximately 14%, 17% and 32%, respectively, of all loans in our portfolio:

Rating	Mar. 31, 2007	Sept. 30, 2006	Sept. 30, 2005
Average	**6.2**	**6.1**	**6.2**
Weighted Average	**6.1**	**6.3**	**6.3**
Highest	**9.0**	**8.0**	**7.0**
Lowest	**4.0**	**4.0**	**5.0**

For syndicated loans that are currently rated by an NRSRO, we risk rate such loans in accordance with the risk rating systems of major risk rating organizations such as those provided by a NRSRO. The following table lists the risk ratings for all syndicated loans in our portfolio that are currently rated by an NRSRO at March 31, 2007, September 30, 2006 and September 30, 2005, representing approximately 22%, 10% and 6%, respectively, of all loans in our portfolio:

Rating	Mar. 31, 2007	Sept. 30, 2006	Sept. 30, 2005
Average	**B-/B3**	**CCC+/Caa1**	**CCC+/Caa1**
Weighted Average	**CCC+/Caa1**	**CCC+/Caa1**	**CCC/Caa2**
Highest	**BB-/Ba2**	**B-/B3**	**CCC+/B3**
Lowest	**CCC/Caa3**	**CCC/Caa1**	**CCC+/Caa2**

Valuation Methods: We determine the value of publicly-traded debt securities based on the closing price for the security on the exchange or securities market on which it is listed on the valuation date. We value debt securities that are not publicly traded, but for which a limited market for the security exists, such as participations in syndicated loans, at the indicative bid price offered by the syndication agent on the valuation date. At March 31, 2007, none of the debt securities in our portfolio were publicly traded and there was a limited market for 31 debt securities in our portfolio. At September 30, 2006, none of the debt securities in our portfolio were publicly traded and there was a limited market for 9 debt securities in our portfolio. At September 30, 2005, none of the debt securities in our portfolio were publicly traded and there was a limited market for 12 debt securities in our portfolio.

For debt securities that are not publicly traded, for which there is no market, or for which there is a market but have not been rated by a NRSRO, we begin with the risk rating designation of the security as described above. Using this risk rating designation, we seek to determine the value of the security as if we currently intended to sell the security and consider some or all of the following factors:

- the cost basis and the type of the security;
- the nature and realizable value of the collateral;
- the portfolio company's ability to make payments and discounted cash flow;
- reports from portfolio company senior management and board meetings;

reported values of similar securities of the portfolio company or comparable companies; and

changes in the economy affecting the portfolio company.

We value convertible debt, equity, success fees or other equity-like securities for which there is a market based on the market prices for such securities, even if that market is not robust. At March 31, 2007, September 30, 2006 and September 30, 2005, there was no market for any of the equity securities we owned. To value equity securities for which no market exists, we use the same information we would use for a debt security valuation described above, except risk-rating, as well as standard valuation techniques used by major valuation firms to value the equity securities of private companies. These valuation techniques consist of discounted cash flow of the expected sale price in the future, valuation of the securities based on recent sales in comparable transactions, and a review of similar companies that are publicly traded and the market multiple of their equity securities. At March 31, 2007, September 30, 2006 and September 30, 2005, we had $146,124, $37,000 and $37,000, respectively, invested, at cost, in equity securities compared to our debt portfolio with a cost basis of $281,379,326, $216,165,986 and $205,338,554, respectively.

At March 31, 2007, we had total unrealized depreciation of $3,037,674, which was mainly comprised of unrealized deprecation of $1,250,000 on our senior subordinated term debt investment in Visual Edge Technology, Inc., unrealized depreciation of $733,000, on the aggregate of our investments in LocalTel, Inc. and unrealized depreciation of $482,488 on our senior subordinated term debt investment in Consolidated Bedding, Inc. Unrealized appreciation of $1,754,910 was primarily composed of unrealized appreciation of $789,061 on our warrants in Finn Corporation, a $180,800 success fee value on our senior term debt investment in Allied Extruders, Inc. and a $94,219 success fee value on our senior term debt investment in SCPH Holdings, Inc. In the aggregate, we recorded net unrealized depreciation of $1,282,764 on our total investment portfolio as of March 31, 2007.

