PROSPECT CAPITAL CORP
Form 10-Q
February 09, 2011

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the Quarter Ended December 31, 2010

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

Commission File Number: 814-00659

PROSPECT CAPITAL CORPORATION
(Exact name of registrant as specified in its charter)

Maryland	**43-2048643**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
10 East 40th Street **44th Floor** **New York, New York**	**10016**
(Address of principal executive offices)	**(Zip Code)**

(212) 448-0702
(Registrant s telephone number, including area code)

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

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

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

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

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

The number of shares of the registrant s common stock, $0.001 par value, outstanding as of February 9, 2011 was 88,199,537.

PROSPECT CAPITAL CORPORATION
FORM 10-Q FOR THE QUARTER ENDED DECEMBER 31, 2010
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PART I: FINANCIAL INFORMATION
Item 1. Financial Statements

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF ASSETS AND LIABILITIES
December 31, 2010 and June 30, 2010
(in thousands, except share and per share data)

	December 31, 2010 (Unaudited)	June 30, 2010 (Audited)
Assets (Note 5)		
Investments at fair value:		
Control investments (cost of $235,729 and $185,720, respectively)	$ 264,228	$ 195,958
Affiliate investments (cost of $65,815 and $65,082, respectively)	74,709	73,740
Non-control/Non-affiliate investments (cost of $584,524 and $477,957, respectively)	579,284	478,785
Total investments at fair value (cost of $886,068 and $728,759, respectively, Note 4)	918,221	748,483
Investments in money market funds	132,194	68,871
Cash	4,019	1,081
Receivables for:		
Interest, net	8,420	5,356
Dividends	2	1
Other	350	419
Prepaid expenses	250	371
Deferred financing costs, net	12,105	7,579
Other assets	534	534
Total Assets	1,076,095	832,695
Liabilities		
Credit facility payable (Note 5)		100,300
Senior Convertible Notes (Note 6)	150,000	
Dividends payable	8,900	6,909
Due to Prospect Administration (Note 10)	317	294
Due to Prospect Capital Management (Note 10)	9,787	9,006
Accrued expenses	2,639	4,057
Other liabilities	1,262	705
Total Liabilities	172,905	121,271
Net Assets	$ 903,190	$ 711,424

Components of Net Assets				
Common stock, par value $0.001 per share (200,000,000 and 100,000,000 common shares authorized, respectively; 88,115,382 and 69,086,862 issued and outstanding, respectively) (Note 7)	$	88	$	69
Paid-in capital in excess of par (Note 7)		988,897		805,918
Distributions in excess of net investment income		(18,369)		(9,692)
Accumulated realized losses on investments		(99,579)		(104,595)
Unrealized appreciation on investments		32,153		19,724
Net Assets	$	903,190	$	711,424
Net Asset Value Per Share	$	10.25	$	10.30

See notes to consolidated financial statements.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
For The Three and Six Months Ended December 31, 2010 and 2009
(in thousands, except share and per share data)
(Unaudited)

	For The Three Months Ended December 31, 2010	For The Three Months Ended December 31, 2009	For The Six Months Ended December 31, 2010	For The Six Months Ended December 31, 2009
Investment Income				
Interest Income: (Note 4)				
Control investments (Net of foreign withholding tax of $0, ($52), $0, and ($19), respectively)	$ 5,428	$ 5,052	$ 10,617	$ 9,643
Affiliate investments	3,524	1,539	6,474	2,388
Non-control/Non-affiliate investments	18,410	11,948	39,192	21,343
Total interest income	27,362	18,539	56,283	33,374
Dividend income:				
Control investments	2,300	4,160	4,050	10,360
Non-control/Non-affiliate investments	1,068		1,508	
Money market funds	3	10	7	28
Total dividend income	3,371	4,170	5,565	10,388
Other income: (Note 8)				
Control investments	14	75	1,785	75
Affiliate investments	7		154	
Non-control/Non-affiliate investments	2,546	385	4,725	849
Gain on Patriot acquisition (Note 3)		8,632		8,632
Total other income	2,567	9,092	6,664	9,556
Total Investment Income	33,300	31,801	68,512	53,318
Operating Expenses				
Investment advisory fees:				
Base management fee (Note 10)	4,903	3,176	9,179	6,385
Income incentive fee (Note 10)	4,769	4,816	10,018	7,896
Total investment advisory fees	9,672	7,992	19,197	14,281
Interest and credit facility expenses	2,261	1,995	4,522	3,369
Legal fees	170	390	480	390

Valuation services		231		153		448		273
Audit, compliance and tax related fees		265		239		481		501
Allocation of overhead from Prospect Administration (Note 10)		840		840		1,640		1,680
Insurance expense		72		63		143		126
Directors fees		64		64		128		128
Other general and administrative expenses		645		807		1,398		994
Total Operating Expenses		14,220		12,543		28,437		21,742
Net Investment Income		19,080		19,258		40,075		31,576
Net realized gain (loss) on investments (Note 4)		4,489		(51,229)		5,016		(51,229)
Net change in unrealized appreciation (depreciation) on investments (Note 4)		8,371		17,451		12,429		(1,245)
Net Increase (Decrease) in Net Assets Resulting from Operations	$	31,940	$	(14,520)	$	57,520	$	(20,898)
Net increase (decrease) in net assets resulting from operations per share: (Note 9 and Note 12)	$	0.38	$	(0.25)	$	0.73	$	(0.39)
Dividends declared per share	$	0.30	$	0.41	$	0.60	$	0.82

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS
For The Six Months Ended December 31, 2010 and 2009
(in thousands, except share data)
(Unaudited)

	For The Six Months Ended December 31, 2010	December 31, 2009
Increase (Decrease) in Net Assets from Operations:		
Net investment income	$ 40,075	$ 31,576
Net realized gain (loss) on investments	5,016	(51,229)
Net change in unrealized appreciation (depreciation) on investments	12,429	(1,245)
Net Increase (Decrease) in Net Assets Resulting from Operations	57,520	(20,898)
Dividends to Shareholders	(48,752)	(67,721)
Capital Share Transactions:		
Net proceeds from capital shares sold	178,317	98,833
Less: Offering costs of public share offerings	(599)	(1,158)
Fair value of equity issued in conjunction with Patriot acquisition		92,800
Reinvestment of dividends	5,280	5,358
Net Increase in Net Assets Resulting from Capital Share Transactions	182,998	195,833
Total Increase in Net Assets	191,766	107,214
Net assets at beginning of period	711,424	532,596
Net Assets at End of Period	$ 903,190	$ 639,810
Capital Share Activity:		
Shares sold	18,494,476	11,431,797
Shares issued for Patriot acquisition		8,444,068
Shares issued through reinvestment of dividends/distributions	534,044	530,797
Net increase in capital share activity	19,028,520	20,406,662
Shares outstanding at beginning of period	69,086,862	42,943,084
Shares Outstanding at End of Period	88,115,382	63,349,746

See notes to consolidated financial statements.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
For The Six Months Ended December 31, 2010 and 2009
(in thousands, except share data)
(Unaudited)

	For The Six Months Ended December 31, 2010	2009
Cash Flows from Operating Activities:		
Net increase (decrease) in net assets resulting from operations	$ 57,520	$ (20,898)
Net realized (gain) loss on investments	(5,016)	51,229
Net change in unrealized (appreciation) depreciation on investments	(12,429)	1,245
Accretion of purchase discount on investments	(5,960)	(6,670)
Amortization of deferred financing costs	2,134	2,106
Gain on Patriot acquisition		(8,632)
Change in operating assets and liabilities:		
Payments for purchases of investments	(275,867)	(7,321)
Payment-in-kind interest	(6,017)	(2,059)
Proceeds from sale of investments and collection of investment principal	135,553	69,735
Purchases of cash equivalents		(199,997)
Sales of cash equivalents		199,997
Net (increase) decrease investments in money market funds	(63,323)	75,317
(Increase) decrease in interest receivable	(3,064)	163
(Increase) decrease in dividends receivable	(1)	26
Decrease in other receivables	69	212
Decrease (increase) in prepaid expenses	121	(72)
Increase in other assets		(535)
Decrease in due from Prospect Administration		502
Decrease in due to Prospect Administration	23	(842)
Increase in due to Prospect Capital Management	781	2,126
Increase in accrued expenses	(1,418)	(227)
Decrease (increase) in other liabilities	557	(277)
Net Cash (Used In) Provided By Operating Activities	(176,337)	155,128
Cash Flows from Investing Activities:		
Acquisition of Patriot, net of cash acquired (Note 3)		(106,586)
Net Cash Used In Investing Activities		(106,586)
Cash Flows from Financing Activities:		
Issuance of Senior Convertible Notes (Note 6)	150,000	
Borrowings under credit facility	180,500	60,000
Payments under credit facility	(280,800)	(174,800)
Financing costs paid and deferred	(6,660)	(1,046)

Net proceeds from issuance of common stock		178,317		98,833
Offering costs from issuance of common stock		(599)		(1,158)
Dividends paid		(41,483)		(36,469)
Net Cash Provided By Financing Activities		179,275		54,640
Total Increase (Decrease) in Cash		2,938		(6,098)
Cash balance at beginning of period		1,081		9,942
Cash Balance at End of Period	$	4,019	$	3,844
Cash Paid For Interest	$	1,314	$	496
Non-Cash Financing Activity:				
Amount of shares issued in connection with Patriot acquisition	$		$	92,800
Amount of shares issued in connection with dividend reinvestment plan	$	5,280	$	5,358

See notes to consolidated financial statements.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS
December 31, 2010 and June 30, 2010
(in thousands, except share data)

			December 31, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
AIRMALL USA, Inc.	Pennsylvania / Property Management	Senior Secured Term Loan (12.00%, due 6/30/2015)[3], [4]	$ 30,000	$ 30,000	$ 30,000	3.3%
		Senior Subordinated Term Loan (12.00% plus 6.00% PIK, due 12/31/2015)	12,500	12,500	12,500	1.4%
		Convertible Preferred Stock (9,919.684 shares)		9,920	9,920	1.1%
		Common Stock (100 shares)			3,376	0.4%
				52,420	**55,796**	**6.2%**
Ajax Rolled Ring & Machine, Inc.	South Carolina / Manufacturing	Senior Secured Note Tranche A (10.50%, due 4/01/2013)[3], [4]	20,827	20,827	20,827	2.3%
		Subordinated Secured Note Tranche B (11.50% plus 6.00% PIK, due 4/01/2013)[3], [4]	14,396	14,396	9,747	1.1%
		Convertible Preferred Stock Series A (6,142.6 shares)		6,057		0.0%
		Unrestricted Common Stock (6 shares)				0.0%
				41,280	**30,574**	**3.4%**
AWCNC, LLC[20]	North Carolina / Machinery	Members Units Class A (1,800,000 units)				0.0%
		Members Units Class B-1 (1 unit)				0.0%
		Members Units Class B-2 (7,999,999 units)				0.0%
						0.0%
Borga, Inc.	California / Manufacturing	Revolving Line of Credit $1,000 Commitment (5.00%	1,000	945	850	0.1%

		plus 3.00% default interest, in non-accrual status effective 03/02/2010, past due)[4], [26]				
		Senior Secured Term Loan B (8.50% plus 3.00% default interest, in non-accrual status effective 03/02/2010, past due)[4]	1,612	1,500	1,370	0.2%
		Senior Secured Term Loan C (12.00% plus 4.00% PIK plus 3.00% default interest, in non-accrual status effective 03/02/2010, past due)	8,802	707	182	0.0%
		Common Stock (100 shares)[22]				0.0%
		Warrants (33,750 warrants)[22]				0.0%
				3,152	**2,402**	**0.3%**
C&J Cladding LLC	Texas / Metal Services and Minerals	Membership Interest (400 units)[23]		580	5,199	0.6%
				580	**5,199**	**0.6%**
Change Clean Energy Holdings, Inc. (CCEHI or Biomass[5])	Maine / Biomass Power	Common Stock (1,000 shares)		2,540		0.0%
				2,540		**0.0%**
Fischbein, LLC	North Carolina / Machinery	Senior Subordinated Debt (13.00% plus 3.50% PIK, due 5/01/2013)	2,121	1,963	2,121	0.3%
		Membership Interest[25]		1,899	11,142	1.2%
				3,862	**13,263**	**1.5%**
Freedom Marine Services LLC[21]	Louisiana / Shipping Vessels	Subordinated Secured Note (12.00% plus 4.00% PIK, in non-accrual status effective 10/1/2010, due 12/31/2011)	10,506	10,367	3,649	0.4%
		Net Profits Interest (22.50% payable on equity distributions)[7]				0.0%
				10,367	**3,649**	**0.4%**

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS (CONTINUED)
December 31, 2010 and June 30, 2010
(in thousands, except share data)

			December 31, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Gas Solutions Holdings, Inc.[8], [3]	Texas / Gas Gathering and Processing	Senior Secured Note (18.00%, due 12/11/2016)	$ 25,000	$ 25,000	$ 25,000	2.8%
		Junior Secured Note (18.00%, due 12/12/2016)	12,000	12,000	12,000	1.3%
		Common Stock (100 shares)		5,003	60,596	6.7%
				42,003	**97,596**	**10.8%**
Integrated Contract Services, Inc.[9]	North Carolina / Contracting	Secured Promissory Note (15.00%, in non-accrual status effective 12/22/2010, due 1/21/2011) [10]	200	200	200	0.0%
		Senior Demand Note (15.00%, in non-accrual status effective 11/1/2010, past due)[10]	1,170	1,170	1,170	0.2%
		Senior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	960	660		0.0%
		Junior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	14,003	14,003		0.0%
		Preferred Stock Series A (10 shares)				0.0%
		Common Stock (49 shares)		679		0.0%
				16,712	**1,370**	**0.2%**
Iron Horse Coiled Tubing, Inc.[24]	Alberta, Canada / Production Services	Senior Secured Tranche 2 (Zero Coupon, due 12/31/2016)	2,338	2,338	2,338	0.2%

		Senior Secured Tranche 3 (2.00%, due 12/31/2016)	16,000	15,781	16,000	1.8%
		Common Stock (3,821 shares)		268	655	0.1%
				18,387	**18,993**	**2.1%**
Manx Energy, Inc. (Manx)[12]	Kansas / Oil & Gas Production	Appalachian Energy Holdings, LLC (AEH) Senior Secured Note (8.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)	2,159	2,000	325	0.0%
		Coalbed, LLC Senior Secured Note (8.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)[6]	6,478	5,991	975	0.1%
		Manx Senior Secured Note (13.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)	3,300	3,300	3,300	0.4%
		Manx Preferred Stock (6,635 shares)		6,307		0.0%
		Manx Common Stock (3,416,335 shares)		1,171		0.0%
				18,769	**4,600**	**0.5%**
NRG Manufacturing, Inc.	Texas / Manufacturing	Senior Secured Note (16.50%, due 8/31/2011)[3], [4]	13,080	13,080	13,080	1.4%
		Common Stock (800 shares)		2,317	5,744	0.6%
				15,397	**18,824**	**2.0%**
Nupla Corporation	California / Home & Office Furnishings, Housewares & Durable	Revolving Line of Credit $2,000 Commitment (7.25% plus 2.00% default interest, due 9/04/2012)[4], [26]	1,093	985	1,093	0.1%
		Senior Secured Term Loan A (8.00% plus 2.00% default interest, due 9/04/2012)[4]	4,708	1,072	4,277	0.5%
		Senior Subordinated Debt (15.00% PIK, in non-accrual status effective 4/01/2009, due 3/04/2013)	3,368			0.0%
		Preferred Stock Class A (2,850 shares)				0.0%
		Preferred Stock Class B (1,330 shares)				0.0%
		Common Stock (2,360,743 shares)				0.0%

2,057	**5,370**	**0.6%**

See notes to consolidated financial statements.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS (CONTINUED)
December 31, 2010 and June 30, 2010
(in thousands, except share data)

			December 31, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
R-V Industries, Inc.	Pennsylvania / Manufacturing	Warrants (200,000 warrants, expiring 6/30/2017)		$ 1,682	$ 1,770	0.2%
		Common Stock (545,107 shares)		5,086	4,822	0.5%
				6,768	**6,592**	**0.7%**
Yatesville Coal Holdings, Inc.[11]	Kentucky / Mining, Steel, Iron and Non-Precious Metals and Coal Production	Senior Secured Note (Non-accrual status effective 1/01/2009, due 12/31/2010)[4]	$ 1,035	1,035		0.0%
		Junior Secured Note (Non-accrual status effective 1/01/2009, due 12/31/2010)[4]	400	400		0.0%
		Common Stock (1,000 shares)				0.0%
				1,435		**0.0%**
		Total Control Investments		**235,729**	**264,228**	**29.3%**
Affiliate Investments (5.00% to 24.99% voting control)						
Biotronic NeuroNetwork	Michigan / Healthcare	Senior Secured Note (11.50% plus 1.00% PIK, due 2/21/2013)[3], [4]	26,227	26,227	27,014	3.0%
		Preferred Stock Series A (9,925.455 shares)[13]		2,300	3,621	
		Preferred Stock Series B (1,753.64 shares)[13]		579	912	0.5%
				29,106	**31,547**	**3.5%**

Boxercraft Incorporated	Georgia / Textiles & Leather	Senior Secured Term Loan A (9.50%, due 9/16/2013)(3), (4)	3,190	2,797	3,050	0.3%
		Senior Secured Term Loan B (10.00%, due 9/16/2013)(3), (4)	4,780	3,924	4,511	0.5%
		Subordinated Secured Term Loan (12.00% plus 6.50% PIK, due 3/16/2014)(3)	7,479	6,117	7,028	0.8%
		Preferred Stock (1,000,000 shares)			216	0.0%
		Common Stock (10,000 shares)				0.0%
				12,838	**14,805**	**1.6%**
KTPS Holdings, LLC	Colorado / Textiles & Leather	Revolving Line of Credit $1,500 Commitment (10.50%, due 1/31/2012)(26), (27)	1,250	1,250	1,250	0.1%
		Senior Secured Term Loan A (10.50%, due 1/31/2012)(3), (4)	2,730	2,548	2,568	0.3%
		Senior Secured Term Loan B (12.00%, due 1/31/2012)(3)	425	384	377	0.0%
		Senior Secured Term Loan C (12.00% plus 12.75% PIK, due 3/31/2012)(3)	5,259	4,806	4,030	0.6%
		Membership Interest Class A (730 units)				0.0%
		Membership Interest Common (199,795 units)				0.0%
				8,988	**8,225**	**1.0%**
Smart, LLC(15)	New York / Diversified / Conglomerate Service	Membership Interest Class B (1,218 units)				0.0%
		Membership Interest Class D (1 unit)				0.0%
						0.0%

See notes to consolidated financial statements.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS (CONTINUED)
December 31, 2010 and June 30, 2010
(in thousands, except share data)

			December 31, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Affiliate Investments (5.00% to 24.99% voting control)						
Sport Helmets Holdings, LLC[15]	New York / Personal & Nondurable Consumer Products	Revolving Line of Credit $3,000 Commitment (5.75%, due 12/14/2013)[26], [27]	$ 500	$ 500	$ 500	0.1%
		Senior Secured Term Loan A (4.30%, due 12/14/2013)[3], [4]	2,575	1,503	2,540	0.3%
		Senior Secured Term Loan B (4.80%, due 12/14/2013)[3], [4]	7,350	5,380	6,338	0.7%
		Senior Subordinated Debt Series A (12.00% plus 3.00% PIK, due 6/14/2014)[3]	7,437	6,080	7,221	0.8%
		Senior Subordinated Debt Series B (10.00% plus 5.00% PIK, due 6/14/2014)[3]	1,392	1,012	1,209	0.1%
		Common Stock (20,554 shares)		408	2,324	0.2%
				14,883	**20,132**	**2.2%**
		Total Affiliate Investments		**65,815**	**74,709**	**8.3%**
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
ADAPCO, Inc.	Florida / Ecological	Common Stock (5,000 shares)		141	325	0.0%
				141	**325**	**0.0%**

