

2017 Gladstone Capital Shareholder's Letter

To Our Shareholders,

We are pleased to share with you our positive results for the fiscal year ended September 30, 2017. During the fiscal year, we were able to deliver on three critical variables essential to sustaining the long term financial returns to you, our shareholders. We generated positive asset growth, maintained our average investment yields and portfolio quality, and reduced operating expenses. These factors combined to produce a 10% increase in net investment income for the year, which allowed us to maintain and cover 100% of all common shareholder dividends. We attribute much of this performance to our continued focus on originating high quality investments to growth oriented lower middle-market companies.

During the fiscal year, we closed on \$112 million of high-quality new investments, representing 11 new portfolio companies, in addition to several new loans to existing borrowers to help them expand their operations. This new investment activity outpaced repayments on the year, resulting in an 8% increase in our investment portfolio over the prior year. Lower middle market company investments do not generally attract the level of competition prevalent in the broader middle market which enabled us to maintain a relatively high average portfolio yield despite while maintaining our predominately secured investment portfolio. Our conservative underwriting and emphasis on portfolio diversity by industry and investment size also served to mitigate any drag or depreciation associated with under-performing assets. We ended the year with investments in 47 businesses, representing 19 different industries, with an average investment cost of \$8.8 million.

For fiscal 2017 an increase in investment income and lower expenses contributed to a 10% increase in net investment income for the year, which allowed us to maintain and cover 100% of all common shareholder dividends with net investment income. Based on the performance trends outlined above, our common stock outperformed the majority of our BDC peers, generating a total return (including dividends) of 27.9% on the year.

Our specific financial accomplishments for the year ended September 30, 2017 include:

- Paid monthly cash dividends that totaled \$0.84 for the year, bringing the cumulative distributions paid since our inception to \$17.77 per share and the consecutive distributions paid to 176;
- The one year return to stockholders for the year was 27.9% with all dividends reinvested;
- Invested an additional \$99.2 million in new portfolio companies and \$12.9 million in existing portfolio companies;
- Maintained our conservative investment strategy, as all of our new debt investments are secured first or second lien loans in a variety of industries;
- Increased our overall portfolio yield to 11.6% for the year, despite the general asset yield pressures, with little drag from underperforming/non-earning assets, which accounted for only 2% of our portfolio at fair value at the end of the year;

- Issued 2.8 million shares of common stock, resulting in gross proceeds of \$23.7 million, through a combination of an overnight public offering and cost-effective at-the-market share issuances; and
- Redeemed all 2.4 million shares of our 6.75% Series 2021 Term Preferred Stock and issued 2.1 million shares of new 6.00% Series 2024 Term Preferred Stock for gross proceeds of \$51.8 million, significantly lowering our financing costs in 2018 and beyond;

Subsequent to September 30, 2017, we closed six additional new investments totaling \$36.0 million and successfully exited three investments, at or above par, resulting in net originations of approximately \$22.0 million.

FINANCIAL RESULTS: Our net investment income increased to \$21.4 million for the year ended September 30, 2017, which, combined with lower portfolio depreciation, lifted our net assets from operations by 51% to \$17.2 million for the year, or \$0.67 per share.

Net assets, as reflected in our balance sheet, increased by 9.2% from \$201.2 million, as of September 30, 2016, to \$219.7 million, as of September 30, 2017. Net asset value per share decreased slightly by 2.3%, year over year, to \$8.40 per share as of September 30, 2017.

INVESTMENT CLIMATE: We believe there are many opportunities in the current marketplace for lending to lower middle market companies that can support attractive risk-adjusted returns. In particular, we believe the general health of the U.S. economy, as well as specific factors reducing lending by banks, have benefited our company. We have focused our investment origination efforts in support of private equity firms and well capitalized companies with experienced management. We will continue to emphasize our investment adviser's long standing dedication, extensive experience and reputation in serving companies in the lower middle market. We have the ability to offer flexible, customized financing solutions to support the growth and equity appreciation of smaller businesses. The risk profile of companies in the lower middle market is different than that of the broader syndicated debt capital markets and we expect our adviser's focus and experience in managing these risks through various economic cycles will prove a key differentiator over time.

OBJECTIVES AND OUTLOOK: Our objective going into fiscal 2018 is to maintain our strong credit discipline while continuing to grow the portfolio to increase interest income and support our shareholder distributions. Our team is dedicated to reinforcing our position as one of the well-recognized debt providers to lower middle market, privately-held companies in the U.S. which has demonstrated the ability to withstand various economic cycles and produce consistent returns for our shareholders. We believe our portfolio and capital base are well positioned to withstand capital market volatility and potentially benefit from the modest increase in interest rates expected in fiscal 2018. We believe our fund, Gladstone Capital, is an attractive investment for shareholders seeking an attractive yield from consistent monthly distributions supported by a well secured loan portfolio.

Our 2018 Annual Meeting of Stockholders will be held on Thursday, February 8, 2018, at 11:00 a.m. EST. The 2018 Annual Meeting of Stockholders will be a completely "virtual

meeting.” You will receive information on how to participate, if you so choose, along with your proxy materials, in the mail.

Please visit our website at www.GladstoneCapital.com for further information. While you are on the website, please sign up for our email notices to keep up to date on all of our affiliated companies’ activities.

Thank you for your continued support.

David Gladstone
Chairman of the Board and Chief Executive Officer

Terry L. Brubaker
Vice Chairman of the Board and Chief Operating Officer

Robert L. Marcotte
President