At September 30, 2006, we had total unrealized appreciation of $2,015,198, which was mainly comprised of unrealized appreciation of $672,431 on our warrants of Finn Corporation, unrealized appreciation of $607,625 on our senior term debt in Mistras Holding Corporation and unrealized appreciation of $148,287 on our senior subordinated term debt investment in Xspedius Communications, LLC. This unrealized appreciation was offset by unrealized depreciation of $575,434, most notably composed of unrealized depreciation of $131,367 on our senior subordinated term debt investment in Consolidated Bedding, Inc. and unrealized depreciation of $115,750 on our senior term debt in LocalTel Inc. In the aggregate, we recorded net unrealized appreciation of $1,439,764 on our total investment portfolio as of September 30, 2006.

At September 30, 2005, we had total unrealized depreciation of $6,231,296, which was mainly composed of unrealized depreciation in our senior subordinated term debt investment in Finn Corporation (excluding the warrants) of $3,150,000, our senior subordinated term debt investment in Xspedius Communications of $1,493,182, and our senior term debt in ARI Holdings, Inc. of $1,053,939 (which was subsequently sold at the September 30, 2005 reflected fair value), partially offset by unrealized appreciation, most notably on, the value of our warrants of Finn Corporation, which had an unrealized appreciation of $645,114 and our senior term debt investment in Woven Electronics Corporation, which had unrealized appreciation of $431,436. This aforementioned unrealized appreciation plus unrealized appreciation of $625,955 on certain other investments, primarily in our originated loan investments and certain syndicate participations, most notably Infor Global Solutions Ltd., which had unrealized appreciation of $248,750, which resulted in overall net unrealized depreciation of $4,528,791 as of September 30, 2005.

Tax Status

Federal Income Taxes

We currently qualify and 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 are required to distribute to stockholders at least 90% of investment company taxable income, as defined by the Code. We have a policy to pay out as a dividend up to 100% of that amount. In an effort to avoid certain excise taxes imposed on RICs, we currently intend to distribute during each calendar year, an amount at least equal the sum of (1) 98% of our ordinary income for the calendar year, (2) 98% of our capital gains in excess of capital losses for the one-year period ending on October 31 of the calendar year and (3) any ordinary income and net capital gains for preceding years that were not distributed during such years.

Revenue Recognition

Interest Income Recognition

Interest income is recorded on the accrual basis to the extent that such amounts are expected to be collected. We will stop accruing interest on investments and write off any previously accrued and uncollected interest when it is determined that interest is no longer collectible. Conditional interest or a success fee is recorded when earned upon full repayment of a loan investment.

Paid in Kind Interest

In the future, we may hold loans in our portfolio which contain a PIK interest provision. The PIK interest, computed at the contractual rate specified in each loan agreement, is added to the principal balance of the loan and recorded as interest income. To maintain our status as a RIC, this non-cash source of income must be paid out to stockholders in the form of dividends, even though we have not yet collected the cash.

RESULTS OF OPERATIONS

Comparison of the Six Months Ended March 31, 2007 to the Six Months Ended March 31, 2006

Investment Income

Investment income for the six months ended March 31, 2007 was $16,877,496, as compared to $13,031,019 for the six months ended March 31, 2006. Interest income from our investment portfolio increased from March 31, 2006 due to the increase in new loans of $127,641,175, offset by principal repayments and investment sales of approximately $62,230,246.

Interest income from our investments in debt securities of private companies was $16,153,059 for the six months ended March 31, 2007 as compared with $12,722,371 for the six months ended March 31, 2006, which included approximately $63,000 of PIK interest. This increase consisted of net new investments of approximately $65.4 million for the six months ended March 31, 2007, as compared to net new investments of approximately $1.6 million for the six months ended March 31, 2006. As a result of a refinancing by Badanco Acquisition Corp. and a full repayment by Mistras Holdings Corp., we recorded success fees of approximately $1,733,000 during the six months ended March 31, 2007.

The annualized weighted average yield on our portfolio for the six months ended March 31, 2007 was 12.6%; there was no PIK interest accrued during the six months ended March 31, 2007. The annualized weighted average yield on our portfolio for the six months ended March 31, 2006 was 12.6% (with and without giving effect to PIK interest).

Interest income from invested cash and cash equivalents for the six months ended March 31, 2007 was $68,914, as compared to $13,536 for the six months ended March 31, 2006 due to an increase in cash held in the custodial account which is interest bearing.

For the six months ended March 31, 2007 and March 31, 2006, we recorded $271,122 and $214,126, respectively, in interest income from loans to our employees in connection with the exercise of employee stock options. The increase is the result of additional loans issued in connection with employee stock option exercises during the fourth quarter of the previous fiscal year.

For the six months ended March 31, 2007, we recorded $384,401 of prepayment fees and other income, as compared to $80,986 for the six months ended March 31, 2006. The income for both periods consisted of prepayment penalty fees received upon the full repayment of certain loan investments ahead of contractual maturity and prepayment fees received upon the early unscheduled principal repayments which, in both instances, were based on a percentage of the outstanding principal amount of the loan at the date of prepayment.