Aircraft Fasteners International, LLC	California / Machinery	Revolving Line of Credit $500 Commitment (9.50%, due 11/01/2012)(26), (27)				0.0%
		Senior Secured Term Loan (9.50%, due 11/01/2012)(3), (4)	3,935	3,935	3,935	0.5%
		Junior Secured Term Loan (12.00% plus 6.00% PIK, due 5/01/2013)(3)	4,804	4,804	4,792	0.5%
		Convertible Preferred Stock (32,500 units)		396	158	0.0%
				9,135	**8,885**	**1.0%**
American Gilsonite Company	Utah / Specialty Minerals	Senior Subordinated Note (12.00% plus 2.50% PIK, due 12/10/2016)	30,000	30,000	30,000	3.3%
		Membership Interest in AGC/PEP, LLC (99.9999%)(16)			3,253	0.4%
				30,000	**33,253**	**3.7%**
Arrowhead General Insurance Agency, Inc.(17)	California / Insurance	Senior Secured Term Loan (8.50%, due 8/08/2012)	846	823	842	0.1%
		Junior Secured Term Loan (10.25% plus 2.50% PIK, due 2/08/2013)	6,258	5,253	5,664	0.6%
				6,076	**6,506**	**0.7%**
Caleel + Hayden, LLC (15)	Colorado / Personal & Nondurable Consumer Products	Membership Units (7,500 shares)		351	878	0.1%
		Options in Mineral Fusion Natural Brands, LLC (11,662 options)				0.0%
				351	**878**	**0.1%**

The Copernicus Group, Inc.	North Carolina / Healthcare	Revolving Line of Credit — $500 Commitment (10.00%, due 10/08/2013)(4), (26)	150	41	148	0.0%
		Senior Secured Term Loan A (10.00%, due 10/08/2013)(3), (4)	5,450	4,841	5,367	0.6%
		Senior Subordinated Debt (10.00% plus 10.00% PIK, due 4/08/2014)	14,083	12,253	14,154	1.6%
		Preferred Stock Series A (1,000,000 shares)		67	558	0.1%
		Preferred Stock Series C (212,121 shares)		212	285	0.0%
				17,414	**20,512**	**2.3%**

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LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Deb Shops, Inc.[17]	Pennsylvania / Retail	Second Lien Debt (14.00% PIK, in non-accrual status effective 2/24/2009, due 10/23/2014)	$ 18,841	$ 14,606	$ 1,372	0.2%
				14,606	**1,372**	**0.2%**
Diamondback Operating, LP	Oklahoma / Oil & Gas Production	Net Profits Interest (15.00% payable on Equity distributions)[7]			191	0.0%
					191	**0.0%**
EXL Acquisition Corporation	South Carolina / Electronics	Revolving Line of Credit $1,000 Commitment (7.75%, due 06/24/2015)[26], [27]				0.0%
		Senior Secured Term Loan A (7.75%, due 6/24/2015)[3], [4]	11,191	11,191	11,303	1.3%
		Senior Secured Term Loan B (12.00% plus 2.00% PIK, due 12/24/2015)[3]	11,797	11,797	11,839	1.3%
		Common Stock Class A (2,475 shares)		437	469	0.1%
		Common Stock Class B (25 shares)		252	5	0.0%
				23,677	**23,616**	**2.6%**
Fairchild Industrial Products, Co.	North Carolina / Electronics	Preferred Stock Class A (285.1 shares)		377	694	0.1%
		Common Stock Class B (28 shares)		211	411	0.0%
				588	**1,105**	**0.1%**
H&M Oil & Gas, LLC	Texas / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% PIK, past due)	60,019	60,019	42,959	4.8%

		Net Profits Interest (8.00% payable on Equity distributions)(7)				0.0%
				60,019	**42,959**	**4.8%**
Hoffmaster Group, Inc.	Wisconsin / Durable Consumer Products	Second Lien Term Loan (13.50%, due 6/2/2017)(3)	20,000	20,000	20,400	2.3%
				20,000	**20,400**	**2.3%**
Hudson Products Holdings, Inc.(17)	Texas / Manufacturing	Senior Secured Term Loan (8.50%, due 8/24/2015)(3), (4)	6,365	5,784	5,248	0.6%
				5,784	**5,248**	**0.6%**
ICON Health & Fitness, Inc.	Utah / Durable Consumer Products	Senior Secured Note (11.875%, due 10/15/2016) (3)	32,500	32,332	32,187	3.6%
				32,332	**32,187**	**3.6%**
IEC Systems LP (IEC) /Advanced Rig Services LLC (ARS)	Texas / Oilfield Fabrication	IEC Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	17,033	17,033	17,033	1.9%
		ARS Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)(3), (4)	9,293	9,293	9,293	1.0%
				26,326	**26,326**	**2.9%**
Jordan Healthcare Holdings, Inc.	Texas / Healthcare	Senior Subordinated Debt (12.00% plus 2.50% PIK, due 6/23/2016)	15,310	15,310	15,300	1.7%
				15,310	**15,300**	**1.7%**
Label Corp Holdings, Inc.	Nebraska / Printing & Publishing	Senior Secured Term Loan (8.50%, due 8/08/2014)(3), (4)	5,764	5,255	5,385	0.6%
				5,255	**5,385**	**0.6%**

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LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
LHC Holdings Corp.[17]	Florida / Healthcare	Revolving Line of Credit $750 Commitment (8.50%, due 6/30/2012)[26], [27]		$	$	0.0%
		Senior Secured Term Loan A (8.50%, due 6/30/2012)[3], [4]	$ 1,456	1,456	1,375	0.2%
		Senior Subordinated Debt (12.00% plus 2.50% PIK, due 5/31/2013)[3]	4,565	4,247	4,278	0.4%
		Membership Interest (125 units)		216	175	0.0%
				5,919	**5,828**	**0.6%**
Mac & Massey Holdings, LLC	Georgia / Food Products	Senior Subordinated Debt (10.00% plus 5.75% PIK, due 2/10/2013) [3]	8,928	7,785	8,928	1.1%
		Membership Interest (250 units)		133	561	0.0%
				7,918	**9,489**	**1.1%**
Maverick Healthcare, LLC	Arizona / Healthcare	Second Lien Debt (12.50% plus 3.50% PIK, due 4/30/2014)[3]	13,357	13,357	13,485	1.5%
		Preferred Units (1,250,000 units)		1,253	1,894	0.2%
		Common Units (1,250,000 units)			2,072	0.2%
				14,610	**17,451**	**1.9%**

Miller Petroleum, Inc.	Tennessee / Oil & Gas Production	Common Stock (616,304 shares) (14)		46	2,564	0.3%
				46	**2,564**	**0.3%**
Northwestern Management Services, LLC	Florida / Healthcare	Revolving Line of Credit $1,500 Commitment (10.50%, due 7/30/2015)(26)				0.0%
		Senior Secured Term Loan A (10.50%, due 7/30/2015)(3), (4)	18,500	18,500	18,500	2.0%
		Common Stock (50 shares)		371	584	0.1%
				18,871	**19,084**	**2.1%**
Prince Mineral Company, Inc. (3)	New York / Metal Services and Minerals	Junior Secured Term Loan (9.00%, due 12/21/2012)(4)	11,075	11,075	11,075	1.2%
		Senior Subordinated Debt (13.00% plus 2.00%, due 7/21/2013)	12,385	1,693	12,385	1.4%
				12,768	**23,460**	**2.6%**
Progrexion Holdings, LLC(4)	Utah / Consumer Services	Revolving Line of Credit $2,000 Commitment (11.0%, due 6/30/2011)				0.0%
		Senior Secured Term Loan (11.0%, due 12/31/2014) (3)	35,820	35,820	35,820	4.0%
				35,820	**35,820**	**4.0%**
R-O-M Corporation	Missouri / Automobile	Revolving Line of Credit $1,750 Commitment (4.25%, due 2/08/2013)(26), (27)				0.0%
		Senior Secured Term Loan A (4.25%, due 2/08/2013)(3), (4)	3,840	3,426	3,751	0.4%
		Senior Secured Term Loan B (8.00%, due 5/08/2013)(3), (4)	7,208	7,208	7,159	0.8%
		Senior Subordinated Debt (12.00% plus 3.00% PIK due 8/08/2013)(3)	7,100	6,820	6,857	0.8%

				17,454	**17,767**	**2.0%**
Royal Adhesives & Sealants, LLC	Indiana / Chemicals	Senior Subordinated Unsecured Term Loan (12.00% plus 2.00% PIK due 11/29/2016)	25,026	25,026	25,026	2.8%
				25,026	**25,026**	**2.8%**

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LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Seaton Corp.	Illinois / Business Services	Subordinated Secured (12.50% plus 2.00% PIK, due 3/14/2014) [3], [4]	$ 12,359	$ 12,148	$ 12,358	1.4%
				12,148	**12,358**	**1.4%**
Shearer s Foods, Inc.	Ohio / Food Products	Junior Secured Debt (12.00% plus 3.50% PIK, due 3/31/2016)[3]	35,809	35,809	37,599	4.1%
		Membership Interest in Mistral Chip Holdings, LLC (2,000 units)[18]		2,000	6,107	0.7%
		Membership Interest in Mistral Chip Holdings, LLC 2 (595 units)[18]		1,322	1,817	0.2%
				39,131	**45,523**	**5.0%**
Skillsoft Public Limited Company	Ireland / Software & Computer Services	Subordinated Unsecured (11.125%, due 06/01/2018)	15,000	14,905	15,000	1.7%
				14,905	**15,000**	**1.7%**
Snacks Holding Corporation	Minnesota / Food Products	Senior Subordinated Unsecured Term Loan (12.00% plus 1.00% PIK, due 11/12/2017)	15,021	14,482	14,814	1.6%
		Series A Preferred Stock (4,021.45 shares)		52	61	0.0%
		Series B Preferred Stock (1,866.10 shares)		52	61	0.0%
		Warrant (to purchase 31,196.52 voting common shares, expires		441	515	0.1%

		11/12/2020)				
				15,027	**15,451**	**1.7%**
SonicWALL, Inc.	California / Software & Computer Services	Subordinated Secured (12.00%, due 1/23/2017) (3), (4))	23,000	22,980	23,000	2.5%
				22,980	**23,000**	**2.5%**
Stryker Energy, LLC	Ohio / Oil & Gas Production	Subordinated Secured Revolving Credit Facility (12.00% plus 3.00% PIK, due 12/01/2012)(3), (4)	30,183	30,034	27,863	3.1%
		Overriding Royalty Interests(19)			2,250	0.2%
				30,034	**30,113**	**3.3%**
Unitek(17)	Pennsylvania / Technical Services	Second Lien Debt (13.08%, due 12/31/2013)(3), (4)	11,500	11,401	11,500	1.2%
				11,401	**11,500**	**1.2%**
VPSI, Inc	Michigan / Transportation	First Lien Senior Secured Note (12.00%, due 12/23/2015)	18,333	18,333	18,333	2.0%
				18,333	**18,333**	**2.0%**
Wind River Resources Corp. and Wind River II Corp.	Utah / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% default interest on principal, 16.00% default interest on past due interest, in non-accrual status effective 12/01/2008, past due)(4)	15,000	15,000	6,955	0.7%
		Net Profits Interest (5.00% payable on Equity distributions)(7)				0.0%
				15,000	**6,955**	**0.7%**
		Total Non-control/Non-affiliate Investments (Level 3 Investments)		**584,405**	**579,170**	**64.1%**
				885,949	**918,107**	**101.7%**

Total Level 3 Portfolio Investments

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				December 31, 2010		
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 1 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Allied Defense Group, Inc.	Virginia / Aerospace & Defense	Common Stock (10,000 shares)		$ 56	$ 34	0.0%
				56	**34**	**0.0%**
Dover Saddlery, Inc.	Massachusetts / Retail	Common Stock (30,974 shares)		63	80	0.0%
				63	**80**	**0.0%**
		Total Non-control/Non-affiliate Investments (Level 1 Investments)		**119**	**114**	**0.0%**
		Total Portfolio Investments		**886,068**	**918,221**	**101.7%**
SHORT TERM INVESTMENTS: Money Market Funds (Level 2 Investments)						
Fidelity Institutional Money Market Funds (Class I)		Government Portfolio		125,023	125,023	13.8%
Fidelity Institutional Money Market Funds (Class I)[3]		Government Portfolio		7,170	7,170	0.8%
Victory Government Money Market Funds				1	1	0.0%
		Total Money Market Funds		**132,194**	**132,194**	**14.6%**
		Total Investments		**1,018,262**	**1,050,415**	**116.3%**

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Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Ajax Rolled Ring & Machine, Inc.	South Carolina / Manufacturing	Senior Secured Note Tranche A (10.50%, due 4/01/2013)[3], [4]	$ 21,047	$ 21,047	$ 21,047	3.0%
		Subordinated Secured Note Tranche B (11.50% plus 6.00% PIK, due 4/01/2013)[3], [4]	16,306	16,306	9,857	1.3%
		Subordinated Secured Note Tranche B (15.00%, due 10/30/2010)	500	500		0.0%
		Convertible Preferred Stock Series A (6,142.6 shares)		6,057		0.0%
		Unrestricted Common Stock (6 shares)				0.0%
				43,910	**30,904**	**4.3%**
AWCNC, LLC[20]	North Carolina / Machinery	Members Units Class A (1,800,000 units)				0.0%
		Members Units Class B-1 (1 unit)				0.0%
		Members Units Class B-2 (7,999,999 units)				0.0%
						0.0%
Borga, Inc.	California / Manufacturing	Revolving Line of Credit $1,000 Commitment (4.75% plus 3.25% default interest, in non-accrual status effective 03/02/2010, past due)[4], [26]	1,000	945	850	0.1%
			1,612	1,500	1,282	0.2%

		Senior Secured Term Loan B (8.25% plus 3.25% default interest, in non-accrual status effective 03/02/2010, past due)[4]				
		Senior Secured Term Loan C (12.00% plus 4.00% PIK plus 3.00% default interest, in non-accrual status effective 03/02/2010, past due)	8,624	707		0.0%
		Common Stock (100 shares)[22]				0.0%
		Warrants (33,750 warrants)[22]				0.0%
				3,152	**2,132**	**0.3%**
C&J Cladding LLC	Texas / Metal Services and Minerals	Membership Interest (400 units)[23]		580	4,128	0.6%
				580	**4,128**	**0.6%**
Change Clean Energy Holdings, Inc. (CCEHI or Biomass[5])	Maine / Biomass Power	Common Stock (1,000 shares)		2,383		0.0%
				2,383		**0.0%**
Fischbein, LLC	North Carolina / Machinery	Senior Subordinated Debt (13.00% plus 5.50% PIK, due 5/01/2013)	3,811	3,631	3,811	0.5%
		Membership Interest[25]		1,899	4,812	0.7%
				5,530	**8,623**	**1.2%**
Freedom Marine Services LLC	Louisiana / Shipping Vessels	Subordinated Secured Note (16.00% PIK, due 12/31/2011)[3]	10,088	10,040	3,583	0.5%
		Net Profits Interest (22.50% payable on equity distributions)[3], [7]				0.0%
				10,040	**3,583**	**0.5%**
Gas Solutions Holdings, Inc.[8], [3]	Texas / Gas Gathering and Processing	Senior Secured Note (18.00%, due 12/11/2016)	25,000	25,000	25,000	3.5%

Junior Secured Note (18.00%, due 12/12/2016)	7,500	7,500	7,500	1.1%
Common Stock (100 shares)		5,003	60,596	8.5%
		37,503	**93,096**	**13.1%**

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Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Integrated Contract Services, Inc.[9]	North Carolina / Contracting	Senior Demand Note (15.00%, past due)[10]	$ 1,170	$ 1,170	$ 1,170	0.2%
		Senior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	1,100	800	1,100	0.2%
		Junior Secured Note (7.00% plus 7.00% PIK plus 6.00% default interest, in non-accrual status effective 10/09/2007, past due)	14,003	14,003	2,272	0.2%
		Preferred Stock Series A (10 shares)				0.0%
		Common Stock (49 shares)		679		0.0%
				16,652	**4,542**	**0.6%**
Iron Horse Coiled Tubing, Inc.[24]	Alberta, Canada / Production Services	Senior Secured Tranche 1 (Zero Coupon, in non-accrual status effective 1/01/2010, due 12/31/2016)	615	396	615	0.1%
		Senior Secured Tranche 2 (Zero Coupon, in non-accrual status effective 1/01/2010, due 12/31/2016)	2,337	2,338	2,338	0.3%
		Senior Secured Tranche 3 (1.00%, in non-accrual status effective 1/01/2010, due	18,000	18,000	9,101	1.3%

		12/31/2016) Common Stock (3,821 shares)		268		0.0%
				21,002	**12,054**	**1.7%**
Manx Energy, Inc. (Manx)[12]	Kansas / Oil & Gas Production	Appalachian Energy Holdings, LLC (AEH) Senior Secured Note (8.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)	2,073	2,000	472	0.1%
		Coalbed, LLC Senior Secured Note (8.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)[6]	6,219	5,991	1,414	0.2%
		Manx Senior Secured Note (13.00%, in non-accrual status effective 1/19/2010, due 1/19/2013)	2,800	2,800	2,800	0.4%
		Manx Preferred Stock (6,635 shares)		6,308		0.0%
		Manx Common Stock (3,416,335 shares)		1,171		0.0%
				18,270	**4,686**	**0.7%**
NRG Manufacturing, Inc.	Texas / Manufacturing	Senior Secured Note (16.50%, due 8/31/2011)[3], [4]	13,080	13,080	13,080	1.8%
		Common Stock (800 shares)		2,317	7,031	1.0%
				15,397	**20,111**	**2.8%**
Nupla Corporation	California / Home & Office Furnishings, Housewares & Durable	Revolving Line of Credit $2,000 Commitment (7.25% plus 2.00% default interest, due 9/04/2012)[4], [26]	1,093	958	1,093	0.1%
		Senior Secured Term Loan A (8.00% plus 2.00% default interest, due 9/04/2012)[4]	5,139	1,503	3,301	0.5%
		Senior Subordinated Debt (10.00% plus 5.00% PIK, in	3,368			0.0%

		non-accrual status effective 4/01/2009, due 3/04/2013)			
		Preferred Stock Class A (2,850 shares)			0.0%
		Preferred Stock Class B (1,330 shares)			0.0%
		Common Stock (2,360,743 shares)			0.0%
			2,461	**4,394**	**0.6%**
R-V Industries, Inc.	Pennsylvania / Manufacturing	Warrants (200,000 warrants, expiring 6/30/2017)	1,682	1,697	0.2%
		Common Stock (545,107 shares)	5,086	4,626	0.7%
			6,768	**6,323**	**0.9%**

