Gabelli ESG Fund, Inc.

Shareholder Commentary
December 31, 2018

(Y)our Portfolio Management Team

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To Our Shareholders,

For the quarter ended December 31, 2018, the net asset value (NAV) per Class AAA Share of the Gabelli ESG Fund decreased 14.4% compared with decreases of 13.5% and 14.3% for the Standard & Poor's (S&P) 500 Index and the Russell 3000 Index, respectively. Other classes of shares are available. See page 2 for additional performance information for all classes.

Environmental, Social, and Governance (ESG) Investing

Environmental, social, and governance (ESG) refers to the three main areas of concern that have developed as central factors in measuring the sustainability and ethical impact of an investment in a business. Incorporating ESG factors into company research can help understand risks and opportunities that may otherwise have been overlooked, and improve the return profile of investment portfolios. ESG analysis differs from a traditional socially responsive investing (SRI) screen in that it does not apply a "negative screen," excluding companies that engage in specific unwanted activities (such as selling tobacco or weapons). Instead, it takes a holistic approach, evaluating a company's performance in a variety of areas, including carbon emissions, energy efficiency, water stress, human capital development, chemical safety, board independence, management pay practices, and business ethics.

Comparative Results

Average Annual Returns through December 31, 2018 (a)(b)

	Quarter	1 Year	3 Year	5 Year	10 Year	Since Inception (6/1/07)
Class AAA (SRIGX)	(14.44)%	(15.83)%	1.72%	1.98%	9.79%	4.37%
S&P 500 Index	(13.52)	(4.38)	9.26	8.49	13.12	6.57
Russell 3000 Index	(14.30)	(5.24)	8.97	7.91	13.18	6.50
Class A (SRIAX)	(14.45)	(15.79)	1.73	1.98	9.80	4.38
With sales charge (c)	(19.36)	(20.63)	(0.26)	0.78	9.15	3.85
Class C (SRICX)	(14.64)	(16.48)	0.97	1.20	8.96	3.59
With contingent deferred sales charge (d)	(15.49)	(17.32)	0.97	1.20	8.96	3.59
Class I (SRIDX)	(14.44)	(15.64)	1.97	2.21	10.06	4.63

In the current prospectuses dated July 30, 2018, as amended August 7, 2018, and February 1, 2019, the gross expense ratios for Class AAA, A, C, and I are 1.75%, 1.75%, 2.50%, and 1.50% respectively, and the net expense ratios for these share classes after contractual reimbursements by Gabelli Funds, LLC, (the "Adviser") are 1.27%, 1.27%, 2.02%, and 1.02% respectively. Class AAA and I Shares do not have a sales charge. The maximum sales charge for Class A Shares and Class C Shares is 5.75%, and 1.00%, 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 S&P 500 Index is a market capitalization weighted index of 500 large capitalization stocks commonly used to represent the U.S. equity market. The Russell 3000 Index is an unmanaged indicator that measures the performance of the 3,000 largest U.S. traded stocks, in which the underlying companies are incorporated in the U.S. The MSCI AC World Index is an unmanaged market capitalization weighted index representing both developed and emerging markets. Dividends are considered reinvested. You cannot invest directly in an index.

(b) The Fund's fiscal year ends March 31.

(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.

We have separated the portfolio managers' 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 managers' commentary is unrestricted. Both the commentary and the financial statements, including the portfolio of investments, are available on our website at www.gabelli.com.

Introduction

For most of the last decade we have lived in what has often been termed a "Goldilocks economy." Much as the fair-haired, home-invading subject of the children's story found one bowl of porridge to be "just right," economic growth and inflation has been neither too hot nor too cold[1]. During this time, coordinated action by the world's central banks kept interest rates near zero and the prices of nearly all asset classes high. The U.S. economy is in its 113th month of expansion, seven months short of the record. Until the fourth quarter stumble, U.S. equities were 119 months into the longest-ever bull market, led mostly by growth stocks riding a global wave of technological innovation and expanding prosperity. Except for growth scares in 2011, 2015, and perhaps one day in November 2016, the market's volatility has been low and the market's upward trajectory largely uninterrupted. There are signs, however, that the narrative may be changing, as a turn in the aging business cycle may be accompanied by a wholesale shift in socio-political regimes from globalism to nationalism and capital to labor. Populism is on the march around the world with long-term effects that are unclear, but unlikely to be positive for equities. As in the story, the bears will eventually return home; their timing and mood is uncertain, as is how much of this eventuality the market has already discounted. Against this backdrop we believe bottom-up, fundamental stock selection of the type we have practiced for over 40 years remains more important than ever.