Operating Expenses

Operating expenses, prior to credits from our Adviser, for the six months ended March 31, 2007 were $8,733,585, as compared to $4,557,552 for the six months ended March 31, 2006. Operating expenses for the six months ended March 31, 2007 reflected a significant increase in interest expense and management fees, prior to credits, as well as the addition of the incentive and administration fees, prior to credits, under the Amended Advisory and Administration Agreements.

Loan servicing fees of $1,479,775 were incurred for the six months ended March 31, 2007, as compared to $1,450,059 for the six months ended March 31, 2006. These fees were incurred in connection with a loan servicing agreement between Business Loan and our Adviser, which is based on the size of the portfolio. These fees were reduced against the amount of the base management fee due to our Adviser.

For the six months ended March 31, 2007, we incurred a gross base management fee of $848,916, less credits for fees received by our Adviser of $1,086,000, for a net base management fee credit of $237,084, as compared to the six months ended March 31, 2006, in which we incurred a gross base management fee of $621,080, less credits for fees received by our Adviser of $1,223,000, for a net base management credit of $601,920. The base management fee is computed quarterly as described under "Investment Advisory and Management Agreement." The fees increased in the current period due to the growth of the investment portfolio as compared to the same period of the prior year and fewer credits for fees received by our Adviser which reduce the base management fee.

Effective October 1, 2006, the income based incentive fee became effective and as such we recorded a gross incentive fee of $2,307,478, which was reduced by a voluntary waiver issued by our Adviser's board of directors of $1,657,372, which resulted in a net incentive fee of $650,106, which is recorded in fees due to Adviser on our consolidated statements of assets and liabilities. There was no incentive fee recorded for the six months ended March 31, 2006, as the Amended Advisory Agreement was not in effect.

Effective October 1, 2006, the Administration Agreement became effective in which we provide payments equal to our allocable portion of our Administrator's overhead expenses in performing its obligations under the Administration Agreement including, but not limited to, rent for employees of our Administrator, and our allocable portion of the salaries and benefits expenses of our chief financial officer, chief compliance officer and controller and their respective staffs. We incurred an administration fee of $294,851 for the six months ended March 31, 2007. There was no administration fee recorded during the six months ended March 31, 2006, as the Administration Agreement was not in effect.

Professional fees, consisting primarily of legal and audit fees, for the six months ended March 31, 2007 were $220,001, as compared to $233,353 for the six months ended March 31, 2006. The slight decrease is due to the reimbursement of certain legal fees at the time of investment funding.

Amortization of deferred financing costs, in connection with our line of credit, was $126,500 for the six months ended March 31, 2007 and $58,536 for the six months ended March 31, 2006. The increase is due to the amortization of additional fees incurred with our line of credit which were not in place during the prior year period.

Interest expense for the six months ended March 31, 2007 was $2,931,276, as compared to $1,600,244 for the six months ended March 31, 2006. This increase is primarily a result of increased borrowings under our line of credit during the six months ended March 31, 2007, which borrowings were partially used to finance our increased investments, borrowings remaining outstanding for longer periods of time and an increase in the interest rates on our borrowings.

Stockholder related costs for the six months ended March 31, 2007 were $151,016, as compared to $244,799 for the six months ended March 31, 2006. Stockholder related costs include such recurring items as transfer agent fees, NASDAQ listing fees, SEC filing fees and annual report printing fees. These fees decreased during the six months ended March 31, 2007 since there was no special proxy solicitation filed as there was during the six months ended March 31, 2006.

Directors' fees for the six months ended March 31, 2007 were $111,220, as compared to $54,212 for the six months ended March 31, 2006 due to the increase in annual stipend fees and their related monthly amortization.

Insurance expense for the six months ended March 31, 2007 was $125,092, as compared to $101,367 for the six months ended March 31, 2006. The increase is primarily the result of an increase in the amortization of our directors and officers insurance policy premiums.

There was no stock option compensation expense recorded for the six months ended March 31, 2007 as there was no longer a stock option plan in effect. Stock option compensation expense for the six months ended March 31, 2006 was $77,322 and was the result of the adoption of the SFAS No. 123 (revised 2004) "*Share-based Payment*."

Other expenses were $137,460 for the six months ended March 31, 2007, as compared to $116,580 for the six months ended March 31, 2006. The expenses primarily represent direct expenses such as travel related specifically to our portfolio companies, loan evaluation services for our portfolio companies, press releases and backup servicer expenses.