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LEVEL 3 PORTFOLIO INVESTMENTS:						
Control Investments (25.00% or greater of voting control)						
Sidump r Trailer Company, Inc.	Nebraska / Automobile	Revolving Line of Credit $2,000 Commitment (7.25%, in non-accrual status effective 11/01/2008, due 1/10/2011)[4], [26]	$ 1,025	$ 479	$ 574	0.1%
		Senior Secured Term Loan A (7.25%, in non-accrual status effective 11/01/2008, due 1/10/2011)[4]	2,048	463		0.0%
		Senior Secured Term Loan B (8.75%, in-non-accrual status effective 11/01/2008, due 1/10/2011)[4]	2,321			0.0%
		Senior Secured Term Loan C (16.50% PIK, in non-accrual status effective 9/27/2008, due 7/10/2011)	3,085			0.0%
		Senior Secured Term Loan D (7.25%, in non-accrual status effective 11/01/2008, due 7/10/2011)[4]	1,700			0.0%
		Preferred Stock (49,843 shares)				0.0%
		Common Stock (64,050 shares)				0.0%
				942	**574**	**0.1%**
Yatesville Coal Holdings, Inc.[11]	Kentucky / Mining, Steel, Iron and Non-Precious Metals and Coal Production	Senior Secured Note (Non-accrual status effective 1/01/2009, due 12/31/2010)[4]	10,000	1,035	808	0.1%
			41,931	95		0.0%

		Junior Secured Note (Non-accrual status effective 1/01/2009, due 12/31/2010)(4)				
		Common Stock (1,000 shares)				0.0%
				1,130	**808**	**0.1%**
		Total Control Investments		**185,720**	**195,958**	**27.5%**
Affiliate Investments (5.00% to 24.99% voting control)						
Biotronic NeuroNetwork	Michigan / Healthcare	Senior Secured Note (11.50% plus 1.00% PIK, due 2/21/2013)(3), (4)	26,227	26,227	26,744	3.8%
		Preferred Stock (9,925.455 shares)(13)		2,300	2,759	0.4%
				28,527	**29,503**	**4.2%**
Boxercraft Incorporated	Georgia / Textiles & Leather	Revolving Line of Credit $1,000 Commitment (9.00%, due 9/16/2013)(26), (27)	1,000	1,000	1,000	0.1%
		Senior Secured Term Loan A (9.50%, due 9/16/2013)(3), (4)	3,843	3,330	3,577	0.5%
		Senior Secured Term Loan B (10.00%, due 9/16/2013)(3), (4)	4,822	3,845	4,386	0.6%
		Subordinated Secured Term Loan (12.00% plus 6.50% PIK, due 3/16/2014)(3)	7,235	5,775	6,717	1.0%
		Preferred Stock (1,000,000 shares)			205	0.0%
		Common Stock (10,000 shares)				0.0%
				13,950	**15,885**	**2.2%**
KTPS Holdings, LLC	Colorado / Textiles & Leather	Revolving Line of Credit $1,500 Commitment (10.50%, due 1/31/2012)(26), (27)	1,000	1,000	1,000	0.1%
		Senior Secured Term Loan A (10.50%, due 1/31/2012)(3), (4)	3,130	2,847	2,916	0.4%
			435	377	409	0.1%

Senior Secured Term Loan B (12.00%, due 1/31/2012)(3)				
Senior Secured Term Loan C (12.00% plus 6.00% PIK, due 3/31/2012)(3)	4,932	4,345	4,796	0.7%
Membership Interest Class A (730 units)				0.0%
Membership Interest Common (199,795 units)				0.0%
		8,569	**9,121**	**1.3%**

See notes to consolidated financial statements.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS (CONTINUED)
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			June 30, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Affiliate Investments (5.00% to 24.99% voting control)						
Smart, LLC[15]	New York / Diversified / Conglomerate Service	Membership Interest Class B (1,218 units)		$	$	0.0%
		Membership Interest Class D (1 unit)				0.0%
						0.0%
Sport Helmets Holdings, LLC[15]	New York / Personal & Nondurable Consumer Products	Revolving Line of Credit $3,000 Commitment (4.54%, due 12/14/2013)[26], [27]				0.0%
		Senior Secured Term Loan A (4.54%, due 12/14/2013)[3], [4]	$ 3,025	1,658	2,993	0.4%
		Senior Secured Term Loan B (5.04%, due 12/14/2013)[3], [4]	7,388	5,161	6,432	0.9%
		Senior Subordinated Debt Series A (12.00% plus 3.00% PIK, due 6/14/2014)[3]	7,325	5,857	6,734	0.9%
		Senior Subordinated Debt Series B (10.00% plus 5.00% PIK, due 6/14/2014)[3]	1,357	952	1,160	0.2%
		Common Stock (20,554 shares)		408	1,912	0.3%
				14,036	**19,231**	**2.7%**
			Total Affiliate Investments	**65,082**	**73,740**	**10.4%**

Non-control/Non-affiliate Investments (less than 5.00% of voting

control)

ADAPCO, Inc.	Florida / Ecological	Common Stock (5,000 shares)		141	340	0.0%
				141	**340**	**0.0%**
Aircraft Fasteners International, LLC	California / Machinery	Revolving Line of Credit $500 Commitment (9.50%, due 11/01/2012)[26], [27]				0.0%
		Senior Secured Term Loan (9.50%, due 11/01/2012)[3], [4]	4,565	4,565	4,248	0.6%
		Junior Secured Term Loan (12.00% plus 6.00% PIK, due 5/01/2013)[3]	5,134	5,134	4,807	0.7%
		Convertible Preferred Stock (32,500 units)		396	98	0.0%
				10,095	**9,153**	**1.3%**
American Gilsonite Company	Utah / Specialty Minerals	Senior Subordinated Note (12.00% plus 3.00% PIK, due 3/14/2013)[3]	14,783	14,783	14,931	2.1%
		Membership Interest in AGC/PEP, LLC (99.9999%)[16]		1,031	3,532	0.5%
				15,814	**18,463**	**2.6%**
Arrowhead General Insurance Agency, Inc.[17]	California / Insurance	Senior Secured Term Loan (8.50%, due 8/08/2012)	850	809	830	0.1%
		Junior Secured Term Loan (10.25% plus 2.50% PIK, due 2/08/2013)	6,179	5,002	5,122	0.7%
				5,811	**5,952**	**0.8%**
Caleel + Hayden, LLC [15]	Colorado / Personal & Nondurable Consumer Products	Membership Units (7,500 shares)		351	818	0.1%
		Options in Mineral Fusion Natural Brands, LLC (11,662 options)				0.0%
				351	**818**	**0.1%**

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			June 30, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Castro Cheese Company, Inc.	Texas / Food Products	Subordinated Secured Note (11.00% plus 2.00% PIK, due 2/28/2013)[3]	$ 7,692	$ 7,597	$ 7,769	1.1%
				7,597	**7,769**	**1.1%**
The Copernicus Group, Inc.	North Carolina / Healthcare	Revolving Line of Credit $500 Commitment (10.00%, due 10/08/2013)[4], [26]	150	22	150	0.0%
		Senior Secured Term Loan A (10.00%, due 10/08/2013)[3], [4]	5,850	5,058	5,416	0.8%
		Senior Subordinated Debt (10.00% plus 10.00% PIK, due 4/08/2014)	13,390	11,421	12,677	1.8%
		Preferred Stock Series A (1,000,000 shares)		67	104	0.0%
		Preferred Stock Series C (212,121 shares)		212	246	0.0%
				16,780	**18,593**	**2.6%**
Deb Shops, Inc.[17]	Pennsylvania / Retail	Second Lien Debt (14.00% PIK, in non-accrual status effective 2/24/2009, due 10/23/2014)	17,562	14,606	2,051	0.3%
				14,606	**2,051**	**0.3%**
Diamondback Operating, LP	Oklahoma / Oil & Gas Production	Net Profits Interest (15.00% payable on Equity distributions)[7]			193	0.0%
					193	**0.0%**

EXL Acquisition Corporation.	South Carolina / Electronics	Revolving Line of Credit $1,000 Commitment (7.75%, due 06/24/2015)[26], [27]				0.0%
		Senior Secured Term Loan A (7.75%, due 6/24/2015)[3], [4]	12,250	12,250	12,250	1.7%
		Senior Secured Term Loan B (12.00% plus 2.00% PIK, due 12/24/2015)[3]	12,250	12,250	12,250	1.7%
		Common Stock Class A (2,475 shares)		437	363	0.1%
		Common Stock Class B (25 shares)		252	103	0.0%
				25,189	**24,966**	**3.5%**
Fairchild Industrial Products, Co.[2]	North Carolina / Electronics	Preferred Stock Class A (285.1 shares)		377	435	0.1%
		Common Stock Class B (28 shares)		211	228	0.0%
				588	**663**	**0.1%**
H&M Oil & Gas, LLC	Texas / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% PIK, due 9/30/2010)	59,107	59,107	48,867	6.9%
		Net Profits Interest (8.00% payable on Equity distributions)[7]			827	0.1%
				59,107	**49,694**	**7.0%**
Hoffmaster Group, Inc.	Wisconsin / Durable Consumer Products	Second Lien Term Loan (13.50%, due 6/2/2017)[3]	20,000	20,000	20,000	2.8%
				20,000	**20,000**	**2.8%**
Hudson Products Holdings, Inc.[17]	Texas / Manufacturing	Senior Secured Term Loan (8.00%, due 8/24/2015)[3], [4]	6,365	5,734	5,314	0.7%
				5,734	**5,314**	**0.7%**
IEC Systems LP (IEC) / Advanced Rig Services LLC (ARS)	Texas / Oilfield Fabrication	IEC Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)[3], [4]	19,008	19,008	19,008	2.7%
		ARS Senior Secured Note (12.00% plus 3.00% PIK, due 11/20/2012)[3], [4]	11,421	11,421	11,421	1.6%
				30,429	**30,429**	**4.3%**

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			June 30, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Impact Products, LLC	Ohio / Home & Office Furnishings, Housewares & Durable	Junior Secured Term Loan (6.38%, due 9/09/2012)[4]	$ 7,300	$ 6,351	$ 7,290	1.0%
		Senior Subordinated Debt (10.00% plus 5.00% PIK, due 9/09/2012)	5,548	5,300	5,548	0.8%
				11,651	**12,838**	**1.8%**
Label Corp Holdings, Inc.	Nebraska / Printing & Publishing	Senior Secured Term Loan (8.50%, due 8/08/2014)[3], [4]	5,794	5,222	5,284	0.7%
				5,222	**5,284**	**0.7%**
LHC Holdings Corp.[17]	Florida / Healthcare	Revolving Line of Credit $750 Commitment (9.00%, due 11/30/2012)[26], [27]				0.0%
		Senior Secured Term Loan A (9.00%, due 11/30/2012)[3], [4]	2,015	2,015	1,839	0.3%
		Senior Subordinated Debt (12.00% plus 2.50% PIK, due 5/31/2013)[3]	4,565	4,199	4,220	0.6%
		Membership Interest (125 units)		216	217	0.0%
				6,430	**6,276**	**0.9%**
			8,671	7,351	8,643	1.2%

Mac & Massey Holdings, LLC	Georgia / Food Products	Senior Subordinated Debt (10.00% plus 5.75% PIK, due 2/10/2013)				
		Membership Interest (250 units)		145	390	0.1%
				7,496	**9,033**	**1.3%**
Maverick Healthcare, LLC	Arizona / Healthcare	Second Lien Debt (12.50% plus 3.50% PIK, due 4/30/2014)(3)	13,122	13,122	13,247	1.9%
		Preferred Units (1,250,000 units)		1,252	2,025	0.2%
		Common Units (1,250,000 units)				0.0%
				14,374	**15,272**	**2.1%**
Miller Petroleum, Inc.	Tennessee / Oil & Gas Production	Warrants, Common Stock (2,208,772 warrants, expiring 5/04/2010 to 3/31/2015)(14)		150	1,244	0.2%
				150	**1,244**	**0.2%**
Northwestern Management Services, LLC	Florida / Healthcare	Revolving Line of Credit $1,000 Commitment (4.36%, due 12/13/2012)(26), (27)	350	350	350	0.0%
		Senior Secured Term Loan A (4.36%, due 12/13/2012)(3), (4)	4,309	3,516	3,578	0.5%
		Senior Secured Term Loan B (4.86%, due 12/13/2012)(3), (4)	1,219	904	956	0.1%
		Subordinated Secured Term Loan (12.00% plus 3.00%, due 6/13/2013)(3)	2,971	2,468	2,606	0.4%
		Common Stock (50 shares)		371	564	0.1%
				7,609	**8,054**	**1.1%**
Prince Mineral Company, Inc.	New York / Metal Services and Minerals	Junior Secured Term Loan (9.00%, due 12/21/2012)(4)	11,150	11,150	11,150	1.6%
		Senior Subordinated Debt (13.00% plus	12,260	1,420	12,260	1.7%

		2.00%, due 7/21/2013)				
				12,570	**23,410**	**3.3%**
Qualitest Pharmaceuticals, Inc.(17)	Alabama / Pharmaceuticals	Second Lien Debt (7.79%, due 4/30/2015)(3), (4)	12,000	11,955	12,000	1.7%
				11,955	**12,000**	**1.7%**

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			June 30, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 3 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Regional Management Corporation.	South Carolina / Financial Services	Second Lien Debt (12.00% plus 2.00% PIK, due 6/29/2012)[3]	$ 25,814	$ 25,814	$ 25,592	3.6%
				25,814	**25,592**	**3.6%**
Roll Coater Acquisition Corp	Indiana / Metal Services and Minerals	Subordinated Secured Debt (10.25%, due 9/30/2010)	6,268	6,102	6,082	0.9%
				6,102	**6,082**	**0.9%**
R-O-M Corporation	Missouri / Automobile	Revolving Line of Credit $1,750 Commitment (4.50%, due 2/08/2013)[26], [27]				0.0%
		Senior Secured Term Loan A (4.50%, due 2/08/2013)[3], [4]	4,640	4,025	4,571	0.6%
		Senior Secured Term Loan B (8.00%, due 5/08/2013)[3], [4]	7,251	7,251	7,078	1.0%
		Senior Subordinated Debt (12.00% plus 3.00% PIK due 8/08/2013)[3]	7,118	6,799	6,392	0.9%
				18,075	**18,041**	**2.5%**
Seaton Corp	Illinois / Business Services	Subordinated Secured (12.50% plus 2.00% PIK, due 3/14/2011)	12,296	12,060	12,132	1.7%
				12,060	**12,132**	**1.7%**

Shearer s Foods, Inc.	Ohio / Food Products	Junior Secured Debt (12.00% plus 3.00% PIK, due 3/31/2016)(3)	35,266	35,266	36,119	5.1%
		Membership Interest in Mistral Chip Holdings, LLC (2,000 units)(18)		2,560	6,136	0.9%
		Membership Interest in Mistral Chip Holdings, LLC 2 (595 units)(18)		762	1,825	0.2%
				38,588	**44,080**	**6.2%**
Skillsoft Public Limited Company	Ireland / Prepackaged Software	Subordinated Unsecured (11.125%, due 06/01/2018)	15,000	14,903	15,000	2.2%
				14,903	**15,000**	**2.2%**
Stryker Energy, LLC	Ohio / Oil & Gas Production	Subordinated Secured Revolving Credit Facility (12.00%, due 12/01/2012)(3), (4)	29,724	29,507	29,624	4.2%
		Overriding Royalty Interests(19)			2,768	0.4%
				29,507	**32,392**	**4.6%**
TriZetto Group(17)	California / Healthcare	Subordinated Unsecured Note (12.00% plus 1.50% PIK, due 10/01/2016)(3)	15,434	15,306	15,895	2.2%
				15,306	**15,895**	**2.2%**
Unitek(17)	Pennsylvania / Technical Services	Second Lien Debt (13.08%, due 12/31/2013)(3), (4)	11,500	11,387	11,615	1.7%
				11,387	**11,615**	**1.7%**
Wind River Resources Corp. and Wind River II Corp.	Utah / Oil & Gas Production	Senior Secured Note (13.00% plus 3.00% default interest, in non-accrual status effective 12/01/2008, due 7/31/2010)(4)	15,000	15,000	8,779	1.2%
		Net Profits Interest (5.00% payable on Equity distributions)(7)				0.0%
				15,000	**8,779**	**1.2%**

Total Non-control/Non-affiliate Investments (Level 3 Investments)	**476,441**	**477,417**	**67.1%**
Total Level 3 Portfolio Investments	**727,243**	**747,115**	**105.0%**

See notes to consolidated financial statements.

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			June 30, 2010			
Portfolio Company	**Locale / Industry**	**Investments[1]**	**Principal Value**	**Cost**	**Fair Value[2]**	**% of Net Assets**
LEVEL 1 PORTFOLIO INVESTMENTS:						
Non-control/Non-affiliate Investments (less than 5.00% of voting control)						
Allied Defense Group, Inc.	Virginia / Aerospace & Defense	Common Stock (10,000 shares)		$ 56	$ 38	0.0%
				56	**38**	**0.0%**
Dover Saddlery, Inc.	Massachusetts / Retail	Common Stock (30,974 shares)		63	97	0.0%
				63	**97**	**0.0%**
LyondellBasell Industries N.V.[22]	Netherlands / Chemical Company	Class A Common Stock (26,961 shares)		874	435	0.2%
		Class B Common Stock (49,421 shares)		523	798	0.0%
				1,397	**1,233**	**0.2%**
	Total Non-control/Non-affiliate Investments (Level 1 Investments)			**1,516**	**1,368**	**0.2%**
		Total Portfolio Investments		**728,759**	**748,483**	**105.2%**
SHORT TERM INVESTMENTS: Money Market Funds (Level 2 Investments)						
Fidelity Institutional Money Market Funds (Class I)		Government Portfolio		62,183	62,183	8.8%
Fidelity Institutional Money Market Funds (Class I)[3]		Government Portfolio		6,687	6,687	0.9%
Victory Government Money Market Funds				1	1	0.0%

Total Money Market Funds	**68,871**	**68,871**	**9.7%**
Total Investments	**797,630**	**817,354**	**114.9%**

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Endnote Explanations for the Consolidated Schedule of Investments as of December 31, 2010 and June 30, 2010

(1) The securities in which Prospect Capital Corporation (we , us or our) has invested were acquired in transactions that were exempt from registration under the Securities Act of 1933, as amended, or the Securities Act. These securities may be resold only in transactions that are exempt from registration under the Securities Act.

(2) Fair value is determined by or under the direction of our Board of Directors. As of December 31, 2010, two of our portfolio investments, Allied Defense Group, Inc. (Allied) and Dover Saddlery, Inc. (Dover) were publically traded and classified as Level 1 within the valuation hierarchy established by Accounting Standards Codification 820, *Fair Value Measurements and Disclosures* (ASC 820). As of June 30, 2010, three of our portfolio investments, Allied, Dover and LyondellBasel Industries N.V., were publically traded and classified as Level 1 within the valuation hierarchy established by ASC 820. As of December 31, 2010 and June 30, 2010, the fair value of our remaining portfolio investments was determined using significant unobservable inputs. ASC 820 classifies such inputs used to measure fair value as Level 3 within the valuation hierarchy. Our investments in money market funds are classified as Level 2. See Note 2 and Note 4 within the accompanying consolidated financial statements for further discussion.

(3) Security, or portion thereof, is pledged as collateral for the revolving credit facility (See Note 5). The market values of these investments at December 31, 2010 and June 30, 2010 were $607,021 and $512,244, respectively; they represent 57.8% and 62.7% of total investments at fair value, respectively. Prospect Capital Funding, LLC (See Note 1), our wholly-owned subsidiary, holds an aggregate market value of $546,425 and $451,648 of these investments as of December 31, 2010 and June 30, 2010, respectively.

(4) Security, or portion thereof, has a floating interest rate. Stated interest rate was in effect at December 31, 2010 and June 30, 2010.

(5) There are several entities involved in the Biomass investment. We own 100 shares of common stock in Worcester Energy Holdings, Inc. (WEHI), representing 100% of the issued and outstanding common stock. WEHI, in turn, owns 51 membership certificates in Biochips LLC (Biochips), which represents a 51% ownership stake.