The Political Economy of 2018

The most salient issue for the market is growth - with corporate tax cuts behind us and little slack left in the economy, real growth will almost certainly slow from the 3.4% posted in Q3 2018. That does not necessarily imply a recession, defined as two consecutive quarters of contraction, is on the immediate horizon. How far above or below the approximately 2% real growth that population and productivity gains suggest is "just right" depends on many factors, including what we have described variously as Three T's: Trade, Treasuries, and Trump.

Trade

President Trump made "fair trade" the centerpiece of his election campaign, and he has thus far made good on his promise to challenge the prevailing post-war "free trade" orthodoxy (however illusory that reality might have been). Hope for a trade deal with China rose when the administration renegotiated NAFTA, now called USMCA (the initials of its U.S., Mexican and Canadian signatories), the market understandably zags with each hint that a China deal could emerge since China accounts for nearly half of the $600 billion U.S. trade deficit, and remains our third largest export destination. The situation takes on even greater significance due to China's role as an engine for global growth. China is slowing as it faces domestic structural imbalances. Pressure from President Trump exacerbates those issues, but a deal will not solve them nor heal the lasting damage done to the Sino-American symbiosis.

[1]"Goldilocks and the Three Bears" was a hoary tale first recorded by poet Robert Southey in 1837. Market commentator use of the analogy dates to at least the late-1990s expansion.

Treasuries

Also critical to the outlook for the economy and stocks are the level and trajectory of interest rates. Since the Federal Reserve began its taper four years ago in October 2014, the ten-year U.S. Treasury rate breached 3% this year for the first time since 2013, standing now just below that level. Higher interest rates have real world impacts – they make the purchases of new homes, cars, capital equipment, and companies more expensive to finance. All else equal, higher rates reduce the value of risk assets by making the alternative home for capital, "riskless" Treasuries, more attractive. The term structure of interest rates (aka the yield curve) has also been ascribed predictive powers. Inverted curves – situations in which the two-year yield exceeds the ten-year yield – have predicted all nine recessions since 1955, albeit with two false positives and a wide variation in timing. The virtually flat yield curve today thus worries some observers.

Trump

While there has always been a healthy interplay between markets and political figures, President Trump's twitter habit, unpredictability, and the potential legal challenges to his presidency have made him more of a focus than past leaders. Among the concerns for the next two years is how a Democratic Congress with no interest in helping Trump get re-elected approves the USMCA, a debt ceiling extension, and further fiscal stimulus, especially when the ask may be a tweak to the tax cuts. Interestingly, the War on Tech (i.e., privacy and anti-trust investigations of Facebook, Google, Amazon, and others) seems to be one of the few issues with bipartisan support and worth watching in 2019. Geopolitical disruption is not unique to the U.S.: if and how the U.K. exits the European Union, the precarious positions of leaders in Germany, France and Italy, not to mention the typical entanglements in the Middle East, also remain a focus.

Skeptics Could Be Wrong If Things Go Right

Not all news – whether real or fake – is bad of course. In fact, many economic indicators are quite strong, with 3.7% unemployment the lowest since the tumult of 1969, record consumer net worth ($109 trillion) and interest rates and inflation that, viewed over a longer time frame, remain quite tame. The Federal Reserve and the President are probably not past the point of no return and still have not lost policy control: President Trump, who possesses a keen sensitivity to the stock market, could resolve the trade war and the Fed could blink on 2019 rate hikes. That would leave reason to believe the expansion could continue and that the current state of the market is the pause, like the previous ones in this cycle, that refreshes.

Mr. Market

Causation, Correlation or Neither

The S&P 500 finished 2018 down 4.4% and the small capitalization Russell 2000 index was down 11%, with each off 13.5% and 20.2% in the fourth quarter, respectively. The performance of the S&P 500, dominated by six technology stocks (Facebook, Amazon, Netflix, Google, Microsoft, and Apple – the "FANGMA") that comprise 15% of its weight, masked the more significant declines posted by a broader group of stocks.

Approximately two-thirds of stocks in the S&P 500 are negative this year, with one-third down more than 20%. Even the vaunted FANGMA is now 25% off its highs, adding credence to the notion that the global growth trend may be broken. "Buy the Dip" has morphed to "Sell the Rip."

Market declines of this magnitude could be expected to impart a negative wealth effect, i.e., consumers with slimmer brokerage statements feeling less inclined to make discretionary purchases, which could exacerbate an economic slowdown, but market declines are more often simply a precursor, not a trigger, of recessions. Since 1929, there have been sixteen bear markets with most, though not all, pacing a recession by approximately one year, with the recession-less crash of October 1987 a notable exception. It is also worth stating that the market does not equal the economy. Just as some have suggested Wall Street. prospered without much of Main Street over the last decade, the reverse could conceivably prove true.

