# The Gabelli Small Cap Growth Fund
## Shareholder Commentary
## September 30, 2017

**Mario J. Gabelli, CFA**
**Portfolio Manager**

**To Our Shareholders,**

For the quarter ended September 30, 2017, the net asset value ("NAV") per Class AAA Share of The Gabelli Small Cap Growth Fund increased 7.2% compared with an increase of 5.7% for the Russell 2000 Index. See page 2 for additional performance information.

**Politics, the Economy and the Markets**

The U.S. stock market advanced to record highs in September, with the S&P 500 in positive territory for an eighth consecutive quarter. The fundamental narrative remains favorable, thanks in large part to an upswing in global growth and still supportive global monetary policy. Economic indicators continue to point upwards around the world, with low inflation, falling unemployment and rising consumer spending all contributing to the stock market's rise. Reported second quarter earnings were, by and large, better than expected, with many companies beating sales and earnings forecasts and reaffirming or raising full year guidance. Furthermore, the weak dollar is helping to increase reported overseas profits for U.S. based multinationals, and could potentially boost U.S. exports.

The Trump administration's policies came back into focus during the quarter with the announcement of a deal to extend the debt ceiling and the release of a highly anticipated tax reform blueprint. More surprising than the across the aisle handshake from President Trump and Democrats on the debt ceiling agreement was the market's positive reaction to tax cut expectations, the possibility of which had been dwindling after several legislative setbacks on healthcare reform. The discussion around tax reform spurred renewed momentum around reflation trades and hope for fiscal stimulus. If a bill resembling the current plan is passed, it will likely be a boon for the U.S. economy and stock market, with industrial companies and domestic-oriented, full cash tax paying small cap stocks being among the biggest winners. Consumer spending may also get a boost from reductions in rates for individuals. Ultimately, the devil is in the details, and the Trump administration has not yet shown ability to advance much of its agenda, but we remain cautiously optimistic that taxes for individuals and corporations will be lower in 2018.

## Comparative Results

**Average Annual Returns through September 30, 2017 (a)(b)**

| | Quarter | 1 Year | 5 Year | 10 Year | 15 Year | Since Inception (10/22/91) |
|---|---|---|---|---|---|---|
| **Class AAA (GABSX)** | 7.22% | 21.56% | 13.78% | 8.66% | 12.30% | 12.78% |
| Russell 2000 Index | 5.67 | 20.74 | 13.79 | 7.85 | 11.37 | 9.93 |
| **Class A (GCASX)** | 7.21 | 21.55 | 13.78 | 8.66 | 12.30 | 12.78 |
| With sales charge (c) | 1.04 | 14.56 | 12.44 | 8.02 | 11.86 | 12.52 |
| **Class C (GCCSX)** | 7.03 | 20.65 | 12.93 | 7.86 | 11.54 | 12.34 |
| With contingent deferred sales charge (d) | 6.03 | 19.65 | 12.93 | 7.86 | 11.54 | 12.34 |
| **Class I (GACIX)** | 7.28 | 21.84 | 14.06 | 8.93 | 12.49 | 12.89 |
| **Class T (GATIZX** | 3.66 | 21.56 | 13.78 | 8.66 | 12.30 | 12.78 |
| With sales charge (e) | 1.07 | 18.52 | 13.20 | 8.39 | 12.11 | 12.02 |

**In the current prospectuses dated January 27, 2017, the expense ratios for Class AAA, A, C, I, and T Shares are 1.39%, 1.39%, 2.14%, 1.14%, and 1.39%, respectively. Class AAA and Class I Shares have no sales charge. The maximum sales charge for Class A Shares, Class C Shares, and Class T Shares is 5.75%, 1.00%, and 2.50%, respectively.**

(a) *Returns represent past performance and do not guarantee future results. Total returns and average annual returns reflect changes in share price, reinvestment of distributions, and are net of expenses. Investment returns and the principal value of an investment will fluctuate. When shares are redeemed, they may be worth more or less than their original cost. Current performance may be lower or higher than the performance data presented. Visit www.gabelli.com for performance information as of the most recent month end. Returns would have been lower had the Adviser not reimbursed certain expenses of the Fund. The Fund imposes a 2% redemption fee on shares sold or exchanged within seven days of purchase. Performance returns for periods of less than one year are not annualized. Investors should carefully consider the investment objectives, risks, charges, and expenses of the Fund before investing. The prospectuses contain information about these and other matters and should be read carefully before investing. To obtain a prospectus, please visit our website at www.gabelli.com.* The Class AAA Share NAVs are used to calculate performance for the periods prior to the issuance of Class A Shares and Class C Shares on December 31, 2003, Class I Shares on January 11, 2008, and Class T Shares on July 5, 2017. The actual performance of the Class A Shares, Class C Shares, and Class T Shares would have been lower due to the additional fees and expenses associated with these classes of shares. The actual performance of the Class I Shares would have been higher due to lower expenses related to this class of shares. Investing in small capitalization securities involves special risks because these securities may trade less frequently and experience more abrupt price movements than large capitalization securities. The Russell 2000 Index is an unmanaged indicator which measures the performance of the small-cap segment of the U.S. equity market. Dividends are considered reinvested. You cannot invest directly in an index.
(b) The Fund's fiscal year ends September 30.
(c) Performance results include the effect of the maximum 5.75% sales charge at the beginning of the period.
(d) Assuming payment of the 1% maximum contingent deferred sales charge imposed on redemptions made within one year of purchase.
(e) Performance results include the effect of the maximum 2.50% sales charge at the beginning of the period.