We own 282 shares of common stock in Worcester Energy Co., Inc. (WECO), which represents 51% of the issued and outstanding common stock. We own directly 1,665 shares of common stock in Change Clean Energy Inc. (CCEI), f/k/a Worcester Energy Partners, Inc., which represents 51% of the issued and outstanding common stock and the remaining 49% is owned by WECO. CCEI owns 100 shares of common stock in Precision Logging and Landclearing, Inc. (Precision), which represents 100% of the issued and outstanding common stock.

During the quarter ended March 31, 2009, we created two new entities in anticipation of the foreclosure proceedings against the co-borrowers (WECO, CCEI and Biochips) Change Clean Energy Holdings, Inc. (CCEHI) and DownEast Power Company, LLC (DEPC). We own 1,000 shares of CCEHI, representing 100% of the issued and outstanding stock, which in turn, owns a 100% of the membership interests in DEPC.

On March 11, 2009, we foreclosed on the assets formerly held by CCEI and Biochips with a successful credit bid of $6,000 to acquire the assets. As a result of the foreclosure our direct ownership in CCEI increased to 3,265 shares of common stock. The assets were subsequently assigned to DEPC. WECO, CCEI and

Biochips are joint borrowers on the term note issued to Prospect Capital. Effective July 1, 2008, this loan was placed on non-accrual status. Biochips, WECO, CCEI, Precision and WEHI currently have no material operations and no significant assets. As of June 30, 2009, our Board of Directors assessed a fair value of $0 for all of these equity positions and the loan position. We determined that the impairment of both CCEI and CCEHI as of June 30, 2009 was other than temporary and recorded a realized loss for the amount that the amortized cost exceeds the fair value at June 30, 2009. Our Board of Directors set value at zero for the CCEHI investment as of December 31, 2010 and June 30, 2010.

(6) During the quarter ended December 31, 2009, we created two new entities, Coalbed Inc. and Coalbed LLC, to foreclose on the outstanding senior secured loan and assigned rights and interests of Conquest Cherokee, LLC (Conquest), as a result of the deterioration of Conquest s financial performance and inability to service debt payments. We own 1,000 shares of common stock in Coalbed Inc., representing 100% of the issued and outstanding common stock. Coalbed Inc., in turn owns 100% of the membership interest in Coalbed LLC.

On October 21, 2009, Coalbed LLC foreclosed on the loan formerly made to Conquest. On January 19, 2010, as part of the Manx rollup, the Coalbed LLC assets and loan was assigned to Manx, the holding company. As of December 31, 2010, our Board of Directors assessed a fair value of $975 for the loan position in Coalbed LLC, a decrease of $439 from the fair value as of June 30, 2010.

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Endnote Explanations for the Consolidated Schedule of Investments as of December 31, 2010 and June 30, 2010 (Continued)

(7) In addition to the stated returns, the net profits interest held will be realized upon sale of the borrower or a sale of the interests.

(8) Gas Solutions Holdings, Inc. is a wholly-owned investment of us.

(9) Entity was formed as a result of the debt restructuring of ESA Environmental Specialist, Inc. In early 2009, we foreclosed on the two loans on non-accrual status and purchased the underlying personal and real property. We own 1,000 shares of common stock in The Healing Staff (THS), f/k/a Lisamarie Fallon, Inc. representing 100% ownership. We own 1,500 shares of Vets Securing America, Inc. (VSA), representing 100% ownership. VSA is a holding company for the real property of Integrated Contract Services, Inc. (ICS) purchased during the foreclosure process.

(10) Loan is with THS an affiliate of ICS.

(11) On June 30, 2008, we consolidated our holdings in four coal companies into Yatesville Coal Holdings, Inc. (Yatesville), and consolidated the operations under one management team. As part of the transaction, the debt that we held of C&A Construction, Inc. (C&A), Genesis Coal Corp. (Genesis), North Fork Collieries LLC (North Fork) and Unity Virginia Holdings LLC (Unity) were exchanged for newly issued debt from Yatesville, and our ownership interests in C&A, E&L Construction, Inc. (E&L), Whymore Coal Company Inc. (Whymore) and North Fork were exchanged for 100% of the equity of Yatesville. This reorganization allows for a better utilization of the assets in the consolidated group.

At December 31, 2010 and at June 30, 2010, Yatesville owned 100% of the membership interest of North Fork. In addition, Yatesville held a $9,325 note receivable from North Fork as of those two respective dates.

At December 31, 2010 and at June 30, 2010, we owned 96% and 87%, respectively, of the common stock of Genesis and held a note receivable of $20,897 as of those two respective dates.

Yatesville held a note receivable of $4,261 from Unity at December 31, 2010 and at June 30, 2010.

There are several entities involved in Yatesville s investment in Whymore at June 30, 2009. As of June 30, 2009, Yatesville owned 10,000 shares of common stock or 100% of the equity and held a $14,973 senior secured debt receivable from C&A, which owns the equipment. Yatesville owned 10,000 shares of common stock or 100% of the equity of E&L, which leases the equipment from C&A, employs the workers, is listed as the operator with the Commonwealth of Kentucky, mines the coal, receives revenues and pays all operating expenses. Yatesville owned 4,900 shares of common stock or 49% of the equity of Whymore, which applies for and holds permits on behalf of E&L. Yatesville also owned 4,285 Series A convertible preferred shares in each of C&A, E&L and Whymore. Whymore and E&L are guarantors under the C&A credit agreement with Yatesville.

In August 2009, Yatesville sold its 49% ownership interest in the common shares of Whymore to the 51% holder of the Whymore common shares (Whymore Purchaser). All reclamation liability was transferred to the Whymore Purchaser. In September 2009, Yatesville completed an auction for all of its equipment.

Yatesville currently has no material operations. During the quarter ended December 31, 2009, our Board of Directors determined that the impairment of Yatesville was other than temporary and we recorded a realized loss for the amount that the amortized cost exceeds the fair value. Our Board of Directors set the value of the remaining Yatesville investment at zero and $808 as of December 31, 2010 and June 30, 2010, respectively.

(12) On January 19, 2010, we modified the terms of our senior secured debt in AEH and Coalbed in conjunction with the formation of Manx Energy, a new entity consisting in the assets of AEH, Coalbed and Kinley Exploration. The assets of the three companies were brought under new common management. We funded $2,800 at closing to Manx to provide for working capital. A portion of our loans to AEH and Coalbed was exchanged for Manx preferred equity, while our AEH equity interest was converted into Manx common stock. There was no change to fair value at the time of restructuring, and we continue to fully reserve any income accrued for Manx.

(13) On a fully diluted basis represents 10.00% of voting common shares.

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PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
CONSOLIDATED SCHEDULE OF INVESTMENTS (CONTINUED)
December 31, 2010 and June 30, 2010
(in thousands, except share data)

Endnote Explanations for the Consolidated Schedule of Investments as of December 31, 2010 and June 30, 2010 (Continued)

(14) Total common shares outstanding of 38,281,253 as of December 7, 2010 from Miller Petroleum, Inc. s (Miller) Quarterly Report on Form 10-Q filed on December 10, 2010. Total common shares outstanding of 33,389,383 as of July 22, 2010 from Miller s Annual Report on Form 10-K filed on July 28, 2010 as applicable to our June 30, 2010 reporting date.

(15) A portion of the positions listed were issued by an affiliate of the portfolio company.

(16) We own 99.9999% of AGC/PEP, LLC. AGC/PEP, LLC owns 2,037.65 out of a total of 83,818.69 shares (including 5,111 vested and unvested management options) of American Gilsonite Holding Company which owns 100% of American Gilsonite Company.

(17) Syndicated investment which had been originated by another financial institution and broadly distributed.

(18) At December 31, 2010 and June 30, 2010, Mistral Chip Holdings, LLC owns 44,800 shares of Chip Holdings, Inc. and Mistral Chip Holdings 2, LLC owns 11,975 shares in Chip Holdings, Inc. Chip Holdings, Inc. is the parent company of Shearer s Foods, Inc. and has 67,936 shares outstanding before adjusting for management options.

(19) The overriding royalty interests held receive payments at the stated rates based upon operations of the borrower.

(20) On December 31, 2009, we sold our investment in Aylward Enterprises, LLC. AWCNC, LLC is the remaining holding company with zero assets. Our remaining outstanding debt after the sale was written off on December 31, 2009 and no value has been assigned to the equity position as of December 31, 2010 and June 30, 2010.

(21) We own 100% of Freedom Marine Holding, Inc., which owns 82.94% of the common units of Freedom Marine Services LLC.

(22) We own warrants to purchase 33,750 shares of common stock in Metal Buildings Holding Corporation (Metal Buildings), the former holding company of Borga, Inc. Metal Buildings Holding Corporation owned 100% of Borga, Inc.

On March 8, 2010, we foreclosed on the stock in Borga, Inc. that was held by Metal Buildings, obtaining 100% ownership of Borga, Inc.

(23) We own 100% of C&J Cladding Holding Company, Inc., which owns 40% of the membership interests in C&J Cladding, LLC.

(24) On January 1, 2010, we restructured our senior secured and bridge loans investment in Iron Horse Coiled Tubing, Inc. (Iron Horse) and we reorganized Iron Horse s management structure. The senior secured loan and bridge loan were replaced with three new tranches of senior secured debt. From June 30, 2009 to December 31, 2010, our total ownership of Iron Horse decreased from 80.0% to 70.4%, respectively, and we will continue to transfer ownership interests to Iron Horse s management as they repay our outstanding debt.

As of December 31, 2010 and June 30, 2010, our Board of Directors assessed a fair value in Iron Horse of $18,993 and $12,054, respectively.

(25) We own 2,800,000 units in Class A Membership Interests and 372,094 units in Class A-1 Membership Interests.

(26) Undrawn committed revolvers incur a 0.50% commitment fee. As of December 31, 2010 and June 30, 2010, we have $11,507 and $10,382 of undrawn revolver commitments to our portfolio companies, respectively.

(27) Stated interest rates are based on December 31, 2010 and June 30, 2010 one month LIBOR rates plus applicable spreads based on the respective credit agreements. Interest rates are subject to change based on actual elections by the borrower for a LIBOR rate contract or Base Rate contract when drawing on the revolver.

PROSPECT CAPITAL CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010
(Unaudited)
(In thousands, except share and per share data)

Note 1. Organization

References herein to we , us or our refer to Prospect Capital Corporation and its subsidiary unless the contex specifically requires otherwise.

We were formerly known as Prospect Energy Corporation, a Maryland corporation. We were organized on April 13, 2004 and were funded in an initial public offering (IPO), completed on July 27, 2004. We are a closed-end investment company that has filed an election to be treated as a Business Development Company (BDC), under the Investment Company Act of 1940 (the 1940 Act). As a BDC, we have qualified and have elected to be treated as a regulated investment company (RIC), under Subchapter M of the Internal Revenue Code. We invest primarily in senior and subordinated debt and equity of companies in need of capital for acquisitions, divestitures, growth, development, project financings, recapitalizations, and other purposes.

On May 15, 2007, we formed a wholly-owned subsidiary, Prospect Capital Funding, LLC, a Delaware limited liability company, for the purpose of holding certain of our loan investments in the portfolio which are used as collateral for our credit facility.

Note 2. Significant Accounting Policies

The following are significant accounting policies consistently applied by us:

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and pursuant to the requirements for reporting on Form 10-Q and Regulation S-X. The financial results of our portfolio investments are not consolidated in the financial statements.

Use of Estimates

The preparation of GAAP financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reported period. Changes in the economic environment, financial markets, creditworthiness of our portfolio companies and any other parameters used in determining these estimates could cause actual results to differ, and these differences could be material.

Basis of Consolidation

Under the 1940 Act rules, the regulations pursuant to Article 6 of Regulation S-X and the American Institute of Certified Public Accountants Audit and Accounting Guide for Investment Companies, we are precluded from consolidating any entity other than another investment company or an operating company which provides substantially all of its services and benefits to us. Our financial statements include our accounts and the accounts of Prospect Capital Funding, LLC, our only wholly-owned, closely-managed subsidiary that is also an investment company. All intercompany balances and transactions have been eliminated in consolidation.

Investment Classification

We are a non-diversified company within the meaning of the 1940 Act. We classify our investments by level of control. As defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling influence over the management or policies of a company. Control is generally deemed to exist when a company or individual possesses or has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an investee company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to exist through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more of the outstanding voting securities of another person.

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Investments are recognized when we assume an obligation to acquire a financial instrument and assume the risks for gains or losses related to that instrument. Investments are derecognized when we assume an obligation to sell a financial instrument and forego the risks for gains or losses related to that instrument. Specifically, we record all security transactions on a trade date basis. Investments in other, non-security financial instruments are recorded on the basis of subscription date or redemption date, as applicable. Amounts for investments recognized or derecognized but not yet settled are reported as receivables for investments sold and payables for investments purchased, respectively, in the Consolidated Statements of Assets and Liabilities.

Investment Risks

The Company s investments are subject to a variety of risks. Those risks include the following:

Market Risk

Market risk represents the potential loss that can be caused by a change in the fair value of the financial instrument.

Credit Risk

Credit risk represents the risk that the Company would incur if the counterparties failed to perform pursuant to the terms of their agreements with the Company.

Liquidity Risk

Liquidity risk represents the possibility that the Company may not be able to rapidly adjust the size of its positions in times of high volatility and financial stress at a reasonable price.

Interest Rate Risk

Interest rate risk represents a change in interest rates, which could result in an adverse change in the fair value of an interest-bearing financial instrument.

Prepayment Risk

Most of the Company s debt investments allow for prepayment of principal without penalty. Downward changes in interest rates may cause prepayments to occur at a faster than expected rate, thereby effectively shortening the maturity of the security and making the security less likely to be an income producing instrument.

Investment Valuation

Our Board of Directors has established procedures for the valuation of our investment portfolio. These procedures are detailed below.

Investments for which market quotations are readily available are valued at such market quotations.

For most of our investments, market quotations are not available. With respect to investments for which market quotations are not readily available or when such market quotations are deemed not to represent fair value, our Board of Directors has approved a multi-step valuation process each quarter, as described below:

1) Each portfolio company or investment is reviewed by our investment professionals with the independent valuation firm;

2) the independent valuation firm engaged by our Board of Directors conducts independent appraisals and makes their own independent assessment;

3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation by our Investment Adviser within the valuation range presented by the independent valuation firm; and

4) the Board of Directors discusses valuations and determines the fair value of each investment in our portfolio in good faith based on the input of our Investment Adviser, the respective independent valuation firm and the audit committee.

Investments are valued utilizing a market approach, an income approach, a liquidation approach, or a combination of approaches, as appropriate. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities (including a business). The income approach uses valuation techniques to convert future amounts (for example, cash flows or earnings) to a single present value amount (discounted) calculated based on an appropriate discount rate. The measurement is based on the net present value indicated by current market expectations about those future amounts. In following these approaches, the types of factors that we may take into account in fair value pricing our investments include, as relevant: available current market data, including relevant and applicable market trading and transaction comparables, applicable market yields and multiples, security covenants, call protection provisions, information rights, the nature and realizable value of any collateral, the portfolio company s ability to make payments, its earnings and discounted cash flows, the markets in which the portfolio company does business, comparisons of financial ratios of peer companies that are public, M&A comparables, the principal market and enterprise values, among other factors.

In September 2006, the Financial Accounting Standards Board (FASB) issued ASC 820, *Fair Value Measurements and Disclosures* (ASC 820). ASC 820 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. We adopted ASC 820 on a prospective basis beginning in the quarter ended September 30, 2008.

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

Level 1: Quoted prices in active markets for identical assets or liabilities, accessible by us at the measurement date.

Level 2: Quoted prices for similar assets or liabilities in active markets, or quoted prices for identical or similar assets or liabilities in markets that are not active, or other observable inputs other than quoted prices.

Level 3: Unobservable inputs for the asset or liability.

In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to each investment. The changes to GAAP from the application of ASC 820 relate to the definition of fair value, framework for measuring fair value, and the expanded disclosures about fair value measurements. ASC 820 applies to fair value measurements already required or permitted by other standards. In accordance with ASC 820, the fair value of our investments is defined as the price that we would receive upon selling an investment in an orderly transaction to an independent buyer in the principal or most advantageous market in which that investment is transacted.

In April 2009, the FASB issued ASC Subtopic 820-10-65, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* (ASC 820-10). This update provides further clarification for ASC 820 in markets that are not active and provides additional guidance for determining when the volume of trading level of activity for an asset or liability has significantly decreased and for identifying circumstances that indicate a transaction is not orderly. ASC 820-10-65 is effective for interim and annual reporting periods ending after June 15, 2009. The adoption of ASC 820-10-65 for the three and six months ended December 31, 2010 and 2009, did not have any effect on our net asset value, financial position or results of operations as there was no change to the fair value measurement principles set forth in ASC 820.

Valuation of Other Financial Assets and Financial Liabilities

In February 2007, FASB issued ASC Subtopic 820-10-05-1, *The Fair Value Option for Financial Assets and Financial Liabilities* (ASC 820-10-05-1). ASC 820-10-05-1 permits an entity to elect fair value as the initial and subsequent measurement attribute for many of assets and liabilities for which the fair value option has been elected and similar assets and liabilities measured using another measurement attribute. We adopted this statement on July 1, 2008 and have elected not to value other assets and liabilities at fair value as would be permitted by ASC 820-10-05-1.

Senior Convertible Notes

We have recorded the Senior Convertible Notes (See Note 6) at their contractual amounts. The Senior Convertible Notes were analyzed for any features that would require its accounting to be bifurcated and they were determined to be immaterial.

Revenue Recognition

Realized gains or losses on the sale of investments are calculated using the specific identification method.

Interest income, adjusted for amortization of premium and accretion of discount, is recorded on an accrual basis. Origination, closing and/or commitment fees associated with investments in portfolio companies are accreted into interest income over the respective terms of the applicable loans. Accretion of such purchase discounts or premiums is calculated by the effective interest method as of the purchase date and adjusted only for material amendments or prepayments. Upon the prepayment of a loan or debt security, any prepayment penalties and unamortized loan origination, closing and commitment fees are recorded as interest income. The purchase discount for portfolio investments acquired from Patriot was determined based on the difference between par value and fair market value as of December 2, 2009, and will continue to accrete until maturity or repayment of the respective loans.

Dividend income is recorded on the ex-dividend date.

Structuring fees and similar fees are recognized as income as earned, usually when paid. Structuring fees, excess deal deposits, net profits interests and overriding royalty interests are included in other income.

Loans are placed on non-accrual status when there is reasonable doubt that principal or interest will not be collected in accordance with the terms of the investment. Accrued interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management s judgment. Non-accrual loans are restored to accrual status when past due principal and interest is paid and in management s judgment, are likely to remain current.

Federal and State Income Taxes

We have elected to be treated as a regulated investment company and intend to continue to comply with the requirements of the Internal Revenue Code of 1986 (the Code), applicable to regulated investment companies. We are required to distribute at least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all of our investment company taxable income and net capital gain to stockholders; therefore, we have made no provision for income taxes. The character of income and gains that we will distribute is determined in accordance with income tax regulations that may differ from GAAP. Book and tax basis differences relating to stockholder dividends and distributions and other permanent book and tax differences are reclassified to paid-in capital.

If we do not distribute (or are not deemed to have distributed) at least 98% of our annual taxable income in the calendar year it is earned, we will generally be required to pay an excise tax equal to 4% of the amount by which 98% of our annual taxable income exceeds the distributions from such taxable income for the year. To the extent that we determine that our estimated current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable income, we accrue excise taxes, if any, on estimated excess taxable income as taxable income is earned using an annual effective excise tax rate. The annual effective excise tax rate is determined by dividing the estimated annual excise tax by the estimated annual taxable income.

