Intrepid Capital Funds
*the constant pursuit of value*

# INTREPID DISCIPLINED VALUE FUND

1ST QUARTER 2016 COMMENTARY

1Q 2016

MARCH 31, 2016

## PERFORMANCE

| | | Total Return | | | Average Annualized Total Returns as of March 31, 2016 | | |
|---|---|---|---|---|---|---|---|
| | Inception Date | Qtr. | YTD | 1 Year | 3 Year | 5 Year | Since Inception |
| Intrepid Disciplined Value Fund - Inv. | 10/31/07 | 4.04% | 4.04% | -1.31% | 5.65% | 6.15% | 5.44% |
| S&P 500 Index | | 1.35% | 1.35% | 1.78% | 11.82% | 11.58% | 5.73% |
| Russell 3000 Index | | 0.97% | 0.97% | -0.34% | 11.15% | 11.01% | 5.76% |

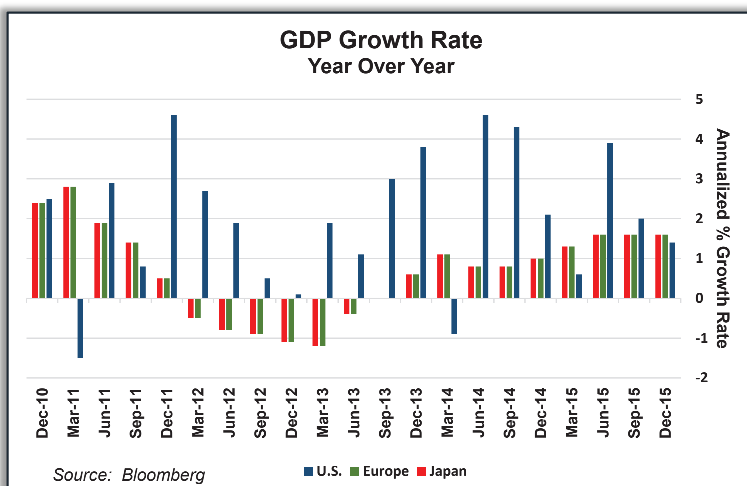
**Performance data quoted represents past performance and does not guarantee future results.** *Investment returns and principal value will fluctuate, and when sold, may be worth more or less than their original cost. Performance current to the most recent month-end may be lower or higher than the performance quoted and can be obtained by calling 866-996-FUND. The Fund imposes a 2% redemption fee on shares held for 30 days or less. 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 1.31%. The Fund's Advisor has contractually agreed to waive a portion of its fees and/or reimburse expenses such that the total operating expense (net) is 1.30% through 1/31/17. Otherwise, performance shown would have been lower.

April 5, 2016

Dear Fellow Shareholders,

When prognosticators and pundits opine on the future prospects of the stock market, they will often look to the state of the U.S. economy. The conventional wisdom is that the simplest way to measure the health of the U.S. economy is by looking at the growth in the U.S. Gross Domestic Product (GDP). GDP is the total output of goods and services in the economy, and is calculated as the sum of consumer spending, investments by businesses (capital spending), the value of government purchases of goods and services, and net exports (exports minus imports). A growing GDP should be good for businesses because it implies that there is more opportunity for growth in profits.



Source: Bloomberg

Over the past five years, the U.S. economy, as measured by GDP, appears to have grown modestly well. As a matter of fact, when compared to European and Japanese GDP, the U.S. appears a more attractive place to invest. The European Central Bank and the Bank of Japan, concerned over the sluggishness of their respective economies, have both ventured into the uncharted waters of negative interest rates.

The low and negative interest rate environment should force more capital to flow into risky assets simply in the hopes of achieving a positive return. For example, why would a European investor, who wants a low-risk or risk-free asset, put money into an investment that is guaranteed a negative return? The current interest rate environment forces that investor to instead put the money into something less appropriate from a risk perspective in the hopes of earning some positive return. Perhaps our hypothetical investor decides to invest in the stock market instead. Now imagine this one hypothetical investor becomes millions of global investors. Under normal circumstances, those investors might have purchased lower-risk

government or high-grade corporate debt. Now, because they do not wish to lock in a zero or negative guaranteed return, they are forced out of their natural investment preference in the hope of earning some positive return. All of this risk-seeking behavior should benefit the stock market as more capital flows into it. Right?

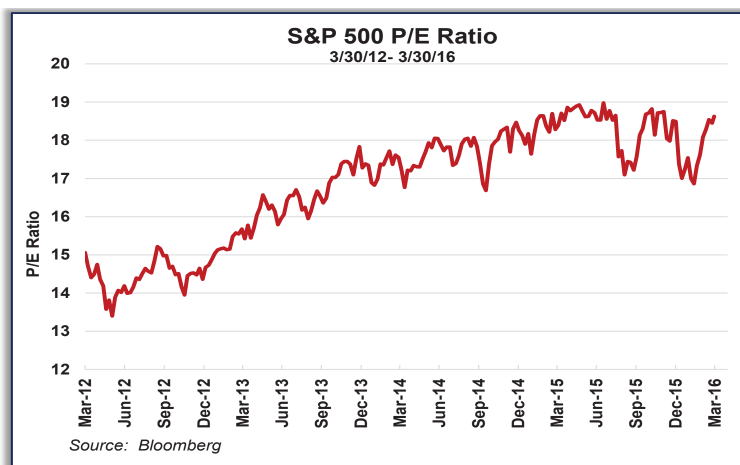
Because we are focusing on the investment in equities, it makes sense to look a little deeper at what supports the underlying businesses and how that impacts stock prices. Earnings are a major factor, and they have been falling over the past two quarters. The fourth quarter alone saw a decrease in total U.S. corporate profits of 11.5% compared to the fourth quarter of 2014. There are a couple of mitigating factors which give some investors comfort. First, BP plc had to pay a $20.8 billion penalty as a settlement for the 2010 Gulf of Mexico oil spill. Excluding that factor, corporate profits were down 7.6% instead of 11.5%.[1] Another point made is that most of the profit weakness came from the energy sector. While that is true, what had previously been a source for investment (and employment) in the U.S. is now gone.