We have separated the portfolio manager's commentary from the financial statements and investment portfolio due to corporate governance regulations stipulated by the Sarbanes-Oxley Act of 2002. We have done this to ensure that the content of the portfolio manager's commentary is unrestricted. The financial statements and investment portfolio are mailed separately from the commentary. Both the commentary and the financial statements, including the portfolio of investments, are available on our website at www.gabelli.com.

Of course, risks always remain, most notably the very public nuclear brinksmanship with North Korea. Any military conflict that could occur has the potential to carry with it an enormous human cost in terms of loss of life. While of lesser importance, it would likely result in a sharp decline in stock prices as well. We are hopeful that a diplomatic solution prevails, and note that in this new era of uncertain geopolitical dynamics, military spending will likely remain robust for years to come.

**Deals, Deals & More Deals**

Merger and acquisition (M&A) activity, while still robust, has not meaningfully accelerated under the Trump administration, as CEOs and boards wait for more clarity on taxes and potential regulatory scrutiny. Worldwide M&A activity totaled $2.4 trillion during the first nine months of 2017, a 3% increase compared to the first nine months of 2016. Overall, 35,360 worldwide deals were announced during the first nine months of 2017, flat compared to a year ago. As soon as policy uncertainties in Washington regarding corporate tax reform, international trade, and various industry reform and deregulation initiatives begins to lift, a resurgence in deal making may start.

**Let's Talk Stocks**

The following are stock specifics on selected holdings of our Fund. Favorable earnings prospects do not necessarily translate into higher stock prices, but they do express a positive trend that we believe will develop over time. Individual securities mentioned are not necessarily representative of the entire portfolio. For the following holdings, the share prices are listed first in United States dollars (USD) and second in the local currency, where applicable, and are presented as of September 30, 2017.

*Ferro Corp. (1.3% of net assets as of September 30, 2017) (FOE – $22.30 – NYSE)* has transformed itself into a specialty materials company focusing on glass technology and colors. The company's end markets include consumer, electronics, construction, automotive, and appliances. Following several divestitures, Ferro's remaining portfolio is fully concentrated on its core technologies: coatings, color and glass science. Highly accretive acquisitions have joined the fold; they brought new products, geographic expansion, entry into new markets, and the needed capacity in certain areas. Having cut costs and upgraded its portfolio, Ferro has now moved into its next phase: the "optimization" program consists of 1) manufacturing efficiencies, 2) having the right capacity at the right place in order to better serve customers, 3) emphasizing high-end products, and 4) successfully cross-selling the recently acquired product lines. The company's balance sheet remains conservative and we anticipate additional accretive acquisitions; management expects to invest, on average, $100-$150 million annually, and we believe that it has a strong backlog of attractive businesses. Since 2013 EBITDA margin has improved from 8.9% to 17.1% in 2016; we conservatively project that it will reach 18.7% in 2020. Ferro is pursuing its valuation-creating strategy by adding accretive properties and focusing on innovation, growth, and efficiencies in its core operations. Ferro recently announced its pending acquisition of Endeka, a producer of high-value coatings for the ceramic tiles market: the acquisition price of $75 million represents an attractive multiple of 5.7x EBITDA of $13 million; we estimate that the acquisition could add $0.04-$0.05 to our current 2018 EPS of $1.40. Excluding Endeka and any future acquisitions, we estimate EPS of $1.25, $1.40, and $1.55 for 2017, 2018, and 2020, respectively; we calculate a 2019 PMV of $24 going to $28 based on our 2020 projections.

*Kaman Corp. (1.3%) (KAMN – $55.78 – NYSE)* is a diversified company serving the aerospace, defense, and industrial markets. The Aerospace segment manufactures aircraft bearings, precision fuses, helicopter components, and subcontracted aero structure work. In the Distribution segment, the company distributes power transmission, motion control, and material handling products to a broad range of industries. Aerospace is expected to benefit from increased fusing demand caused by ongoing geopolitical instability.