We adopted FASB ASC 740, *Income Taxes* (ASC 740). ASC 740 provides guidance for how uncertain tax positions should be recognized, measured, presented, and disclosed in the financial statements. ASC 740 requires the evaluation of tax positions taken or expected to be taken in the course of preparing our tax returns to determine whether the tax positions are more-likely-than-not of being sustained by the applicable tax authority. Tax positions not deemed to meet the more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption of ASC 740 was applied to all open tax years as of July 1, 2007. The adoption of ASC 740 did not have an effect on our net asset value, financial condition or results of operations as there was no liability for unrecognized tax benefits and no change to our beginning net asset value. As of December 31, 2010 and for the three and six months then ended, we did not have a liability for any unrecognized tax benefits. Management s determinations regarding ASC 740 may be subject to review and adjustment at a later date based upon factors including, but not limited to, an on-going analysis of tax laws, regulations and interpretations thereof.

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be paid as a monthly dividend or distribution is approved by our Board of Directors quarterly and is generally based upon our management s estimate of our earnings for the quarter. Net realized capital gains, if any, are distributed at least annually.

Financing Costs

We record origination expenses related to our credit facility and the Senior Convertible Notes as deferred financing costs. These expenses are deferred and amortized as part of interest expense using the straight-line method for our revolving credit facility and the effective interest method for our Senior Convertible Notes, over the respective stated life.

We record registration expenses related to shelf filings as prepaid assets. These expenses consist principally of Securities and Exchange Commission (SEC) registration fees, legal fees and accounting fees incurred. These prepaid assets will be charged to capital upon the receipt of an equity offering proceeds or charged to expense if no offering completed.

Guarantees and Indemnification Agreements

We follow FASB ASC 460, *Guarantees* (ASC 460). ASC 460 elaborates on the disclosure requirements of a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also requires a guarantor to recognize, at the inception of a guarantee, for those guarantees that are covered by ASC 460, the fair value of the obligation undertaken in issuing certain guarantees. ASC 460 did not have a material effect on the financial statements.

Per Share Information

Net increase or decrease in net assets resulting from operations per common share are calculated using the weighted average number of common shares outstanding for the period presented. In accordance with ASC 946, *Financial Services Investment Companies*, convertible securities are not considered in the calculation of net assets per share.

Recent Accounting Pronouncements

In June 2009, the FASB issued ASC 860, *Accounting for Transfers of Financial Assets an amendment to FAS 140* (ASC 860). ASC 860 improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets: the effects of a transfer on its financial position, financial performance, and cash flows: and a transferor s continuing involvement, if any, in transferred financial assets. ASC 860 is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. The adoption of this standard had no effect on our results of operation or our financial position.

In June 2009, the FASB issued ASC 810, *Consolidation* (ASC 810). ASC 810 is intended to (1) address the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities, as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, and (2) constituent concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accounting and disclosures under the Interpretation do not always provide timely and useful information about an enterprise s involvement in a variable interest entity. ASC 810 is effective as of the beginning of our first annual reporting period that begins after November 15, 2009. The adoption of this standard had no effect on our results of operation or our financial position.

In January 2010, the FASB issued Accounting Standards Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASC 2010-06). ASU 2010-06 amends ASC 820-10 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers disclosures about postretirement benefit plan assets. ASU 2010-06 is effective December 15, 2009, except for the disclosure about purchase, sales, issuances and settlements in the roll forward of activity in level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. Our management does not believe that the adoption of the amended guidance in ASC 820-10 will have a significant effect on our financial statements.

In February 2010, the FASB issued Accounting Standards Update 2010-10, *Consolidation (Topic 810) Amendments for Certain Investments Funds* (ASU 2010-10), which defers the application of the consolidation guidance in ASC 810 for certain investments funds. The disclosure requirements continue to apply to all entities. ASU 2010-10 is effective as of the beginning of the first annual period that begins after November 15, 2009 and for interim periods within that first annual period. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-21, *Accounting for Technical Amendments to Various SEC Rules and Schedules* (ASU 2010-21). ASU 2010-21 amends various SEC paragraphs pursuant to the issuance of Release No. 33-9026: Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-22, *Accounting for Various Topics Technical Corrections to SEC Paragraphs* (ASU 2010-22). ASU 2010-22 amends various SEC paragraphs based on external comments received and the issuance of Staff Accounting Bulletin (SAB) 112, which amends or rescinds portions of certain SAB topics. The adoption of this standard had no effect on our results of operation or our financial position.

In December 2010, the FASB issued Accounting Standards Update 2010-29, *Business Combinations (Topic 805) Disclosure of Supplementary Pro Forma Information for Business Combinations (a consensus of the FASM Emerging Issues Task Force* (ASU 2010-29). ASU 2010-29 addresses diversity in practice about the interpretation of pro forma revenue and earnings disclosure requirements for business combinations. The amended guidance in ASU 2010-29 specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior reporting period only. This standard also expands the supplemental pro forma disclosures under ASC 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in ASU 2010-29 are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010, with early adoption permitted. We do not believe that the adoption of the amended guidance in ASU 2010-29 will have a significant effect on our financial statements

Note 3. Patriot Acquisition

On December 2, 2009, we acquired the outstanding shares of Patriot Capital Funding, Inc. (Patriot) common stock for $201,083. Under the terms of the merger agreement, Patriot common shareholders received 0.363992 shares of our common stock for each share of Patriot common stock, resulting in 8,444,068 shares of common stock being issued by us. In connection with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

On December 2, 2009, Patriot made a final dividend payment equal to its undistributed net ordinary income and capital gains of $0.38 per share. In accordance with a recent IRS revenue procedure, the dividend was paid 10% in cash and 90% in newly issued shares of Patriot s common stock. The exchange ratio was adjusted to give effect to the final income distribution.

The merger has been accounted for as an acquisition of Patriot by Prospect Capital Corporation (Prospect) in accordance with acquisition method of accounting as detailed in ASC 805, *Business Combinations* (ASC 805). The fair value of the consideration paid was allocated to the assets acquired and liabilities assumed based on their fair values as the date of acquisition. As described in more detail in ASC 805, goodwill, if any, would have been recognized as of the acquisition date, if the consideration transferred exceeded the fair value of identifiable net assets acquired. As of the acquisition date, the fair value of the identifiable net assets acquired exceeded the fair value of the consideration transferred, and we recognized the excess as a gain. A preliminary gain of $5,714 was recorded by Prospect in the quarter ended December 31, 2009 related to the acquisition of Patriot, which was revised in the fourth quarter of Fiscal 2010 to $7,708, when we settled severance accruals related to certain members of Patriot s top management and finalized during the first quarter of Fiscal 2011, to $8,632, when we settled the remaining severance accruals related to the last two members of Patriot s top management. Under ASC 805, the adjustments to our preliminary estimate were reflected in the three months ended December 31, 2009 (See Note 13). The acquisition of Patriot was negotiated in July 2009 with the purchase agreement being signed on August 3, 2009. Between July 2009 and December 2, 2009, our valuation of certain of the investments acquired from Patriot increased due to market improvement, which resulted in the recognition of the gain at closing.

Purchase Price Allocation

The purchase price has been allocated to the assets acquired and the liabilities assumed based on their estimated fair values as summarized in the following table:

Cash (to repay Patriot debt)	$	107,313
Cash (to fund purchase of restricted stock from former Patriot employees)		970
Common stock issued [(1)]		92,800
Total purchase price		201,083
Assets acquired:		
Investments [(2)]		207,126
Cash and cash equivalents		1,697
Other assets		3,859
Assets acquired		212,682
Other liabilities assumed		(2,967)
Net assets acquired		209,715
Gain on Patriot acquisition [(3)]	$	8,632

(1) The value of the shares of common stock exchanged with the Patriot common shareholders was based upon the closing price of our common stock on December 2, 2009, the price immediately prior to the closing of the transaction.

(2) The fair value of Patriot s investments were determined by the Board of Directors in conjunction with an independent valuation agent. This valuation resulted in a purchase price which was $98,150 below the amortized cost of such investments. For those assets which are performing, Prospect will record the accretion to par value in interest income over the remaining term of the investment.

(3) The gain has been determined after the final payments of certain liabilities have been settled.

Condensed Statement of Net Assets Acquired

The following condensed statement of net assets acquired reflects the values assigned to Patriot s net assets as of the acquisition date, December 2, 2009.

Investment securities	$ 207,126
Cash and cash equivalents	1,697
Other assets	3,859
Total assets	212,682
Other liabilities	(2,967)
Final fair value of net assets acquired	$ 209,715

The following unaudited pro forma condensed combined financial information does not purport to be indicative of actual financial position or results of our operations had the Patriot acquisition actually been consummated as of July 1, 2009. Certain one-time charges have been eliminated. The pro forma adjustments reflecting the allocation of the purchase price of Patriot and the gain of $8,632 recognized on the Patriot Acquisition have been eliminated. Management has realized net operating synergies from this transaction. The pro forma condensed combined financial information does not reflect the potential impact of these synergies and does not reflect any impact of additional accretion which would have been recognized on the transaction, except for that which was recorded after the transaction was consummated on December 2, 2009

	For the Three Months Ended December 31, 2009	For the Six Months Ended December 31, 2009
Total Investment Income	$ 28.449	$ 58,017
Net Investment Income	11,431	24,934
Net Decrease in Net Assets Resulting from Operations	(22,320)	(33,396)
Net Decrease in Net Assets Resulting from Operations per share	$ (0.34)	$ (0.54)

Note 4. Portfolio Investments

At December 31, 2010, we had invested in 58 long-term portfolio investments, which had an amortized cost of $886,068 and a fair value of $918,221 and at June 30, 2010, we had invested in 58 long-term portfolio investments, which had an amortized cost of $728,759 and a fair value of $748,483.

As of December 31, 2010, we own controlling interests in AIRMALL USA, Inc., Ajax Rolled Ring & Machine, Inc., AWCNC, LLC, Borga, Inc. (Borga), C&J Cladding, LLC, Change Clean Energy Holdings, Inc., Fischbein, LLC, Freedom Marine Services LLC (Freedom Marine), Gas Solutions Holdings, Inc. (GSHI), Integrated Contract Services, Inc. (ICS), Iron Horse Coiled Tubing, Inc. (Iron Horse), Manx Energy, Inc. (Manx), NRG Manufacturing, Inc., Nupla Corporation (Nupla), R-V Industries, Inc. and Yatesville Coal Holdings, Inc. (Yatesville). We also own an affiliated interest in Biotronic NeuroNetwork, Boxercraft Incorporated, KTPS Holdings, LLC, Smart, LLC, and Sport Helmets Holdings, LLC.

The fair values of our portfolio investments as of December 31, 2010 disaggregated into the three levels of the ASC 820 valuation hierarchy are as follows:

	Quoted Prices in Active Markets for Identical Securities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Investments at fair value				
Control investments	$	$	$ 264,228	$ 264,228
Affiliate investments			74,709	74,709
Non-control/Non-affiliate investments	114		579,170	579,284
	114		918,107	918,221
Investments in money market funds		132,194		132,194
Total assets reported at fair value	$ 114	$ 132,194	$ 918,107	$ 1,050,415

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The aggregate values of Level 3 portfolio investments changed during the six months ended December 31, 2010 as follows:

	Fair Value Measurements Using Unobservable Inputs (Level 3)			
	Control Investments	Affiliate Investments	Non-Control/ Non-Affiliate Investments	Total
Fair value as of June 30, 2010	$ 195,958	$ 73,740	$ 477,417	$ 747,115
Total realized (loss) gain, net	(803)		5,416	4,613
Change in unrealized (depreciation) appreciation	17,893	236	(4,460)	13,669(1)
Net realized and unrealized gain (loss)	17,090	236	956	18,282
Purchases of portfolio investments	58,198	1,329	207,142	266,669
Payment-in-kind interest	1,639	718	3,660	6,017
Accretion of purchase discount	66	1,276	4,618	5,960
Repayments and sales of portfolio investments	(8,723)	(2,590)	(114,623)	(125,936)
Transfers within Level 3				
Transfers in (out) of Level 3				
Fair value as of December 31, 2010	$ 264,228	$ 74,709	$ 579,170	$ 918,107

(1) Relates to assets held at December 31, 2010

The aggregate values of Level 3 portfolio investments changed during the six months ended December 31, 2009 as follows:

	Fair Value Measurements Using Unobservable Inputs (Level 3)			
	Control Investments	Affiliate Investments	Non-Control/ Non-Affiliate Investments	Total
Fair value as of June 30, 2009	$ 206,332	$ 32,254	$ 308,582	$ 547,168
Total realized loss	(51,229)			(51,229)
Change in unrealized appreciation (depreciation)	7,390	(283)	(7,209)	(102)(1)
	(43,839)	(283)	(7,209)	(51,331)
Assets acquired in the Patriot acquisition	10,534	36,400	160,073	207,007
Purchases of portfolio investments	5,854		1,467	7,321
Payment-in-kind interest	725	193	1,141	2,059
Accretion of purchase discount	3,343	281	3,046	6,670
Repayments and sales of portfolio investments	(8,733)	(2,516)	(59,628)	(70,877)
Transfers within Level 3	17,682	150	(17,832)	
Transfers in (out) of Level 3				
Fair value as of December 31, 2009	$ 191,898	$ 66,479	$ 389,640	$ 648,017

(1) Relates to assets held at December 31, 2009

At December 31, 2010, eight loan investments were on non-accrual status: Borga, Deb Shops, Inc. (Deb Shops), Freedom Marine, ICS, Nupla, Manx, Wind River Resources Corp. and Wind River II Corp. (Wind River), and Yatesville. At June 30, 2010, nine loan investments were also on non-accrual status: Borga, Deb Shops, ICS, Iron Horse, Nupla, Manx, Sidump r Trailer Company, Inc., Wind River and Yatesville. The loan principal of these loans amounted to $88,834 and $163,653 as of December 31, 2010 and June 30, 2010, respectively. The fair values of these investments represent approximately 2.3% and 5.6% of our net assets as of December 31, 2010 and June 30, 2010, respectively. For the three months ended December 31, 2010 and December 31, 2009, the income foregone as a result of not accruing interest on non-accrual debt investments amounted to $3,495 and $8,052, respectively. For the six months ended December 31, 2010 and December 31, 2009, the income foregone as a result of not accruing interest on non-accrual debt investments amounted to $6,568 and $12,510, respectively. At December 31, 2010, we held one asset on accrual status for which the payment of interest was past-due more than 90 days, H&M Oil and Gas, LLC. The principal balance of this loan is $60,019 and the accrued interest receivable is $3,952 at December 31, 2010. The past due interest of $3,952 was collected in full on January 18, 2011. We expect full repayment of principal and interest on this loan.

GSHI has indemnified us against any legal action arising from its investment in Gas Solutions, LP. We have incurred approximately $2,093 from the inception of the investment in GSHI through December 31, 2009 for fees associated with a legal action, and GSHI has reimbursed us for the entire amount. There were no such legal fees incurred or reimbursed for the three and six months ended December 31, 2010 and December 31, 2009. Additionally, certain other expenses incurred by us which are attributable to GSHI have been reimbursed by GSHI and are reflected as dividend income: control investments in the Consolidated Statements of Operations. For the three months ended December 31, 2010 and December 31, 2009, such reimbursements totaled as $2,100 and $800, respectively. For the six months ended December 31, 2010 and December 31, 2009, such reimbursements totaled as $3,850 and $2,031, respectively.

On December 3, 2010, we exercised our warrants in Miller Petroleum, Inc (Miller) and received 2,013,814 shares of Miller common stock. On December 27, 2010, we sold 1,397,510 these shares at $3.95 net proceeds per share, realizing a gain of $5,415. The remaining 616,304 shares of Miller common stock were sold on January 10, 2010.

During the three months ended December 31, 2009, we discontinued operations at Yatesville. As of December 31, 2009, consistent with the decision to discontinue operations, we determined that the impairment of Yatesville was other-than-temporary and recorded a realized loss of $51,228 for the amount that the amortized cost exceeded the fair market value. As of December 31, 2010 and June 30, 2010, Yatesville is valued at zero and $808, respectively.

The original cost basis of debt placements and equity securities acquired, including follow-on investments for existing portfolio companies, totaled $138,070 and $210,438 during the three months ended December 31, 2010 and December 31, 2009, respectively. These placements and acquisitions totaled $275,867 and $216,506 during the six months ended December 31, 2010 and December 31, 2009, respectively. The $210,438 and $216,506 for the three and six months ended December 31, 2009, respectively, include $207,126 of portfolio investments acquired from Patriot.

Debt repayments and sales of equity securities with a cost basis of $62,915 and $45,494 were received during the three months ended December 31, 2010 and December 31, 2009, respectively. These repayments and sales amounted to $131,063 and $69,735 during the six months ended December 31, 2010 and December 31, 2009, respectively.

During the three and six months ended December 31, 2010, we recognized $1,305 and $5,353, respectively, of interest income due to purchase discount accretion from the assets acquired from Patriot. Included in the $5,353 for the six months ended December 31, 2010, is $1,116 of accelerated accretion resulting from the repayment of Impact Products, LLC. We also recapitalized our debt investment in Northwestern Management Services, LLC. The $20,000 loan was issued at market terms comparable to other industry transactions. In accordance with ASC 320-20-35 the cost basis of the new loan was recorded at par value, which precipitated the acceleration of $1,612 of original purchase discount from the loan repayment which was recognized as interest income. There was no accelerated accretion recorded during the quarter ended December 31, 2010.

During the period from the acquisition of Patriot on December 2, 2009 to December 31, 2009, we recognized $7,495 of interest income from the assets acquired from Patriot. Included in this amount is $4,560 resulting from the acceleration of purchase discounts from the early repayments of three loans, three revolving lines of credit and the sale of one investment position.

Note 5. Revolving Credit Agreements

On June 6, 2007, we closed on a $200,000 three-year revolving credit facility (as amended on December 31, 2007) with Rabobank Nederland (Rabobank) as administrative agent and sole lead arranger (the Rabobank Facility).

On June 25, 2009, we completed a first closing on an expanded $250,000 revolving credit facility. The new Syndicated Facility, which had $175,000 total commitments as of June 30, 2009, included an accordion feature which allows the Syndicated Facility to accept up to an aggregate total of $250,000 of commitments for which we solicited additional commitments from other lenders for an additional $35,000 raising the commitments to $210,000. The revolving period ended on June 11, 2010, when we closed on our expanded revolving credit facility. On June 11, 2010, we closed an extension and expansion of our revolving credit facility with a syndicate of lenders (the Syndicated Facility). The lenders have extended commitments of $285,000 under the Syndicated Facility as of December 31, 2010. The Syndicated Facility includes an accordion feature which allows the facility to be increased to up to $400,000 of commitments in the aggregate to the extent additional or existing lenders commit to increase the commitments (See Note 14.). We will seek to add additional lenders in order to reach the maximum size; although no assurance can be given we will be able to do so. As we make additional investments which are eligible to be pledged under the Syndicated Facility, we will generate additional availability to the extent such investments are eligible to be placed into the borrowing base. The revolving period of the Syndicated Facility extends through June 2012, with an additional one year amortization period (with distributions allowed) after the completion of the revolving period. During such one year amortization period, all principal payments on the pledged assets will be applied to reduce the balance. At the end of the one year amortization period, the remaining balance will become due if required by the lenders.

