Intrepid Capital Funds

*the constant pursuit of value*

# INTREPID INCOME FUND 4th QUARTER 2010 COMMENTARY

## PERFORMANCE

**Average Annualized Total Returns as of December 31, 2010**

| | Inception Date | 3 Month | YTD | 1 Year | 3 Year | Since Inception |
|---|---|---|---|---|---|---|
| Intrepid Income Fund - Inv. | 07/02/07 | 1.22% | 6.16% | 6.16% | 5.35% | 4.83% |
| Intrepid Income Fund - Inst. | 08/16/10 | 1.19% | - | -- | | 2.79% |
| B of A Merrill Lynch High Yield Master II Index | | 3.07% | 15.19% | 15.19% | 10.13% | 8.38%^ |

^Since Inception returns are as of the fund's Investor Class inception date, the Inst. Class cumulative return for the B of A Merrill High Yield Master Index is 6.28%.

***Performance data quoted represents past performance and does not guarantee future results.*** *Investment returns and principal value will fluctuate, and when sold, may be worth more or less than their original cost. Performance current to the most recent month-end may be lower or higher than the performance quoted and can be obtained by calling 866-996-FUND. The Fund imposes a 2% redemption fee on shares held less than 30 days. Performance data does not reflect the redemption fee. If it had, returns would be reduced.*
Per the Prospectus, the Fund's annual operating expense (gross) for the Investor Shares is 1.48% and 1.23% for the Institutional Share Class.

Dear Fellow Shareholders,

The fourth quarter of 2010 was marked by a dramatic shift in risk-free rates. Yields on U.S. Treasury securities had been on a steady downward path for most of the year, but reversed direction in early November. The interest rate offered by five-year Treasury bonds bounced from a low of 1.03% up to 2.01% by the end of the year. Ten-year and thirty-year rates responded in similar fashion, and returns on these securities suffered over the three-month period. Prices of investment grade bonds, as measured by the Bank of America Merrill Lynch Corporate Master Index, retreated as low yield levels were forced higher. It was this type of scenario for which we have positioned the Intrepid Income Fund over the last several quarters, deliberately avoiding exposure to fixed income securities with substantial duration risk. While this strategy led to our outperformance of U.S. Government and investment grade corporate indexes, the high-yield market continued to plod higher as spreads compressed.

During the three months ended December 31, 2010, the Intrepid Income Fund returned 1.22%, net-of-fees, while the Bank of America Merrill Lynch High Yield Master II index returned 3.07%. For the year, the Fund gained 6.16%, while the index gained 15.19%. As we have alluded to in previous letters, the Intrepid Income Fund will usually underperform during periods of strong market performance. In the fourth quarter, the Bank of America Merrill Lynch High Yield Master II index fluctuated to a greater degree than the fund, gaining nearly 3.43% by early November before retreating 2.08% by the end of the month. The Intrepid Income Fund's maximum drawdown during the quarter was 0.61%. The Fund's underperformance and lower volatility were a function of cash equivalent levels exceeding 25% of the fund's assets, combined with our bias toward high-quality, short-duration high-yield securities. To reiterate our thoughts on cash allocation, we will never make a broad market call on whether or not to be invested in the asset class: our cash balance is a function of the opportunities available in the marketplace. If we cannot find securities with attractive risk/return characteristics, we will hold cash.

The Intrepid Income Fund established new positions in four bond issues in the quarter: Amscan Holdings 8.75% due May 1, 2014, Carrols Corporation 9.00% due January 15, 2013, Da-Lite Screen Co 12.50% due April 1, 2015, and Smith & Wesson Holdings 4.00% convertible bonds due December 15, 2026. Note that the Smith & Wesson notes are not as long in duration as they appear because the bonds are putable (we can require the company to repurchase them) in 2011. We exited our position in Chemed 1.875% convertible bonds due in 2014 as the price increased to a point where we believed the bond no longer offered an attractive yield. Several of our holdings were called by their issuers in the fourth quarter, including Church & Dwight 6.00% due in 2012, Interline Brands 8.125% due in 2014, Mobile Mini 9.75% due in 2014, and Silgan Holdings 6.75% due in 2013.

Amscan Holdings operates as a vertically integrated supplier of party goods, metallic balloons, gifts and stationary, as well as Halloween costumes and supplies. Amscan was founded in 1947 and is the largest designer, manufacturer and distributor of decorated party goods and party accessories. The company has a long history of successfully servicing its debt, and its acquisition spree seems to have come to an end. At the time of our purchase, the notes yielded over 750 basis points more than the comparable U.S. Treasury security.