Income Tax Expense

During the six months ended March 31, 2006, we recorded approximately $50,000 in connection with penalties incurred on misclassified revenue on its fiscal year 2004 corporate tax return.

Net Realized Gain (Loss) on Sale of Investments

During the six months ended March 31, 2007, we sold or were repaid in full on eleven syndicate loan investments for a net gain of $86,519, as compared to an aggregate net loss of $803,095, which was composed of $1,180,595 loss from the sale of two investments and a gain of $377,500 from the sale of a syndicate investment during the six months ended March 31, 2006.

Realized Gain on Settlement of Derivative

During the six months ended March 31, 2007, we received interest rate cap agreement payments of $22,793 as a result of the one month LIBOR, the Prime Rate or the Federal Funds Rate, exceeding

5%. There was no realization during the six months ended March 31, 2006 as the one month LIBOR was below 5%.

Net Unrealized (Depreciation) Appreciation on Derivative

During the six months ended March 31, 2007, we recorded net unrealized depreciation of $25,613 due to a decrease in the fair market value of our interest rate cap agreement, as compared to unrealized appreciation of $23,766 during the six months ended March 31, 2006.

Net Unrealized (Depreciation) Appreciation on Investments

For the six months ended March 31, 2007, we recorded net unrealized depreciation on investments of $2,722,528, as compared to net unrealized appreciation of $4,956,829, for the six months ended March 31, 2006. The unrealized depreciation is mainly attributable to the depreciated fair value on certain investments.

Net Increase in Net Assets from Operations

Overall, we realized a net increase in net assets resulting from operations of $8,248,454 for the six months ended March 31, 2007. Based on a weighted-average of 12,272,012 basic and diluted shares outstanding, our net increase in net assets from operations per weighted-average common share for the six months ended March 31, 2007 was $0.67, basic and diluted.

For the six months ended March 31, 2006, we realized a net increase in net assets resulting from operations of $13,823,730. Based on a weighted-average of 11,307,510 (basic) and 11,555,479 (diluted) shares outstanding, our net increase in net assets from operations per weighted-average common share for the six months ended March 31, 2006 was $1.22 (basic) and $1.20 (diluted).

Comparison of the Fiscal Years Ended September 30, 2006 and September 30, 2005

Investment Income

Investment income for the fiscal year ended September 30, 2006 was approximately $26.9 million as compared to approximately $23.9 million for the fiscal year ended September 30, 2005. This increase is primarily a result of a rise in interest income from an increase of approximately $136.0 million of new investments from the prior year and the collection of approximately $1.3 million of exit fees upon the full repayment of two portfolio company investments.

Interest income from our investments in debt securities of private companies was approximately $25.6 million, including $63,000 of PIK interest, for the fiscal year ended September 30, 2006 as compared to $22.4 million for the fiscal year ended September 30, 2005, including $394,000 of PIK interest. This increase was primarily the result of approximately $136.0 million of new investments for the fiscal year ended September 30, 2006 and the collection of approximately $1.3 million of exit fees upon the full repayment of two portfolio company investments. The decrease in PIK income for the fiscal year ended September 30, 2006 was the result of the early repayment in full of one loan containing a PIK provision.

The weighted average yield on our portfolio for the fiscal year ended September 30, 2006 was 12.74% (with and without giving effect to PIK interest). The weighted average yield on our portfolio for the fiscal year ended September 30, 2005 was 12.23% (without giving effect to PIK interest) and 12.36% (after giving effect to PIK interest). The yields were computed based on the cost value of the investment portfolios.

Interest income from invested cash and cash equivalents for the fiscal year ended September 30, 2006 was approximately $38,000, as compared to approximately $33,000 for the fiscal year ended

September 30, 2005. This increase was primarily caused by an increase in cash balances during the year resulting from sales and principal repayments of portfolio investments of approximately $124 million for the fiscal year ended September 30, 2006.

Prepayment fees and other income was approximately $0.8 million for the fiscal year ended September 30, 2006 and $1.1 million for the fiscal year ended September 30, 2005. For the fiscal year ended September 30, 2006, this consisted of approximately $0.8 million of prepayment penalty fees. For the fiscal year ended September 30, 2005, this consisted of approximately $1.0 million of prepayment penalty fees and approximately $24,000 of waiver fees for certain loan covenants.