The Syndicated Facility contains restrictions pertaining to the geographic and industry concentrations of funded loans, maximum size of funded loans, interest rate payment frequency of funded loans, maturity dates of funded loans and minimum equity requirements. The Syndicated Facility also contains certain requirements relating to portfolio performance, including required minimum portfolio yield and limitations on delinquencies and charge-offs, violation of which could result in the early termination of the Syndicated Facility. The Syndicated Facility also requires the maintenance of a minimum liquidity requirement. At December 31, 2010, we were in compliance with the applicable covenants.

Interest on borrowings under the Syndicated Facility is one-month LIBOR plus 325 basis points, subject to a minimum Libor floor of 100 basis points. Additionally, the lenders charge a fee on the unused portion of the Syndicated Facility equal to either 75 basis points if at least half of the credit facility is used or 100 basis points otherwise. The Syndicated Facility requires us to pledge assets as collateral in order to borrow under the credit facility. As of December 31, 2010 and June 30, 2010, we had \$242,890 and \$180,678 available to us for borrowing under our Syndicated Facility, of which zero and \$100,300 was outstanding, respectively. As we make additional investments which are eligible to be pledged under the Syndicated Facility, we will generate additional availability to the extent such investments are eligible to be placed into the borrowing base. At December 31, 2010, the investments used as collateral for the Syndicated Facility had an aggregate market value of \$607,021, which represents 67.2% of net assets. Prospect Capital Funding, LLC, our wholly-owned subsidiary, holds \$546,425 of these investments at market value as of December 31, 2010. The release of any assets from Prospect Capital Funding, LLC requires the approval of Rabobank as facility agent.

In connection with the origination and amendments of the Syndicated Facility, we incurred \$9,390 of fees, including \$3,224 of fees carried over from the previous facility, which are being amortized over the term of the facility in accordance with ASC 470-50, *Debt Modifications and Extinguishments*, of which \$7,079 remains to be amortized.

Note 6. Senior Convertible Notes

On December 21, 2010, we issued \$150,000 in aggregate principal amount of our 6.25% senior convertible notes due 2015 (Senior Convertible Notes) for net proceeds following underwriting expenses of approximately \$145,200. Interest on the Senior Convertible Notes is paid semi-annually in arrears on June 15 and December 15, at a rate of 6.25% per year, commencing June 15, 2011. The Senior Convertible Notes mature on December 15, 2015 unless converted earlier. The Senior Convertible Notes are convertible into shares of Common Stock at an initial conversion rate and conversion rate at December 31, 2010 of 88.0902 shares of Common Stock per \$1,000 principal amount of Senior Convertible Notes, which is equivalent to a conversion price of approximately \$11.352 per share of Common Stock, subject to adjustment in certain circumstances. The conversion rate for the Senior Convertible Notes will be increased if monthly cash dividends paid to common shares exceed the rate of \$0.101125 cents per share, subject to adjustment.

In no event will the total number of shares of common stock issuable upon conversion exceed 96.8992 per \$1,000 principal amount of the Senior Convertible Notes (the conversion rate cap), except that, to the extent we receive written guidance or a no-action letter from the staff of the Securities and Exchange Commission (the Guidance) permitting us to adjust the conversion rate in certain instances without regard to the conversion rate cap and to make the Senior Convertible Notes convertible into certain reference property in accordance with certain reclassifications, business combinations, asset sales and corporate events by us without regard to the conversion rate cap, we will make such adjustments without regard to the conversion rate cap and will also, to the extent that we make any such adjustment without regard to the conversion rate cap pursuant to the Guidance, adjust the conversion rate cap accordingly. We will use our commercially reasonable efforts to obtain such Guidance as promptly as practicable.

Prior to obtaining the Guidance, we will not engage in certain transactions that would result in an adjustment to the conversion rate increasing the conversion rate beyond what it would have been in the absence of such transaction unless we have engaged in a reverse stock split or share combination transaction such that in our reasonable best estimation, the conversion rate following the adjustment for such transaction will not be any closer to the conversion rate cap than it would have been in the absence of such transaction.

Upon conversion, unless a holder converts after a record date for an interest payment but prior to the corresponding interest payment date, the holder will receive a separate cash payment with respect to the Notes surrendered for conversion representing accrued and unpaid interest to, but not including the conversion date. Any such payment will be made on the settlement date applicable to the relevant conversion on the Senior Convertible Notes.

No holder of Senior Convertible Notes will be entitled to receive shares of our common stock upon conversion to the extent (but only to the extent) that such receipt would cause such converting holder to become, directly or indirectly, a beneficial owner (within the meaning of Section 13(d) of the Securities Exchange Act of 1934 and the rules and regulations promulgated thereunder) of more than 5.0% of the shares of our common stock outstanding at such time. The 5.0% limitation shall no longer apply following the effective date of any fundamental change. We will not issue any shares in connection with the conversion or redemption of the Notes which would equal or exceed 20% of the shares outstanding at the time of the transaction in accordance with NASDAQ rules.

Subject to certain exceptions, holders may require us to repurchase, for cash, all or part of their Notes upon a fundamental change at a price equal to 100% of the principal amount of the Notes being repurchased plus any accrued and unpaid interest up to, but excluding, the fundamental change repurchase date. In addition, upon a fundamental change that constitutes a non-stock change of control we will also pay holders an amount in cash equal to the present value of all remaining interest payments (without duplication of the foregoing amounts) on such Senior Convertible Notes through and including the maturity date.

In connection with the issuance of the Senior Convertible Notes, we incurred $5,045 of fees which are being amortized over the term of the facility in accordance with ASC 470-50, *Debt Modifications and Extinguishments,* of which $5,026 remains to be amortized.

For the period from December 21, 2010 (the date of issuance of the notes) to December 31, 2010, we recorded $280 of interest costs and amortization of financing costs as interest expense.

Note 7. Equity Offerings and Related Expenses

We issued 18,494,476 and 11,431,797 shares of our common stock during the six months ended December 31, 2010 and December 31, 2009, respectively. The proceeds raised, the related underwriting fees, the offering expenses and the prices at which these shares were issued are as follows:

Issuances of Common Stock	Number of Shares Issued	Gross Proceeds Raised	Underwriting Fees	Offering Expenses	Offering Price
November 16, 2010 December 15, 2010[1]	4,513,920	$ 45,147	$ 904	$ 333	$ 10.00
September 29, 2010 November 3, 2010[2]	5,231,956	$ 51,597	$ 1,033	$ 163	$ 9.861
July 22, 2010 September 28, 2010[3]	6,000,000	$ 58,403	$ 1,156	$ 103	$ 9.734
July 1, 2010 July 21, 2010[4]	2,748,600	$ 26,799	$ 536	$	$ 9.749
September 24, 2009 [5]	2,807,111	$ 25,264	$	$ 840	$ 9.000
August 20, 2009 [5]	3,449,686	$ 29,322	$	$ 117	$ 8.500
July 7, 2009	5,175,000	$ 46,575	$ 2,329	$ 200	$ 9.000

(1) On November 10, 2010, we established a fourth at-the-market program through which we may sell, from time to time and at our sole discretion 9,750,000 shares of our common stock. Through this program we issued 4,513,920 shares of our common stock at an average price of $10.00 per share, raising $45,147 of gross proceeds, from November 16, 2010 through December 15, 2010.

(2) On September 24, 2010, we established a third at-the-market program through which we sold 5,231,956 shares of our common stock at an average price of $9.86 per share, raising $51,597 of gross proceeds, from September 29, 2010 through November 3, 2010.

(3) On July 19, 2010, we established a second at-the-market program through which we sold 6,000,000 shares of our common stock at an average price of $9.73 per share, raising $58,403 of gross proceeds, from July 22, 2010 through September 28, 2010.

(4) On March 17, 2010, we established an at-the-market program through which we sold 8,000,000 shares of our common stock. Through this program we issued 2,748,600 shares of our common stock at an average price of $9.75 per share, raising $26,799 of gross proceeds, from July 1, 2010 through July 21, 2010.

(5) Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purchasers certain registration rights with respect to the shares. We have filed with the SEC a post-effective amendment to the registration statement on Form N-2 which has been declared effective by the SEC.

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Our shareholders equity accounts at December 31, 2010 and June 30, 2010 reflect cumulative shares issued as of those respective dates. Our common stock has been issued through public offerings, a registered direct offering, private offerings, the exercise of over-allotment options on the part of the underwriters and our dividend reinvestment plan. When our common stock is issued, the related offering expenses have been charged against paid-in capital in excess of par. All underwriting fees and offering expenses were borne by us.

On December 2, 2009, we issued 8,444,068 shares of common stock to acquire Patriot. This transaction is described in further detail in Note 3.

On October 9, 2008, our Board of Directors approved a share repurchase plan under which we may repurchase up to $20,000 of our common stock at prices below our net asset value as reported in our financial statements published for the year ended June 30, 2008. We have not made any purchases of our common stock during the period from October 9, 2008 to December 31, 2010 pursuant to this plan.

On October 29, 2010, November 30, 2010 and December 31, 2010, we issued shares of our common stock in connection with the dividend reinvestment plan of 92,999, 87,941 and 89,603, respectively.

On November 8, 2010, we announced the declaration of monthly dividends in the following amounts and with the following dates:

- $0.100875 per share for November 2010 to holders of record on November 30, 2010 with a payment date of December 31, 2010;

- $0.101000 per share for December 2010 to holders of record on December 31, 2010 with a payment date of January 31, 2011; and

- $0.101125 per share for January 2011 to holders of record on January 31, 2011 with a payment date of February 28, 2011.

Our Board of Directors, pursuant to the Maryland General Corporation Law, executed Articles of Amendment to increase the number of shares authorized for issuance from 100,000,000 to 200,000,000 in the aggregate. The amendment became effective August 31, 2010.

We have reserved 13,213,531 shares of our common stock for issuance upon conversion of the Senior Convertible Notes (See Note 6).

Note 8. Other Investment Income

Other investment income consists of structuring fees, overriding royalty interests, settlement of net profit interests, deal deposits, administrative agent fee, and other miscellaneous and sundry cash receipts. Income from such sources for the three and six months ended December 31, 2010 and December 31, 2009 were as follows:

Income Source	For The Three Months Ended December 31, 2010	For The Three Months Ended December 31, 2009	For The Six Months Ended December 31, 2010	For The Six Months Ended December 31, 2009
Gain on Patriot acquisition	$	$ 8,632	$	$ 8,632
Structuring and amendment fees	2,516	408	6,497	813
Overriding royalty interests	51	44	99	88
Administrative agent fee		8	68	23
Other Investment Income	$ 2,567	$ 9,092	$ 6,664	$ 9,556

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Note 9. Net Increase (Decrease) in Net Assets per Common Share

The following information sets forth the computation of net increase (decrease) in net assets resulting from operations per common share for the three and six months ended December 31, 2010 and December 31, 2009, respectively.

	For The Three Months Ended December 31,		For The Six Months Ended December 31,	
	2010	2009	2010	2009
Net increase (decrease) in net assets resulting from operations	$ 31,940	$ (14,520)	$ 57,520	$ (20,898)
Weighted average common shares outstanding	84,091,152	57,613,489	79,134,173	53,709,197
Net increase (decrease) in net assets resulting from operations per common share	$ 0.38	$ (0.25)	$ 0.73	$ (0.39)

Note 10. Related Party Agreements and Transactions

Investment Advisory Agreement

We have entered into an investment advisory and management agreement with Prospect Capital Management (the Investment Advisory Agreement) under which the Investment Adviser, subject to the overall supervision of our Board of Directors, manages the day-to-day operations of, and provides investment advisory services to, us. Under the terms of the Investment Advisory Agreement, our Investment Adviser: (i) determines the composition of our portfolio, the nature and timing of the changes to our portfolio and the manner of implementing such changes, (ii) identifies, evaluates and negotiates the structure of the investments we make (including performing due diligence on our prospective portfolio companies); and (iii) closes and monitors investments we make.

Prospect Capital Management s services under the Investment Advisory Agreement are not exclusive, and it is free to furnish similar services to other entities so long as its services to us are not impaired. For providing these services the Investment Adviser receives a fee from us, consisting of two components: a base management fee and an incentive fee. The base management fee is calculated at an annual rate of 2.00% on our gross assets (including amounts borrowed). For services currently rendered under the Investment Advisory Agreement, the base management fee is payable quarterly in arrears. The base management fee is calculated based on the average value of our gross assets at the end of the two most recently completed calendar quarters and appropriately adjusted for any share issuances or repurchases during the current calendar quarter.

The total base management fees incurred to the favor of the Investment Adviser for the three months ended December 31, 2010 and December 31, 2009 were $4,903, and $3,176, respectively. The fees incurred for the six months ended December 31, 2010 and December 31, 2008 were $9,179, and $6,385, respectively.

The incentive fee has two parts. The first part, the income incentive fee, is calculated and payable quarterly in arrears based on our pre-incentive fee net investment income for the immediately preceding calendar quarter. For this purpose, pre-incentive fee net investment income means interest income, dividend income and any other income (including any other fees (other than fees for providing managerial assistance), such as commitment, origination, structuring, diligence and consulting fees and other fees that we receive from portfolio companies) accrued during the calendar quarter, minus our operating expenses for the quarter (including the base management fee, expenses payable under the Administration Agreement described below, and any interest expense and dividends paid on any issued and outstanding preferred stock, but excluding the incentive fee). Pre-incentive fee net investment income includes, in the case of investments with a deferred interest feature (such as original issue discount, debt instruments with payment in kind interest and zero coupon securities), accrued income that we have not yet received in cash. Pre-incentive fee net investment income does not include any realized capital gains, realized capital losses or unrealized capital appreciation or depreciation. Pre-incentive fee net investment income, expressed as a rate of return on the value of our net assets at the end of the immediately preceding calendar quarter, is compared to a hurdle rate of 1.75% per quarter (7.00% annualized).

The net investment income used to calculate this part of the incentive fee is also included in the amount of the gross assets used to calculate the 2.00% base management fee. We pay the Investment 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;
- 100.00% 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 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate); and
- 20.00% of the amount of our pre-incentive fee net investment income, if any, that exceeds 125.00% of the quarterly hurdle rate in any calendar quarter (8.75% annualized assuming a 7.00% annualized hurdle rate).

These calculations are appropriately prorated for any period of less than three months and adjusted for any share issuances or repurchases during the current quarter.
The second part of the incentive fee, the capital gains incentive fee, is determined and payable in arrears as of the end of each calendar year (or upon termination of the Investment Advisory Agreement, as of the termination date), and equals 20.00% of our realized capital gains for the calendar year, if any, computed net of all realized capital losses and unrealized capital depreciation at the end of such year. In determining the capital gains incentive fee payable to the Investment Adviser, we calculate the aggregate realized capital gains, aggregate realized capital losses and aggregate unrealized capital depreciation, as applicable, with respect to each investment that has been in its portfolio. For the purpose of this calculation, an investment is defined as the total of all rights and claims which maybe asserted against a portfolio company arising from our participation in the debt, equity, and other financial instruments issued by that company. Aggregate realized capital gains, if any, equals the sum of the differences between the aggregate net sales price of each investment and the aggregate cost basis of such investment when sold or otherwise disposed. Aggregate realized capital losses equal the sum of the amounts by which the aggregate net sales price of each investment is less than the aggregate cost basis of such investment when sold or otherwise disposed. Aggregate unrealized capital depreciation equals the sum of the differences, if negative, between the aggregate valuation of each investment and the aggregate cost basis of such investment as of the applicable calendar year-end. At the end of the applicable calendar year, the amount of capital gains that serves as the basis for our calculation of the capital gains incentive fee involves netting aggregate realized capital gains against aggregate realized capital losses on a since-inception basis and then reducing this amount by the aggregate unrealized capital depreciation. If this number is positive, then the capital gains incentive fee payable is equal to 20.00% of such amount, less the aggregate amount of any capital gains incentive fees aid since inception.
For the three months ended December 31, 2010 and December 31, 2009, income incentive fees of $4,769 and $4,816, respectively, were incurred. For the six months ended December 31, 2010 and December 31, 2009, income incentive fees of $10,018 and $7,896, respectively, were incurred. No capital gains incentive fees were incurred for the three or six months ended December 31, 2010 and December 31, 2009.
Administration Agreement
We have also entered into an Administration Agreement with Prospect Administration, LLC (Prospect Administration) under which Prospect Administration, among other things, provides (or arranges for the provision of) administrative services and facilities for us. For providing these services, we reimburse Prospect Administration for our allocable portion of overhead incurred by Prospect Administration in performing its obligations under the Administration Agreement, including rent and our allocable portion of the costs of our chief compliance officer and chief financial officer and his staff. For the three months ended December 31, 2010 and 2009, the reimbursement was approximately $840. For the six months ended December 31, 2010 and 2009, the reimbursement was approximately $1,640 and $1,680, respectively. Under this agreement, Prospect Administration furnishes us with office facilities, equipment and clerical, bookkeeping and record keeping services at such facilities. Prospect Administration also performs, or oversees the performance of, our required administrative services, which include, among other things, being responsible for the financial records that we are required to maintain and preparing reports to our stockholders and reports filed with the SEC. In addition, Prospect Administration assists us in determining and publishing our net asset value, overseeing the preparation and filing of our tax returns and the printing and dissemination of reports to our stockholders, and generally oversees the payment of our expenses and the performance of administrative and professional services rendered to us by others. Under the Administration Agreement, Prospect Administration also provides on our behalf managerial assistance to those portfolio companies to which we are required to provide such assistance. The Administration Agreement may be terminated by either party without penalty upon 60 days written notice to the other party. Prospect Administration is a wholly owned subsidiary of our Investment Adviser.
The Administration Agreement provides that, absent willful misfeasance, bad faith or negligence in the performance of its duties or by reason of the reckless disregard of its duties and obligations, Prospect Administration and its officers, managers, partners, agents, employees, controlling persons, members and any other person or entity affiliated with it are entitled to indemnification from us for any damages, liabilities, costs and expenses (including reasonable attorneys fees and amounts reasonably paid in settlement) arising from the rendering of Prospect Administration s

services under the Administration Agreement or otherwise as administrator for us.

Prospect Administration, pursuant to the approval of our Board of Directors, engaged Vastardis Fund Services LLC (Vastardis) to serve as our sub-administrator to perform certain services required of Prospect Administration. Under the sub-administration agreement, Vastardis provided us with office facilities, equipment, clerical, bookkeeping and record keeping services at such facilities. Vastardis also conducted relations with custodians, depositories, transfer agents, dividend disbursing agents, other stockholder servicing agents, accountants, attorneys, underwriters, brokers and dealers, corporate fiduciaries, insurers, banks and such other persons in any such other capacity deemed to be necessary or desirable.

On April 30, 2009 we gave a 60-day notice to Vastardis of termination of our agreement to provide sub-administration services effective June 30, 2009. We entered into a new consulting services agreement for the period from July 1, 2009 until the filing of our Form 10-K for the year ended June 30, 2009. We paid Vastardis a total of $30 for services rendered in conjunction with preparation of Form 10-K under the new agreement. All services previously provided by Vastardis were assumed by Prospect Administration beginning on July 1, 2009.

Managerial Assistance

As a business development company, we offer, and must provide upon request, managerial assistance to certain of our portfolio companies. This assistance could involve, among other things, monitoring the operations of our portfolio companies, participating in board and management meetings, consulting with and advising officers of portfolio companies and providing other organizational and financial guidance. We billed $360 and $215 of managerial assistance fees for the three months ended December 31, 2010 and June 30, 2010, respectively, of which $195 and $247 remains on the consolidated statement of assets and liabilities as of December 31, 2010, and June 30, 2010, respectively. We billed $613 and $431 of managerial assistance fees for the six months ended December 31, 2010 and June 30, 2010, respectively. These fees are paid to the Administrator when received. We simultaneously accrue a payable to the Administrator for the same amounts, which remain on the consolidated statements of assets and liabilities.