## INTREPID INCOME FUND 4th QUARTER 2010 COMMENTARY (continued)

Carrols Corporation is the largest franchisee of Burger King restaurants in the U.S. In addition to the 309 Burger King stores, the company also owns and operates two of its own concepts, Pollo Tropical and Taco Cabana. These stores are located primarily in Florida and Texas, respectively. Carrols is levered approximately 3.6x, and the notes offer an 8.65% yield-to-maturity in early 2013.

The Da-Lite Corporation should be familiar to many of our longer-term shareholders. We owned the company's 2010 bond issue, but these notes were refinanced when Da-Lite issued new 12.5% notes maturing in 2015. Da-Lite manufactures projection screens, and has faced competition from Asian producers and flat-screen televisions. We believe these concerns are overblown. Additionally, the total size of the issue is very small, which means it may be overlooked by larger funds. The notes offer the highest yield-to-maturity of any bond in the portfolio at 9.66%.

Smith & Wesson is a manufacturer of revolvers, semi-automatic pistols, tactical rifles, hunting rifles, and perimeter security products. The company has a conservatively levered capital structure, with a debt-to-EBITDA ratio of 1.7 times, but some uncertainty exists surrounding a Department of Justice investigation. We believe even a worst case outcome to the investigation would not impair the notes. The 4.00% convertible notes mature in 2026, but as noted above, we have the ability to require the company to repurchase the bonds in December 2011. We believe this feature makes the issue attractive and is in line with our strategy to earn an attractive spread in short-duration fixed income securities. The bonds offer a 434 basis point spread to the 2011 put date.

**Top Ten Equity Holdings** (% of net assets)

| | |
|---|---|
| PEP Boys Manny Moe & Jack | 4.01% |
| AEP Industries, Inc. | 3.94% |
| Perry Ellis International, Inc. | 3.90% |
| Speedway Motorsports, Inc | 3.90% |
| Hanesbrands, Inc. | 3.88% |
| American Greetings Corp. | 3.87% |
| Amscan Holdings, Inc | 3.85% |
| Scholastic Corp. | 3.79% |
| Collective Brands, Inc. | 3.78% |
| Bio-Rad Laboratories, Inc. | 3.74% |

Top ten holdings are as of December 31, 2010. Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

At Intrepid, we are willing to accept the uncomfortable position of running against the herd when we believe the returns available are not compensatory with the risks involved. We believe the recent returns experienced in the high-yield market are more a function of asset inflows, with investors seeking higher yielding fixed-income securities, rather than the belief that the credit quality of these business has improved materially. While the spreads offered in the high-yield market may not look overly egregious, investors should ask themselves whether underlying risk-free rates are at normalized levels. We believe risk-free rates are abnormally low, and as such we have focused more intently on the absolute yields we are receiving on our securities. Opportunities have become more difficult to uncover, but we still have had success in finding attractive high-yield investments. We will remain diligent in investing your capital, and will focus on keeping the fund's risk low even if it is not the easy thing to do.

Sincerely,

Ben O Franklin IV

Ben Franklin
Research Analyst

Jason Lazarus
Research Analyst

**Mutual fund investing involves risk. Principal loss is possible. Investments in debt securities typically decrease in value when interest rates rise. The risk is generally greater for longer term debt securities. Investments by the Fund in lower-rated and non-rated securities presents a greater risk of loss to principal and interest than higher rated securities. The fund is non-diversified, meaning it may concentrate its assets in fewer individual holdings than a diversified fund. Therefore, the fund is more exposed to individual securities volatility than a diversified fund.**

The Bank of America Merrill Lynch U.S. Corporate Index tracks the performance of U.S. dollar denominated investment grade corporate debt publicly issued in the U.S. domestic market. The Bank of America Merrill Lynch High Yield Master II Index is Merrill Lynch's broadest high yield index, and as such is comparable with the broad indices published by other investment banks. You cannot invest directly in an index.

Opinions expressed are subject to change, are not guaranteed and should not be considered investment advice or recommendations to buy or sell any security.

Basis point is a unit that is equal to 1/100th of 1% and is used to denote the change in a financial instrument.
Debt-to-EBITDA is the ratio of total debt to earnings before interest, taxes, depreciation and amortization.

The Intrepid Capital Funds are distributed by Quasar Distributors, LLC