*Kikkoman Corp. (1.1%) (2801 – $30.75/¥3,460 – Tokyo Stock Exchange)*, based just outside of Tokyo, Japan, is the world's largest producer of soy sauce and soy-based condiments, with a history going back to 1607. The company has been successful in expanding overseas, particularly in the U.S.; 80% of operating profit now comes from non-Japan sources. Currently, expansion efforts center on Europe, where operating margins are surprisingly high; 14% vs. 2% in Japan. Kikkoman also owns JFC International, the largest wholesaler of Japanese and Asian food products outside of Japan. The growing popularization of Japanese cuisine, especially in the developed markets of North America, Europe, and Asia, is likely to sustain growth in the medium and longer term.

*Maple Leaf Foods (0.9%) (MFI – $27.26/CAD$34.01 – Toronto Stock Exchange)* is the largest Canadian processor of fresh and prepared pork and poultry products, with over 40% market share of Canada's $4-$5 billion processed pork market. Through a series of asset sales over the past several years, Maple Leaf has transformed from a conglomerate operating in a wide range of businesses (animal nutrition, animal by-product recycling, fresh and frozen bakery, and hog production) to a pure-play protein company. With these divestitures completed, the company has minimal debt and holds a significant amount of cash, which we expect it to use for accretive bolt-on acquisitions, such as its recent purchase of Lightlife Foods, a leader in plant-based meat alternatives. Additionally, Maple Leaf has invested significant capital to modernize an aging and inefficient manufacturing and distribution network. We believe that this modernization, which is now complete, will drive significantly higher profitability and act as a catalyst for shares.

*Myers Industries Inc. (0.3%) (MYE – $20.95 – NYSE)* is an Akron, Ohio-based multi-industry manufacturer and distributor of a variety of consumable products. The company's leading portfolios of branded products are in two segments: Material Handling and Distribution. After a series of acquisitions and divestitures over the past several years, Myers should thrive, as new CEO David Banyard sets a new strategy to increase market share and optimize operations in both segments. Ultimately, we see a potential separation of Material Handling and Distribution as a way to surface value for investors.

*PNM Resources (1.3%) (PNM – $40.30 – NYSE)*, based in Albuquerque, New Mexico, is the holding company for regulated electric utilities Public Service Company of New Mexico (PSNM) and Texas-New Mexico Power Company (TNMP). PSNM serves 520,000 customers in and around Albuquerque, Rio Rancho and Santa Fe and owns 2,800 MWs (15% nuclear) of generation. TNMP is a distribution/transmission company and serves 247,000 customers in three non-contiguous areas of Texas. PSNM is awaiting regulatory approval of a rate settlement calling for a $32 million revenue increase in 2018 and an additional $30 million in 2019 based on a 9.575% allowed ROE. Higher rates are necessary to recognize its environmental plan, the addition of Palo Verde 3 at $1,118/kW ($150 million) into rate base, other investments, and declining sales. Importantly, the request was based on a future 2018 test year. PNM targets earnings growth of 7%-8% and outlines 2018 and 2019 earnings power ranges of $1.68-$1.76 per share and $2.00-$2.18 per share, respectively, based on an earned 9.575% ROE.

*RPC, Inc. (1.4%) (RES – $24.79 – NYSE)* based in Atlanta, Georgia, provides a broad range of specialized oilfield services and equipment (such as pressure pumping, coiled tubing, rental tools, etc.) to independent and major oil and gas companies engaged in the exploration, production and development of oil and gas properties throughout the United States. We have entered the part of the recovery cycle where quality pressure pumpers such as RPC make outsized profitability (over 40% incremental margins). The company plans to have its full fleet of 927,000 horsepower active and ready to work by the end of 3Q'17. After suspending its quarterly dividend during the downturn to preserve its balance sheet, RPC resumed paying a $0.06/share dividend in 2Q'17. Further, we would not be surprised if the company also paid a special yearend dividend, similar to last year. Our 2018P PMV is $29 per share.

*Ryman Hospitality Properties Inc. (0.9%) (RHP – $62.49 – NYSE)* is the owner/operator of four large convention-centric hotels under the Gaylord brand. It also owns the Opryland brand and entertainment complex in Nashville, the city of its origin. As such, it has benefited from the growth in country music and consumer preference for live entertainment. The company's hotels are group-centric, and revenues and bookings have remained strong due to its long and steady economic expansion in the United States. Future growth should come from 8 new hotels (probably established as joint ventures) as well as the development of additional live entertainment venues, one of which will open in Times Square in New York City later this year. The company recently converted to a real estate investment trust (REIT), providing an extra level of tax efficiency to enhance its investment attraction. Given the low level of interest rates, the company's tax efficient dividend stream provides significant investor protection, as does the consistency of its cash flow.