Note 11. Litigation

From time to time, we may become involved in various investigations, claims and legal proceedings that arise in the ordinary course of our business. These matters may relate to intellectual property, employment, tax, regulation, contract or other matters. The resolution of these matters as they arise will be subject to various uncertainties and, even if such claims are without merit, could result in the expenditure of significant financial and managerial resources. We are not aware of any such litigation as of December 31, 2010.

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Note 12. Financial Highlights

	For The Three Months Ended December 31, 2010	For The Three Months Ended December 31, 2009	For The Six Months Ended December 31, 2010	For The Six Months Ended December 31, 2009
Per Share Data[1]:				
Net asset value at beginning of period	$ 10.24	$ 11.11	$ 10.30	$ 12.40
Net investment income	0.23	0.33	0.51	0.59
Net realized gain (loss)	0.05	(0.89)	0.06	(0.95)
Net unrealized appreciation (depreciation)	0.10	0.30	0.16	(0.02)
Net decrease in net assets as a result of public offerings	(0.06)	(0.01)	(0.16)	(0.79)
Net increase in net assets as a result of shares issued for Patriot acquisition		0.08		0.13
Dividends declared and paid	(0.31)	(0.82)	(0.62)	(1.26)
Net asset value at end of period	$ 10.25	$ 10.10	$ 10.25	$ 10.10
Per share market value at end of period	$ 10.80	$ 11.81	$ 10.80	$ 11.81
Total return based on market value[2]	14.34%	14.09%	18.62%	37.87%
Total return based on net asset value[2]	2.90%	(5.94%)	5.48%	(12.52%)
Shares outstanding at end of period	88,115,382	63,349,746	88,115,382	63,349,746
Average weighted shares outstanding for period	84,091,152	57,613,489	79,134,173	53,709,197
Ratio / Supplemental Data:				
Net assets at end of period (in thousands)	$ 903,190	$ 639,810	$ 903,190	$ 639,810
Annualized ratio of operating expenses to average net assets	6.67%	8.01%	7.04%	7.43%
Annualized ratio of net operating income to average net assets	8.95%	12.39%	9.97%	10.55%

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Note 12. Financial Highlights (continued)

	Year Ended June 30, 2010	Year Ended June 30, 2009	Year Ended June 30, 2008	Year Ended June 30, 2007	Year Ended June 30, 2006
Per Share Data[1]:					
Net asset value at beginning of period	$ 12.40	$ 14.55	$ 15.04	$ 15.31	$ 14.59
Costs related to the initial public offering					0.01
Costs related to the secondary public offering			(0.07)	(0.06)	
Net investment income	1.13	1.87	1.91	1.47	1.21
Realized (loss) gain	(0.87)	(1.24)	(0.69)	0.12	0.04
Net unrealized appreciation (depreciation)	0.07	0.48	(0.05)	(0.52)	0.58
Net (decrease) increase in net assets as a result of public offering	(0.85)	(2.11)		0.26	
Net increase in net assets as a result of shares issued for Patriot acquisition	0.12				
Dividends declared and paid	(1.70)	(1.15)	(1.59)	(1.54)	(1.12)
Net asset value at end of period	$ 10.30	$ 12.40	$ 14.55	$ 15.04	$ 15.31
Per share market value at end of period	$ 9.65	$ 9.20	$ 13.18	$ 17.47	$ 16.99
Total return based on market value[2]	17.66%	(18.60%)	(15.90%)	12.65%	44.90%
Total return based on net asset value[2]	(6.82%)	(0.61%)	7.84%	7.62%	12.76%
Shares outstanding at end of period	69,086,862	42,943,084	29,520,379	19,949,065	7,069,873
Average weighted shares outstanding for period	59,429,222	31,559,905	23,626,642	15,724,095	7,056,846
Ratio / Supplemental Data:					
Net assets at end of period (in thousands)	$ 711,424	$ 532,596	$ 429,623	$ 300,048	$ 108,270
Annualized ratio of operating expenses to average net assets	7.54%	9.03%	9.62%	7.36%	8.19%
Annualized ratio of net investment income to	10.69%	13.14%	12.66%	9.71%	7.90%

average net assets

(1) Financial highlights are based on weighted average shares.

(2) Total return based on market value is based on the change in market price per share between the opening and ending market prices per share in each period and assumes that dividends are reinvested in accordance with our dividend reinvestment plan. Total return based on net asset value is based upon the change in net asset value per share between the opening and ending net asset values per share in each period and assumes that dividends are reinvested in accordance with our dividend reinvestment plan.

Note 13. Selected Quarterly Financial Data (Unaudited)

	Investment Income		Net Investment Income		Net Realized and Unrealized Gains (Losses)		Net Increase (Decrease) in Net Assets from Operations	
Quarter Ended	Total	Per Share(1)	Total	Per Share(1)	Total	Per Share(1)	Total	Per Share(1)
September 30, 2007	15,391	0.77	7,865	0.39	685	0.04	8,550	0.43
December 31, 2007	18,563	0.80	10,660	0.46	(14,346)	(0.62)	(3,686)	(0.16)
March 31, 2008	22,000	0.92	12,919	0.54	(14,178)	(0.59)	(1,259)	(0.05)
June 30, 2008	23,448	0.85	13,669	0.50	10,317	0.38	23,986	0.88
September 30, 2008(2)	35,799	1.21	23,502	0.80	(9,504)	(0.33)	13,998	0.47
December 31, 2008	22,213	0.75	11,960	0.40	(5,436)	(0.18)	6,524	0.22
March 31, 2009	20,669	0.69	11,720	0.39	3,611	0.12	15,331	0.51
June 30, 2009	21,800	0.59	11,981	0.32	(12,730)	(0.34)	(749)	(0.02)
September 30, 2009	21,517	0.43	12,318	0.25	(18,696)	(0.38)	(6,378)	(0.13)
December 31, 2009(3)	31,801	0.55	19,258	0.33	(33,778)	(0.59)	(14,520)	(0.25)
March 31, 2010	32,005	0.50	18,974	0.30	6,966	0.11	25,940	0.41
June 30, 2010	29,236	0.44	16,640	0.25	(2,057)	(0.03)	14,583	0.22
September 30, 2010	35,212	0.47	20,995	0.28	4,585	0.06	25,580	0.34
December 31, 2010	33,300	0.40	19,080	0.23	12,861	0.16	31,940	0.38

(1) Per share amounts are calculated using weighted average shares during period.

(2) Additional income for this quarter was driven by other investment income from the settlement of net profits interests on IEC Systems LP and Advanced Rig Services LLC for $12,576.

(3) As adjusted for increase in gain from Patriot acquisition. See Note 3.

Note 14. Subsequent Events

On January 6, 2011, we made a senior secured term loan investment of $30,000 to support the acquisition of Progressive Logistics Services, LLC by a middle market private equity firm.

On January 10, 2011, we made a senior secured debt investment of $19,000 to support the acquisition of Endeavor House by Pinnacle Treatment Centers, Inc.

On January 10, 2011, we sold 616,304 shares of Miller common stock realizing $4.23 of net proceeds per share, realizing a gain of $2,561 on the sale.

On January 13, 2011, we amended our revolving credit facility. The amendment increases the accordion feature limit from $300,000 to $400,000 of commitments, of which $285,000 of commitments are currently in place. Other changes in the amendment increase our borrowing base with the investments currently pledged to the facility by reducing some concentration limits and allow us to pledge new assets to the facility on an expedited basis.

On January 21, 2011, we provided senior secured credit facilities of $28,200 to support the acquisition of Stauber Performance Ingredients, by ICV Partners. Through February 9, 2011, we have funded $26,450 of the commitment.

On January 24, 2011, Maverick Healthcare, LLC repaid the $13,122 loan receivable to us.

On January 31, 2011, we issued 84,155 shares of our common stock in connection with the dividend reinvestment plan.

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On January 31, 2011, we made a senior secured term investment of $7,500 to support the recapitalization of Empire Today, LLC, which is the second largest independent provider of carpet and hard surface flooring to consumers in the residential replacement flooring industry.

On February 3, 2011, we made a senior secured debt investment of $22,000 to support the recapitalization of a pharmacy services company by a leading private equity firm. Through February 9, 2011, we have funded $20,500 of the commitment.

On February 4, 2011, we made a secured second-lien debt investment of $45,000 to support the refinancing of Clearwater Seafoods Limited Partnership, a leading premium seafood company based in Nova Scotia, Canada.

On February 8, 2011, we announced the declaration of monthly dividends in the following amounts and with the following dates:

- $0.101150 per share for February 2011 to holders of record on February 28, 2011 with a payment date of March 31, 2011;

- $0.101175 per share for March 2011 to holders of record on March 31, 2011 with a payment date of April 29, 2011;

- $0.101200 per share for April 2011 to holders of record on April 29, 2011 with a payment date of May 31, 2011.

On February 9, 2011, we made a net follow-on investment of $2,967 in The Copernicus Group, Inc. that increased our total investment to $22,500.

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

(All figures in this item are in thousands except share, per share and other data)

References herein to we, us or our refer to Prospect Capital Corporation and its subsidiary unless the contex specifically requires otherwise.

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this quarterly report on Form 10-Q. Historical results set forth are not necessarily indicative of our future financial position and results of operations.

Note on Forward Looking Statements

Some of the statements in this report constitute forward-looking statements, which relate to future events or our future performance or financial condition. The forward-looking statements contained herein involve risks and uncertainties, including statements as to:

- our future operating results;
- our business prospects and the prospects of our portfolio companies;
- the impact of investments that we expect to make;
- our contractual arrangements and relationships with third parties;
- the dependence of our future success on the general economy and its impact on the industries in which we invest;
- the ability of our portfolio companies to achieve their objectives;
- our expected financings and investments;
- the adequacy of our cash resources and working capital; and
- the timing of cash flows, if any, from the operations of our portfolio companies.

We generally use words such as anticipates, believes, expects, intends and similar expressions to iden forward-looking statements. Our actual results could differ materially from those projected in the forward-looking statements for any reason, including the factors set forth in Risk Factors and elsewhere in this report.

We have based the forward-looking statements included in this report on information available to us on the date of this report, and we assume no obligation to update any such forward-looking statements. Although we undertake no obligation to revise or update any forward-looking statements, whether as a result of new information, future events or otherwise, you are advised to consult any additional disclosures that we may make directly to you or through reports that we in the future may file with the Securities and Exchange Commission (SEC), including any annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K.

General

We are a financial services company that primarily lends to and invests in middle market privately-held companies. We are a closed-end investment company that has filed an election to be treated as a business development company under the Investment Company Act of 1940, or the 1940 Act. We invest primarily in senior and subordinated debt and equity of companies in need of capital for acquisitions, divestitures, growth, development, project financing and recapitalization. We work with the management teams or financial sponsors to seek investments with historical cash flows, asset collateral or contracted pro-forma cash flows.

We seek to be a long-term investor with our portfolio companies. From our July 27, 2004 inception to the fiscal year ended June 30, 2007, we invested primarily in industries related to the industrial/energy economy. Since then, we have widened our strategy to focus in other sectors of the economy and continue to diversify our portfolio holdings.

The aggregate value of our portfolio investments was $918,221 and $748,483 as of December 31, 2010 and June 30, 2010, respectively. During the six months ended December 31, 2010, our net cost of investments increased by $157,309, or 21.6%, primarily as a result of our investment in ten new and seven follow-on investments of $275,867, while we received full repayment on eight investments, sold three investments and received several partial prepayments and revolver paydowns of $135,553. Several new investments that we anticipated closing prior to December 31, 2010 were delayed by the borrowers when the expiring tax breaks were extended. The closing of these loans has increased the level of activity during the current quarter ending March 31, 2011 as detailed in the *Recent Developments*, which follows.

Compared to the end of last fiscal year (ended June 30, 2010), net assets increased by $191,766 or 27.0% during the six months ended December 31, 2010, from $711,424 to $903,190. This increase resulted from the issuance of new shares of our common stock (less offering costs) in the amount of $177,718, dividend reinvestments of $5,280, and another $57,520 from operations. These increases, in turn, were offset by $48,752 in dividend distributions to our stockholders. The $57,520 increase in net assets resulting from operations is net of the following: net investment income of $40,075, net realized gain on investments of $5,016, and an increase in net assets due to changes in net unrealized appreciation of investments of $12,429.

Market Conditions

While the economy continues to show signs of recovery from the deteriorating credit markets of 2008 and 2009, there is still a level of uncertainty and volatility in the capital markets. The growth and improvement in the capital markets that began during the second half of 2009 carried over into the first half of 2010. While encouraged by the signs of improvement, we operate in a challenging environment that is still recovering from a recession and financial services industry negatively affected by the deterioration of credit quality in subprime residential mortgages that spread rapidly to other credit markets. Market liquidity and credit quality conditions continue to remain weaker today than three years ago.

We believe that Prospect is well positioned to navigate through these adverse market conditions. As a business development company, we are limited to a maximum 1 to 1 debt to equity ratio. On December 21, 2011, we issued $150,000 of 6.25% Senior Convertible Notes due December 15, 2015 to further enhance our liquidity position and to demonstrate our access to the unsecured term debt market (See Note 6 to our consolidated financial statements.). The Senior Convertible Notes are general unsecured obligations, rank equally in right of payment with our existing and future senior unsecured debt, and will rank senior in right of payment to any potential subordinated debt, should any be issued in the future. The Senior Convertible Notes have no restrictions related to the type and security of assets in which Prospect might invest.

As of December 31, 2010, we had no outstanding borrowings on the credit facility and $150,000 outstanding on our Senior Convertible Notes. We also had $242,890 available under our credit facility for additional borrowing. Further, as we make additional investments that are eligible to be pledged under the credit facility, we will generate additional credit facility availability. The revolving period for our credit facility continues until June 13, 2012, with an amortization running to June 13, 2013. During the amortization period only principal payments received on the pledged assets are required to be used for amortization.

We also continue to generate liquidity through public and private stock offerings. On July 7, 2009, we completed a public stock offering for 5,175,000 shares of our common stock at $9.00 per share, raising $46,575 of gross proceeds. On August 20, 2009 and September 24, 2009, we issued 3,449,686 shares and 2,807,111 shares, respectively, of our common stock at $8.50 and $9.00 per share, respectively, in private stock offerings, raising $29,322, and $25,264 of gross proceeds, respectively. Concurrent with the sale of these shares, we entered into a registration rights agreement in which we granted the purchasers certain registration rights with respect to the shares. Under the terms and conditions of the registration rights agreement, we filed with the SEC a post-effective amendment to the registration statement on Form N-2 on November 6, 2009. Such amendment was declared effective by the SEC on November 9, 2009.

On March 4, 2010, our Registration Statement on Form N-2 was declared effective by the SEC. Under this Shelf Registration Statement, we can issue up to $257,676 of additional equity securities as of December 31, 2010.

On March 17, 2010, we established an at-the-market program through which we sold shares of our common stock. An at-the-market offering is a registered offering by a publicly traded issuer of its listed equity securities selling shares directly into the market at market prices. We engaged two broker-dealers to act as agents and sell our common stock directly into the market over a period of time. We paid a 2% commission to the broker-dealer on shares sold. Through this program we issued 8,000,000 shares of our common stock at an average price of $10.90 per share, raising $87,177 of gross proceeds, from March 23, 2010 through July 21, 2010.

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On July 19, 2010, we established a second at-the-market program, as we had sold all the shares authorized in the original at-the-market program. We engaged three broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We paid a 2% commission to the broker-dealer on shares sold. Through this program we issued 6,000,000 shares of our common stock at an average price of $9.73 per share, raising $58,403 of gross proceeds, from July 22, 2010 through September 28, 2010.

On September 24, 2010, we established a third at-the-market program, as we had sold all the shares authorized in the preceding at-the-market programs, through which we may sell, from time to time and at our discretion, 6,000,000 shares of our common stock. We engaged three broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We currently pay a 2% commission to the broker-dealer on shares sold. Through this program we issued 302,400 shares of our common stock at an average price of $9.87 per share, raising $2,986 of gross proceeds, from September 29, 2010 through September 30, 2010. During the period from October 1, 2010 to November 3, 2010, we continued this program and issued an additional 4,929,556 shares of our common stock at an average price of $9.86 per share, raising $48,611 of gross proceeds.

On November 10, 2010, we established a fourth at-the-market program, through which we may sell, from time to time and at our discretion, 9,750,000 shares of our common stock. We engaged four broker-dealers to act as potential agents and sell our common stock directly into the market over a period of time. We pay a 2% commission to the broker-dealer on shares sold. Through this program we issued 4,513,920 shares of our common stock at an average price of $10.00 per share, raising $45,147 of gross proceeds, from November 16, 2010 through December 15, 2010.

Our Board of Directors, pursuant to the Maryland General Corporation Law, executed Articles of Amendment to increase the number of shares authorized for issuance from 100,000,000 to 200,000,000 in the aggregate. The amendment became effective August 31, 2010.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reported period. Changes in the economic environment, financial markets and any other parameters used in determining these estimates could cause actual results to differ.

Second Quarter Highlights

Investment Transactions

On October 12, 2010, we made a senior secured debt investment of $32,500 in ICON Health & Fitness, Inc., a leading manufacturer and marketer of branded health and fitness equipment. The first lien note bears interest in cash at 11.875% and has a final maturity on October 15, 2016.

On October 29, 2010, Castro Cheese Company, Inc. repaid the $7,732 loan receivable to us.

On November 3, 2010, TriZetto Group repaid the $15,492 loan receivable to us.

On November 12, 2010, we made a senior subordinated debt investment of $15,000 in American Importing Company, Inc and Ann s House of Nuts Inc, collectively Snacks Holding Corporation, a leading manufacturer and marketer of dried fruits and trail mixes. The unsecured note bears interest in cash at 12.0% plus 1.0% PIK and has a final maturity on November 12, 2007.

On November 29, 2010, we made a senior subordinated debt investment of $14,000 in Royal Adhesives & Sealants LLC (Royal), a leading producer of proprietary, high-performance adhesives and sealants. The unsecured note bears interest in cash at the greater of 12.0% or Libor plus 8.5%, with a Libor ceiling of 4.5%, plus 2.0% PIK and has a final maturity on November 29, 2016. On December 13, 2010, we made a follow-on secured debt investment of $11,000 in Royal.

On December 1, 2010, Qualitest Pharmaceuticals, Inc. repaid the $12,000 loan receivable to us.

On December 3, 2010, we exercised our warrants in Miller and received 2,013,814 shares of Miller common stock. On December 27, 2010, we sold 1,397,510 of these shares at $3.95 net proceeds per share, realizing a gain of $5,415.

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On December 10, 2010, we made a $30,000 secured second-lien financing to American Gilsonite Company (American Gilsonite) for a dividend recapitalization. After the financing, we received a $2,098 dividend as a result of our equity holdings in American Gilsonite and repayment of the loan that was outstanding.

On December 23, 2010, we made a second lien secured debt investment of $15,300 in Jordan Healthcare Holdings, Inc. (Jordan), a leading provider of home healthcare services in Texas. The second lien note bears interest in cash at the greater of 12.0% or Libor plus 10.0% plus 2.5% PIK and has a final maturity on June 23, 2016.

On December 23, 2010, we made a senior secured investment of $18,333 in VPSI, Inc. (VPSI), a leading market share transportation services company. The first lien note bears interest in cash at the greater of 12.0% or Libor plus 10.0% and has a final maturity on December 23, 2015.

Equity Issuance

On October 29, 2010, November 30, 2010 and December 31, 2010, we issued shares of our common stock in connection with the dividend reinvestment plan of 92,999, 87,941 and 89,603, respectively.