Operating Expenses

Operating expenses for the fiscal year ended September 30, 2006 were approximately $9.5 million, as compared to approximately $7.5 million for the fiscal year ended September 30, 2005. This increase was mainly a result of an increase in loan servicing fees, interest expense, stockholder related costs and other expenses, offset by reductions in professional fees and amortization of deferred financing fees.

Loan servicing fees of approximately $2.9 million were incurred for the fiscal year ended September 30, 2006 as compared to approximately $2.5 million for the fiscal year ended September 30, 2006. These fees were incurred in connection with a loan servicing agreement between Business Loan and our Adviser, which is based on the size of the aggregate outstanding loan portfolio. These fees were directly credited against the amount of the management fee due to our Adviser.

Effective October 1, 2004, we entered into an advisory agreement with our Adviser whereby our Adviser serves as our external adviser. As compensation for the services of our Adviser, we pay our Adviser an annual advisory fee of 1.25% of total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.3125%, and an annual administrative fee of 0.75% of total assets (as reduced by cash and cash equivalents pledged to creditors), payable in quarterly computed increments of 0.1875%, for a total fee of 2% of total assets (as reduced by cash and cash equivalents pledged to creditors). Effective in April 2006, our Adviser's board of directors voluntarily waived the advisory fee on a temporary basis by reducing the 1.25% annual fee to 0.5% per annum applicable only to the senior syndicated loans in which we already have a second lien position. We continue to pay direct expenses including, but not limited to, directors' fees, legal and accounting fees, stockholder related expenses, and directors and officers insurance. Under the advisory agreement, our Adviser provides the managerial assistance and other services to our portfolio companies and likewise our Adviser directly receives any fees for such services. Any such fees are credited directly against the 2% management fee payable to our Adviser. The 2% management fee is also directly reduced by the amount of the monthly loan servicing fees we pay to our Adviser. Overall, the management fee due to our Adviser cannot exceed 2% of total assets (as reduced by cash and cash equivalents pledged to creditors) during any given fiscal year. On October 1, 2006, we entered into the Amended Advisory Agreement with our Adviser and the Administration Agreement with our Administrator.

The following table sets forth the quarterly computations of the management fee for the fiscal years ended September 30, 2006 and September 30, 2005, based on the quarterly increment of 0.50% (0.3125% quarterly advisory fee plus 0.1875% quarterly administrative fee) and the reduced fee for senior syndicated loans of 0.125% per quarter:

	September 30, 2006	June 30, 2006	March 31, 2006	December 31, 2005
Fee:				
Total assets at	$ 223,979,932(a)	$ 207,265,095	$ 217,404,695	$ 211,823,244
Less: Senior syndicated loans subject to reduced fee	(11,011,616)(b)	(3,018,897)(b)		
Less: Borrowings under line of credit at				(15,000,000)(c)
Total assets subject to quarterly fee of 0.50% as of	212,968,316	204,246,198	217,404,695	196,823,244
Quarterly fee rate	0.50%	0.50%	0.50%	0.50%
Management fee before senior syndicated loan advisory fee	1,064,841	1,021,231	1,087,023	984,116
Total senior syndicated loan advisory fee at quarterly rate 0.125%	13,765(d)	3,774(d)		
Gross management fee before loan servicing fee credit	1,078,606	1,025,005	1,087,023	984,116
Less: loan servicing fee from Business Loan	763,851	693,965	734,644	715,415
Management fee before credit	314,755	331,040	352,379	268,701
Direct Credit to Management Fee:				
Fee revenue recorded by our Adviser	289,000	539,000	673,000	550,000
Net management fee for the three months ended(e)	$ 25,755	$ (207,960)	$ (320,621)	$ (281,299)

	September 30, 2005	June 30, 2005	March 31, 2005	December 31, 2004
Fee:				
Total assets	$ 205,793,094	$ 209,320,463	$ 213,753,998	$ 194,085,591
Less: Borrowings under line of credit			(18,644,179)(f)	(22,435,000)(f)
Total assets subject to quarterly fee of 0.50% as of	205,793,094	209,320,463	195,109,819	171,650,591
Quarterly fee rate	0.50%	0.50%	0.50%	0.50%
Gross management fee before loan servicing fee credit	1,028,965	1,046,602	975,549	858,254
Less: loan servicing fee from Business Loan	745,263	687,971	585,542	530,952
Management fee before credit	283,702	358,631	390,007	327,302
Direct Credit to Management Fee:				
Fee revenue recorded by our Adviser	100,000	240,600	450,000	286,500

	September 30, 2005	June 30, 2005	March 31, 2005	December 31, 2004
Net management fee for the three months ended	$ 183,702	$ 118,031	$ (59,993)	$ 40,802