**Conclusion**

Markets continue to climb, but risks – geopolitical and otherwise – as always remain. We continue to seek high-quality companies trading at a discount to Private Market Value – the price an informed industrialist would pay to own an entire business – and hope to use any opportunity "Mr. Market" provides to us. We also look for catalysts to surface value, such as industry consolidation, financial engineering, new management, regulatory changes, or a change in cash flow allocation. Finally, tax reform has the potential to increase consumer spending, corporate profits, and lead to an acceleration of deal making activity.

October 27, 2017

**Top Ten Holdings** **(Percent of Net Assets)**
**September 30, 2017**

| | | | |
|---|---|---|---|
| Navistar International Corp. | 1.6% | Curtiss-Wright Corp. | 1.2% |
| RPC Inc. | 1.4% | Live Nation Entertainment Inc. | 1.2% |
| Ferro Corp. | 1.4% | Aerojet Rocketdyne Holdings, Inc. | 1.2% |
| PNM Resources Inc. | 1.3% | Tyler Technologies Inc. | 1.1% |
| Kaman Corp. | 1.3% | Interpublic Group of Cos., Inc. | 1.1% |

**Note:** The views expressed in this Shareholder Commentary reflect those of the Portfolio Manager only through the end of the period stated in this Shareholder Commentary. The Portfolio Manager's views are subject to change at any time based on market and other conditions. The information in this Portfolio Manager's Shareholder Commentary represents the opinions of the individual Portfolio Manager and is not intended to be a forecast of future events, a guarantee of future results, or investment advice. Views expressed are those of the Portfolio Manager and may differ from those of other portfolio managers or of the Firm as a whole. This Shareholder Commentary does not constitute an offer of any transaction in any securities. Any recommendation contained herein may not be suitable for all investors. Information contained in this Shareholder Commentary has been obtained from sources we believe to be reliable, but cannot be guaranteed.

**Minimum Initial Investment – $1,000**

The Fund's minimum initial investment for regular accounts is $1,000. There are no subsequent investment minimums. No initial minimum is required for those establishing an Automatic Investment Plan. Additionally, the Fund and other Gabelli/GAMCO Funds are available through the no-transaction fee programs at many major brokerage firms. The Fund imposes a 2% redemption fee on shares sold or exchanged within seven days after the date of purchase. See the prospectuses for more details.

**www.gabelli.com**

Please visit us on the Internet. Our homepage at www.gabelli.com contains information about GAMCO Investors, Inc., the Gabelli/GAMCO Mutual Funds, IRAs, 401(k)s, current and historical quarterly reports, closing prices, and other current news. We welcome your comments and questions via e-mail at info@gabelli.com.

You may sign up for our e-mail alerts at www.gabelli.com and receive early notice of quarterly report availability, news events, media sightings, and mutual fund prices and performance.

The Fund's daily NAVs are available in the financial press and each evening after 7:00 PM (Eastern Time) by calling 800-GABELLI (800-422-3554). Please call us during the business day, between 8:00 AM – 7:00 PM (Eastern Time), for further information.

**e-delivery**

We are pleased to offer electronic delivery of Gabelli fund documents. Direct shareholders of our mutual funds can elect to receive their Annual and Semiannual Reports, Manager Commentaries, and Prospectus via e-delivery. For more information or to sign up for e-delivery, please visit our website at www.gabelli.com.

**Multi-Class Shares**

The Gabelli Small Cap Growth Fund began offering additional classes of Fund shares on December 31, 2003. Class AAA Shares are no-load shares offered directly through selected broker/dealers. Class A, Class C, and Class T Shares are targeted to the needs of investors who seek advice through financial consultants. Class I Shares are available directly through the Fund's distributor or brokers that have entered into selling agreements specifically with respect to Class I Shares. The Board of Directors determined that expanding the types of Fund shares available through various distribution options will enhance the ability of the Fund to attract additional investors.

## Portfolio Manager Biography

**Mario J. Gabelli, CFA,** is Chairman, Chief Executive Officer, and Chief Investment Officer – Value Portfolios of GAMCO Investors, Inc. that he founded in 1977, and Chief Investment Officer – Value Portfolios of Gabelli Funds, LLC and GAMCO Asset Management Inc. He is also Executive Chairman of the Board of Directors of Associated Capital Group, Inc. Mr. Gabelli is a summa cum laude graduate of Fordham University and holds an MBA degree from Columbia Business School, and Honorary Doctorates from Fordham University and Roger Williams University.

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# THE GABELLI SMALL CAP GROWTH FUND

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