During the period from October 1, 2010 to November 3, 2010, we issued 4,929,556 shares of our common stock at an average price of $9.86 per share, and raised $48,611 of gross proceeds, under our at-the-market program. Net proceeds were $47,639 after 2% commission to the broker-dealer on shares sold.

On November 10, 2010, we established a new at-the-market program through which we may sell 9,750,000 shares of our common stock. Through this program we issued 4,513,920 shares of our common stock at an average price of $10.00 per share, raising $45,147 of gross proceeds, from November 16, 2010 to December 15, 2010. Net proceeds were $44,244 after 2% commission to the broker-dealer on shares sold.

Dividend

On November 8, 2010, we announced the declaration of monthly dividends in the following amounts and with the following dates:

- $0.100875 per share for November 2010 to holders of record on November 30, 2010 with a payment date of December 31, 2010;

- $0.101000 per share for December 2010 to holders of record on December 31, 2010 with a payment date of January 31, 2011;

- $0.101125 per share for January 2011 to holders of record on January 31, 2011 with a payment date of February 28, 2011.

Credit Facility

On November 1, 2010, we announced an increase in commitments to our credit facility of $20,000. As of December 31, 2010, the lenders have extended commitments of $285,000 under the credit facility. Our credit facility includes an accordion feature which allows the facility to be increased to up to $300,000 of commitments in the aggregate to the extent additional or existing lenders commit to increase the commitments. We will seek to add additional lenders in order to reach the maximum size; although no assurance can be given we will be able to do so.

Senior Convertible Notes

On December 21, 2010, we issued $150,000 in aggregate principal amount of 6.25% Senior Convertible Notes due 2015. The Notes mature on December 15, 2015, unless previously converted in accordance with their terms. The Notes are general unsecured obligations, rank equally in right of payment with our existing and future senior unsecured debt, and rank senior in right of payment to any potential subordinated debt, should any be issued in the future. The Senior Convertible Notes are convertible into shares of Common Stock at an initial conversion rate and conversion rate at December 31, 2010 of 88.0902 shares of Common Stock per $1,000 principal amount of Senior Convertible Notes, which is equivalent to a conversion price of approximately $11.352 per share of Common Stock, subject to adjustment in certain circumstances. The holders of the Notes may also put back the Notes to the Company under certain circumstances. The net proceeds from the offering of the Senior Convertible Notes were approximately $145,200, which will be used initially to maintain balance sheet liquidity, including repayment of debt under the Company s credit facility, investments in high quality short-term debt instruments or a combination thereof, and thereafter to make long-term investments in accordance with the Company s investment objective. We have analyzed the features of the Senior Convertible Notes to determine if bifurcation was necessary and have determined that it is not material.

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Recent Developments

On January 6, 2011, we made a senior secured term loan investment of $30,000 to support the acquisition of Progressive Logistics Services, LLC by a middle market private equity firm.

On January 10, 2011, we made a senior secured debt investment of $19,000 to support the acquisition of Endeavor House by Pinnacle Treatment Centers, Inc.

On January 10, 2011, we sold 616,304 shares of Miller Petroleum, Inc. (Miller) common stock realizing $4.23 of net proceeds per share, realizing a gain of $2,561 on the sale.

On January 13, 2011, we amended our revolving credit facility. The amendment increases the accordion feature limit from $300,000 to $400,000 of commitments, of which $285,000 of commitments are currently in place. Other changes in the amendment increase our borrowing base with the investments currently pledged to the facility by reducing some concentration limits and allow us to pledge new assets to the facility on an expedited basis.

On January 21, 2011, we provided senior secured credit facilities of $28,200 to support the acquisition of Stauber Performance Ingredients, by ICV Partners. Through February 9, 2011, we have funded $26,450 of the commitment.

On January 24, 2011, Maverick Healthcare, LLC (Maverick) repaid the $13,122 loan receivable to us.

On January 31, 2011, we issued 84,155 shares of our common stock in connection with the dividend reinvestment plan.

On January 31, 2011, we made a senior secured term investment of $7,500 to support the recapitalization of Empire Today, LLC, which is the second largest independent provider of carpet and hard surface flooring to consumers in the residential replacement flooring industry.

On February 3, 2011, we made a senior secured debt investment of $22,000 to support the recapitalization of a pharmacy services company by a leading private equity firm. Through February 9, 2011, we have funded $20,500 of the commitment.

On February 4, 2011, we made a secured second-lien debt investment of $45,000 to support the refinancing of Clearwater Seafoods Limited Partnership, a leading premium seafood company based in Nova Scotia, Canada.

On February 8, 2011, we announced the declaration of monthly dividends in the following amounts and with the following dates:

- $0.101150 per share for February 2011 to holders of record on February 28, 2011 with a payment date of March 31, 2011;
- $0.101175 per share for March 2011 to holders of record on March 31, 2011 with a payment date of April 29, 2011;
- $0.101200 per share for April 2011 to holders of record on April 29, 2011 with a payment date of May 31, 2011.

On February 9, 2011, we made a net follow-on investment of $2,967 in The Copernicus Group, Inc. that increased our total investment to $22,500.

Critical Accounting Policies and Estimates

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

Basis of Consolidation

Under the 1940 Act rules, the regulations pursuant to Article 6 of Regulation S-X, and the American Institute of Certified Public Accountants Audit and Accounting Guide for Investment Companies, we are precluded from consolidating any entity other than another investment company or an operating company which provides substantially all of its services and benefits to us. Our December 31, 2010 and June 30, 2010 financial statements include our accounts and the accounts of Prospect Capital Funding, LLC, our only wholly-owned, closely-managed subsidiary, which is also an investment company. All intercompany balances and transactions have been eliminated in consolidation.

Investment Classification

We are a non-diversified company within the meaning of the 1940 Act. We classify our investments by level of control. As defined in the 1940 Act, control investments are those where there is the ability or power to exercise a controlling influence over the management or policies of a company. Control is generally deemed to exist when a company or individual possesses or has the right to acquire within 60 days or less, a beneficial ownership of 25% or more of the voting securities of an investee company. Affiliated investments and affiliated companies are defined by a lesser degree of influence and are deemed to exist through the possession outright or via the right to acquire within 60 days or less, beneficial ownership of 5% or more of the outstanding voting securities of another person.

Investments are recognized when we assume an obligation to acquire a financial instrument and assume the risks for gains or losses related to that instrument. Investments are derecognized when we assume an obligation to sell a financial instrument and forego the risks for gains or losses related to that instrument. Specifically, we record all security transactions on a trade date basis. Investments in other, non-security financial instruments are recorded on the basis of subscription date or redemption date, as applicable. Amounts for investments recognized or derecognized but not yet settled are reported as Receivables for investments sold and Payables for investments purchased, respectively, in the Consolidated Statements of Assets and Liabilities.

Investment Valuation

Our Board of Directors has established procedures for the valuation of our investment portfolio. These procedures are detailed below.

Investments for which market quotations are readily available are valued at such market quotations.

For most of our investments, market quotations are not available. With respect to investments for which market quotations are not readily available or when such market quotations are deemed not to represent fair value, our Board of Directors has approved a multi-step valuation process each quarter, as described below:

1) Each portfolio company or investment is reviewed by our investment professionals with the independent valuation firm engaged by our Board of Directors;

2) the independent valuation firm conducts independent appraisals and makes their own independent assessment;

3) the audit committee of our Board of Directors reviews and discusses the preliminary valuation by our Investment Adviser within the valuation range presented by the independent valuation firm; and

4) the Board of Directors discusses the valuations and determines the fair value of each investment in our portfolio in good faith based on the input of our Investment Adviser, the independent valuation firm and the audit committee.

In September 2006, the Financial Accounting Standards Board (FASB) issued ASC 820, *Fair Value Measurements and Disclosures* (ASC 820). ASC 820 defines fair value, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. We adopted ASC 820 on a prospective basis beginning in the quarter ended September 30, 2008.

ASC 820 classifies the inputs used to measure these fair values into the following hierarchy:
Level 1: Quoted prices in active markets for identical assets or liabilities, accessible by the Company at the measurement date.
Level 2: Quoted prices for similar assets or liabilities in active markets, or quoted prices for identical or similar assets or liabilities in markets that are not active, or other observable inputs other than quoted prices.
Level 3: Unobservable inputs for the asset or liability.
In all cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to each investment.
The changes to generally accepted accounting principles from the application of ASC 820 relate to the definition of fair value, framework for measuring fair value, and the expanded disclosures about fair value measurements. ASC 820 applies to fair value measurements already required or permitted by other standards.
In accordance with ASC 820, the fair value of our investments is defined as the price that we would receive upon selling an investment in an orderly transaction to an independent buyer in the principal or most advantageous market in which that investment is transacted.
In April 2009, the FASB issued ASC 820-10-65, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly* (ASC 820-10-65). This update provides further clarification for ASC 820 in markets that are not active and provides additional guidance for determining when the volume of trading level of activity for an asset or liability has significantly decreased and for identifying circumstances that indicate a transaction is not orderly. ASC 820-10-65 is effective for interim and annual reporting periods ending after June 15, 2009. The adoption of ASC 820-10-65 for the three and six months ended December 31, 2010 and 2009, did not have any effect on our net asset value, financial position or results of operations as there was no change to the fair value measurement principles set forth in ASC 820.
In January 2010, the FASB issued Accounting Standards Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). ASU 2010-06 amends ASC 820-10 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers disclosures about postretirement benefit plan assets. ASU 2010-06 is effective for interim and annual reporting periods beginning after December 15, 2009. Our management does not believe that the adoption of the amended guidance in ASC 820-10 will have a significant effect on our financial statements.
Federal and State Income Taxes
We have elected to be treated as a regulated investment company and intend to continue to comply with the requirements of the Internal Revenue Code of 1986 (the Code), applicable to regulated investment companies. We are required to distribute at least 90% of our investment company taxable income and intend to distribute (or retain through a deemed distribution) all of our investment company taxable income and net capital gain to stockholders; therefore, we have made no provision for income taxes. The character of income and gains that we will distribute is determined in accordance with income tax regulations that may differ from GAAP. Book and tax basis differences relating to stockholder dividends and distributions and other permanent book and tax differences are reclassified to paid-in capital.
If we do not distribute (or are not deemed to have distributed) at least 98% of our annual taxable income in the calendar year earned, we will generally be required to pay an excise tax equal to 4% of the amount by which 98% of our annual taxable income exceeds the distributions from such taxable income for the year. To the extent that we determine that our estimated current year annual taxable income will be in excess of estimated current year dividend distributions from such taxable income, we accrue excise taxes, if any, on estimated excess taxable income as taxable income is earned using an annual effective excise tax rate. The annual effective excise tax rate is determined by dividing the estimated annual excise tax by the estimated annual taxable income.
We adopted FASB ASC 740, *Income Taxes* (ASC 740). ASC 740 provides guidance for how uncertain tax positions should be recognized, measured, presented, and disclosed in the financial statements. ASC 740 requires the evaluation of tax positions taken or expected to be taken in the course of preparing our tax returns to determine whether the tax

positions are more-likely-than-not of being sustained by the applicable tax authority. Tax positions not deemed to meet the more-likely-than-not threshold are recorded as a tax benefit or expense in the current year. Adoption of ASC 740 was applied to all open tax years as of July 1, 2007. The adoption of ASC 740 did not have an effect on our net asset value, financial condition or results of operations as there was no liability for unrecognized tax benefits and no change to our beginning net asset value. As of December 31, 2010 and for the three and six months then ended, we did not have a liability for any unrecognized tax benefits. Management s determinations regarding ASC 740 may be subject to review and adjustment at a later date based upon factors including, but not limited to, an on-going analysis of tax laws, regulations and interpretations thereof.

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Revenue Recognition

Realized gains or losses on the sale of investments are calculated using the specific identification method.

Interest income, adjusted for amortization of premium and accretion of discount, is recorded on an accrual basis. Origination, closing and/or commitment fees associated with investments in portfolio companies are accreted into interest income over the respective terms of the applicable loans. Upon the prepayment of a loan or debt security, any prepayment penalties and unamortized loan origination, closing and commitment fees are recorded as interest income.

Loans are placed on non-accrual status when there is reasonable doubt that principal or interest will not be collected in accordance with the terms of the investment. Accrued interest is generally reversed when a loan is placed on non-accrual status. Interest payments received on non-accrual loans may be recognized as income or applied to principal depending upon management s judgment. Non-accrual loans are restored to accrual status when past due principal and interest is paid and in management s judgment, are likely to remain current. As of December 31, 2010, approximately 2.3% of our net assets are in non-accrual status.

Dividend income is recorded on the ex-dividend date.

Structuring fees and similar fees are recognized as income as earned, usually when paid. Structuring fees, excess deal deposits, net profits interests and overriding royalty interests are included in other income.

Dividends and Distributions

Dividends and distributions to common stockholders are recorded on the ex-dividend date. The amount, if any, to be paid as a monthly dividend or distribution is approved by our Board of Directors quarterly and is generally based upon our management s estimate of our earnings for the quarter. Net realized capital gains, if any, are distributed at least annually.

Financing Costs

We record origination expenses related to our credit facility and the Senior Convertible Notes as deferred financing costs. These expenses are deferred and amortized as part of interest expense using the straight-line method for our revolving credit facility and the effective interest method for our Senior Convertible Notes, over the respective stated life.

We record registration expenses related to shelf filings as prepaid assets. These expenses consist principally of Securities and Exchange Commission (SEC) registration fees, legal fees and accounting fees incurred. These prepaid assets will be charged to capital upon the receipt of an equity offering proceeds or charged to expense if no offering completed.

Senior Convertible Notes

We have recorded the Senior Convertible Notes (See Note 6 to our consolidated financial statements.) at their contractual amounts. The Senior Convertible Notes were analyzed for any features that would require its accounting to be bifurcated and they were determined to be immaterial.

Guarantees and Indemnification Agreements

We follow FASB ASC 460, *Guarantees* (ASC 460). ASC 460 elaborates on the disclosure requirements of a guarantor in its interim and annual financial statements about its obligations under certain guarantees that it has issued. It also requires a guarantor to recognize, at the inception of a guarantee, for those guarantees that are covered by ASC 460, the fair value of the obligation undertaken in issuing certain guarantees. ASC 460 did not have a material effect on the financial statements.

Per Share Information

Net increase or decrease in net assets resulting from operations per common share are calculated using the weighted average number of common shares outstanding for the period presented. In accordance with ASC 946, *Financial Services Investment Companies*, convertible securities are not considered in the calculation of net assets per share.

Recent Accounting Pronouncements

In June 2009, the FASB issued ASC 860, *Accounting for Transfers of Financial Assets an amendment to FAS 140* (ASC 860). ASC 860 improves the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets: the effects of a transfer on its financial position, financial performance, and cash flows: and a transferor s continuing involvement, if any, in transferred financial assets. ASC 860 is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. The adoption of this standard had no effect on our results of operation or our financial position.

In June 2009, the FASB issued ASC 810, *Consolidation* (ASC 810). ASC 810 is intended to (1) address the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities, as a result of the elimination of the qualifying special-purpose entity concept in ASC 860, and (2) constituent concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accounting and disclosures under the Interpretation do not always provided timely and useful information about an enterprise s involvement in a variable interest entity. ASC 810 is effective as of the beginning of our first annual reporting period that begins after November 15, 2009. The adoption of this standard had no effect on our results of operation or our financial position.

In January 2010, the FASB issued Accounting Standards Update 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASC 2010-06). ASU 2010-06 amends ASC 820-10 and clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements and employers disclosures about postretirement benefit plan assets. ASU 2010-06 is effective December 15, 2009, except for the disclosure about purchase, sales, issuances and settlements in the roll forward of activity in level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. We do not believe that the adoption of the amended guidance in ASC 820-10 will have a significant effect on our financial statements.

In February 2010, the FASB issued Accounting Standards Update 2010-10, *Consolidation (Topic 810) - Amendments for Certain Investments Funds* (ASU 2010-10), which defers the application of the consolidation guidance in ASC 810 for certain investments funds. The disclosure requirements continue to apply to all entities. ASU 2010-10 is effective as of the beginning of the first annual period that begins after November 15, 2009 and for interim periods within that first annual period. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-21, *Accounting for Technical Amendments to Various SEC Rules and Schedules* (ASU 2010-21). This Accounting Standards Update various SEC paragraphs pursuant to the issuance of Release No. 33-9026: Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies. The adoption of this standard had no effect on our results of operation or our financial position.

In August 2010, the FASB issued Accounting Standards Update 2010-22, Accounting for Various Topics - Technical Corrections to SEC Paragraphs (ASU 2010-22). ASU 2010-22 amends various SEC paragraphs based on external comments received and the issuance of Staff Accounting Bulletin (SAB) 112, which amends or rescinds portions of certain SAB topics. The adoption of this standard had no effect on our results of operation or our financial position.

In December 2010, the FASB issued Accounting Standards Update 2010-29, *Business Combinations (Topic 805) Disclosure of Supplementary Pro Forma Information for Business Combinations (a consensus of the FASM Emerging Issues Task Force* (ASU 2010-29). ASU 2010-29 addresses diversity in practice about the interpretation of pro forma revenue and earnings disclosure requirements for business combinations. The amended guidance in ASU 2010-29 specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior reporting period only. This standard also expands the supplemental pro forma disclosures under ASC 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments in ASU 2010-29 are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010, with early adoption permitted. Our management does not believe that the adoption of the amended guidance in ASU 2010-29 will have a significant effect on our financial statements

Patriot Acquisition

On December 2, 2009, we acquired the outstanding shares of Patriot Capital Funding, Inc. (Patriot) common stock for $201,083. Under the terms of the merger agreement, Patriot common shareholders received 0.363992 shares of our common stock for each share of Patriot common stock, resulting in 8,444,068 shares of common stock being issued by us. In connection with the transaction, we repaid all the outstanding borrowings of Patriot, in compliance with the merger agreement.

On December 2, 2009, Patriot made a final dividend equal to its undistributed net ordinary income and capital gains of $0.38 per share. In accordance with a recent IRS revenue procedure, the dividend was paid 10% in cash and 90% in newly issued shares of Patriot s common stock. The exchange ratio was adjusted to give effect to the final income distribution.

The merger has been accounted for as an acquisition of Patriot by Prospect Capital Corporation (Prospect) in accordance with acquisition method of accounting as detailed in Accounting Standards Codification (ASC or Codification) 805, *Business Combinations* (ASC 805). The fair value of the consideration paid was allocated to the assets acquired and liabilities assumed based on their fair values as the date of acquisition. As described in more detail in ASC 805, goodwill, if any, would have been recognized as of the acquisition date, if the consideration transferred exceeded the fair value of identifiable net assets acquired. As of the acquisition date, the fair value of the identifiable net assets acquired exceeded the fair value of the consideration transferred, and we recognized the excess as a gain. A preliminary gain of $5,714 was recorded by Prospect in the quarter ended December 31, 2009 related to the acquisition of Patriot, which was revised in the fourth quarter of Fiscal 2010, to $7,708, when we settled severance accruals related to certain members of Patriot s top management, and finalized during the first quarter of Fiscal 2011, to $8,632, when we settled the remaining severance accruals related to the last two members of Patriot s top management. Under ASC 805, the adjustments to our preliminary estimates were reflected in the three months ended December 31, 2009 (See Note 13 to our consolidated financial statements.). The acquisition of Patriot was negotiated in July 2009 with the purchase agreement being signed on August 3, 2009. Between July 2009 and December 2, 2009, our valuation of certain of the investments acquired from Patriot increased due to market improvement, which resulted in the recognition of the gain