Valuation Today vs. Five Years Out

In any case, stocks are already pricing a slowdown and/or higher rates. A flat year-to-date equity market, compared with estimated EPS gains of 22% in 2018 and 8% in 2019, implies a contraction in forward multiples from 18x at the end of 2017 to roughly 15x today. That is at the low end of historical multiples during periods with inflation in the 0%-3% area. This suggests that the market as a whole does not appear expensive. We do not buy the "market," but we are finding a lot of bargains in individual stocks recently.

Rx for Investors

What is an investor in a choppy environment, lacking a reliable crystal ball, to do? Historically, it has proven foolish to attempt to time the market, especially based on macroeconomic data. In 2009, for example, the market rallied 36% between its bottom in March and the June end to the recession. None of this is to suggest investors should ignore their positioning in an evolving environment.

Indeed, we believe we are poised to capitalize from change. Historically we have gravitated toward companies with characteristics such as pricing power, stable cash flows, solid managements and resilient balance sheets – factors which may not have been appreciated in a zero inflation, easy money world. Higher interest rates and greater market volatility substantially increase the cost of capital even for the large internet companies. Combined with a possible economic slowdown, this should flush excess capital from the system, eliminating many of the seemingly disruptive companies backed by venture capital and accommodative capital markets to the benefit of those with truly sound business models and actual cash flow, rather than the promise of future cash flow. Finally, a change in market structure over the last decade, with an estimated 15% of U.S. equities managed passively, could accentuate any downside as withdrawals from ETFs retrace what was relentlessly bought on the way up. Our portfolio, which tends not to resemble what is represented in the popular ETFs, should be less susceptible to those forces, and the volatility that could be caused by a rush to the exit would present buying opportunities for active managers who conduct old fashioned research to uncover value.

Investment Scorecard

After strong performance in 2016 and 2017, 2018 was mostly forgettable from a stock perspective. The largest contributor to returns for the fourth quarter and the year was ConAgra (CAG) (3.6%) (4.6%, -42%) spin-off Lamb Weston (3.2% of net assets as of December 31, 2018) (3.0% average weighting in 2018, +32% for the year) which turned tight potato supply into strong sales and EPS growth and authorized a $250 million share repurchase. O'Reilly Automotive (1.7%) (1.4%, +43%) bounced back from 2017 concerns about the negative impact of moderate weather and Amazon's designs on the parts distribution business. eBay spin-off and online payment facilitator Paypal (4.1%) (3.1%, +14%) continued to benefit from the shift to e-commerce. Finally, new holding NextEra Energy (2.5%) (1.7%, +14%), the largest electric utility in the U.S. and the largest producer of wind and solar in the world, held up well amidst an uncertain backdrop.

With some exceptions, consumer staples stocks such as Conagra Brands and Edgewell Personal Care (1.4%) (2.4%, -37%) were weak as they faced changing consumer tastes, new competition, and headwinds from higher interest rates as former "bond proxies." Most of Conagra's decline occurred in December after it reported weaker than expected top line results for brands from recently acquired Pinnacle Foods – specifically, Birds Eye frozen vegetables, Duncan Hines baking items, and Wishbone salad dressing. Management believes it can turn around these brands (much as it has done for the stand alone ConAgra portfolio) but cautioned that improvement will probably not come until the back half of fiscal 2020 (ending May 30). While declining top line trends coupled with increased financial leverage are not welcome, we note that CAG is still an excellent free cash flow producer that now trades at one of the lowest multiples in the food sector. Any improvement in business trends should lead to outsized returns for equity holders. There were several detractors among industrial stocks with economic and trade sensitivity, including auto-efficiency specialist Tenneco (0.8%) (1.8%, -52%), infrastructure equipment rental firm HERC Holdings (0.9%) (1.2%, -58%) and building efficiency leader Johnson Controls (2.4%) (3.0%, -20%). Finally, Liberty Global (1.9%) (2.1, -39%), the largest cable operator in Europe, faced regulatory, economic, and execution headwinds despite agreeing to sell its second-largest market (Germany) to Vodafone (1.3%) at a multiple more than twice where the company now trades.

Conclusion

In our Q4 2017 letter we expressed surprise that a strong market was overlooking what seemed to be mounting risks late in the economic cycle. As many of those challenges - trade disputes, higher interest rates, political discord - play out, we wonder if the market is now ignoring what continue to be decent corporate fundamentals. Ultimately our job is to do the work on the microeconomic elements of each company and industry we cover, examine how the changing macroeconomic environment impacts those variables and make buy and sell decisions that balance the resulting opportunities and risks. Since the bears inevitably come home in each cycle, we have always erred on the side of capital preservation and that will especially be the case going forward. Children's stories don't always have happy endings but they serve as cautionary examples that we believe we have heeded well.

January 29, 2019

Top Ten Holdings (Percent of Net Assets)
December 31, 2018

Xylem Inc.	5.2%	Sony Corp.	3.4%
Danone SA	5.1%	Genuine Parts Co.	3.2%
Paypal Holdings Inc.	4.1%	Lamb Weston Holdings Inc.	3.2%
Mondelez International Inc.	3.9%	Watts Water Technologies Inc.	3.1%
Conagra Brands Inc.	3.6%	American Express Co.	3.0%

Note: The views expressed in this Shareholder Commentary reflect those of the Portfolio Managers only through the end of the period stated in this Shareholder Commentary. The Portfolio Managers' views are subject to change at any time based on market and other conditions. The information in this Shareholder Commentary represents the opinions of the Portfolio Managers 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 Managers 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.

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.

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.

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 Prospectuses via e-delivery. For more information or to sign up for e-delivery, please visit our website at www.gabelli.com.

Multi-Class Shares

Class AAA Shares are no-load shares offered directly through selected broker/dealers. Class A and Class C 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 would enhance the ability of the Fund to attract additional investors.

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Gabelli/GAMCO Funds and Your Personal Privacy

Who are we?

The Gabelli/GAMCO Funds are investment companies registered with the Securities and Exchange Commission under the Investment Company Act of 1940. We are managed by Gabelli Funds, LLC which is affiliated with GAMCO Investors, Inc., a publicly held company that has subsidiaries that provide investment advisory services for a variety of clients.

What kind of non-public information do we collect about you if you become a fund shareholder?

If you apply to open an account directly with us, you will be giving us some non-public information about yourself. The non-public information we collect about you is:

- *Information you give us on your application form.* This could include your name, address, telephone number, social security number, bank account number, and other information.
- *Information about your transactions with us, any transactions with our affiliates, and transactions with the entities we hire to provide services to you.* This would include information about the shares that you buy or redeem. If we hire someone else to provide services—like a transfer agent—we will also have information about the transactions that you conduct through them.

What information do we disclose and to whom do we disclose it?

We do not disclose any non-public personal information about our customers or former customers to anyone other than our affiliates, our service providers who need to know such information, and as otherwise permitted by law. If you want to find out what the law permits, you can read the privacy rules adopted by the Securities and Exchange Commission. They are in volume 17 of the Code of Federal Regulations, Part 248. The Commission often posts information about its regulations on its website, www.sec.gov.

What do we do to protect your personal information?

We restrict access to non-public personal information about you to the people who need to know that information in order to provide services to you or the fund and to ensure that we are complying with the laws governing the securities business. We maintain physical, electronic, and procedural safeguards to keep your personal information confidential.

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Portfolio Management Team Biographies

Christopher C. Desmarais joined GAMCO Investors, Inc. in 1993. Currently he is a Managing Director of GAMCO Asset Management Company, a portfolio manager of Gabelli Funds, LLC, as well as the Director of Socially Responsive Investments. His responsibilities also include marketing and client service of GAMCO's Value, Growth, and International capabilities for institutional, endowment, and family office clients as well as direct oversight of all of the Firm's SRI equity products. He is a graduate of Fairfield University with a B.A. in Economics.

Kevin V. Dreyer joined Gabelli in 2005 as a research analyst covering companies within the consumer sector. Currently he is a Managing Director and Co-Chief Investment Officer for GAMCO Investors, Inc.'s Value team. In addition, he serves as a portfolio manager of Gabelli Funds, LLC and manages several funds within the Gabelli/GAMCO Funds Complex. Mr. Dreyer received a B.S.E. from the University of Pennsylvania and an MBA from Columbia Business School.

Christopher J. Marangi joined Gabelli in 2003 as a research analyst. Currently he is a Managing Director and Co-Chief Investment Officer for GAMCO Investors, Inc.'s Value team. In addition, he serves as a portfolio manager of Gabelli Funds, LLC and manages several funds within the Gabelli/GAMCO Funds Complex. Mr. Marangi graduated magna cum laude and Phi Beta Kappa with a B.A. in Political Economy from Williams College and holds an MBA with honors from Columbia Business School.

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