| Top Ten Holdings | (% OF NET ASSETS) |
|---|---|
| Oaktree Capital Group LLC | 3.5% |
| Corus Entertainment, Inc. - Class B | 3.4% |
| Teradata Corp. | 3.3% |
| Verizon Communications, Inc. | 3.3% |
| Mattel, Inc. | 3.1% |
| Northern Trust Corp. | 3.0% |
| SanDisk Corp. | 2.9% |
| Symantec Corp. | 2.7% |
| Coach, Inc. | 2.6% |
| Silver Wheaton Corp. | 2.1% |

Top ten holdings are as of March 31, 2016. Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

We think that dismissing the decline in corporate profits is akin to whistling past the graveyard. Even after making revisions to exclude the worst of the data, it still appears that profits are down 3.9%.[2] For stock prices to continue to move up, investors generally need to feel optimistic that profits will grow in the future. That is not happening right now. According to Factset, analysts lowered earnings estimates for Q1 2016 by 9.6% for S&P 500 companies. That means that analysts felt worse about S&P 500 companies' next earnings release over the course of the past three months. Much of that is based on what company management teams said during their Q4 2015 earnings calls about their future prospects.

Our last point about the state of the equity market is illustrated in the chart to the right, in which we show the Price-to-Earnings ratio for the S&P 500 Index. It had been growing for the past three years. P/E ratios, which take today's price and divide by the trailing twelve month earnings per share, typically increase when investors are optimistic about *future growth* in earnings per share. Only within the past year have we seen the S&P 500 Index P/E falter twice - first in the summer of 2015 and then again during January and February of this year. The only counter to this perceived heightened uncertainty came from the incredibly dovish comments from Federal Reserve




[1]Miller, Rich and Tazi, Alex. "Behind U.S. GDP Data Is Reason for Recession Worry: Weak Profits." *Bloomberg News*. 25 March 2016.

[2]Silva Laughlin, Laura. "Here's Another Sign a Recession is Coming." *Fortune*. 29 March 2016.

Chairwoman Janet Yellen, when she indicated that the Fed would take an extremely slow approach to increasing rates due to global concerns. Based upon recent behavior then, it appears that the two opposing forces at work in equity markets are: 1) increased uncertainty about future corporate earnings along with potential earnings declines, and 2) relief that near-zero interest rates may continue to fuel capital flows into equities. Factor one is a case against stocks while factor two is a case for stocks. While factor two has been playing out for several years, factor one appears to be increasing in strength. As investors, we believe that we are better served by "missing out" on some stock price reflation caused by low rates than we are by fully participating in a stock market reaction to a corporate earnings decline. At times, this decision makes us look a step slow, but we believe it is the responsible thing to do.

For the 1st quarter of 2016, the Intrepid Disciplined Value Fund (the "Fund") returned 4.04% compared to 1.35% for the S&P 500 Index and 0.97% for the Russell 3000 Index. The lowest return for the Fund during the period occurred in late January when it was down -5.80%. Setting aside specific holdings for the moment, the general theme was that we suffered less than the market as it fell through January and February while capturing some of the market's gains through March. Our allocation to precious metals and some out-of-favor consumer discretionary stocks helped the return, while overall, our allocation to financial stocks hindered.

The Fund's top contributors for the quarter were Alamos Gold (ticker: AGI), Mattel (ticker: MAT), and Silver Wheaton (ticker: SLW). Both Alamos and Silver Wheaton participated in an overall strong showing for precious metals, with the dollar spot price of gold rising 16% from $1,061.10 per troy ounce at year end to close the quarter at $1,232.75 per troy ounce. In a similar fashion, the dollar spot price for silver rose 11% from a year-end $13.85 per troy ounce to close the quarter at $15.44 per troy ounce. Late in the quarter, we trimmed back the Alamos position. Mattel made the list on the strength of a Barbie resurgence. As a matter of fact, Barbie posted her first quarter of sales growth in nine quarters. To paraphrase Mark Twain, the reports of Barbie's death have been greatly exaggerated. Other consumer discretionary names that contributed to performance were Corus Entertainment (ticker: CJR/B), which has been cleared to acquire Shaw Media. This acquisition will more than double Corus' size and give the company a huge presence in the Canadian TV market. Coach (ticker: COH) had a similar story to Mattel; its latest earnings release showed that it is making progress in selling its newer line of products. As a matter of fact, Coach is already achieving same-store sales growth at its refurbished locations.

On the other side, the Fund's worst return detractors were American Science & Engineering (ticker: ASEI), Northern Trust (ticker: NTRS), and Unit Corp (ticker: UNT). ASEI had a big 4th quarter revenue miss due to order delays initiated by a handful of foreign customers. The company, which sells sophisticated X-ray detection equipment, could be thought of as an indirect victim of low oil prices, since many of its customers are Middle Eastern governments whose budgets are under pressure and must therefore delay expenditures. We still have conviction that, because of the security environment today, customers cannot indefinitely delay purchasing. Northern Trust has been hit by both an industry and a company-specific problem. Asset managers and custody banks have been hurt in the quarter due to declining market values and by the prospect of future declines. For the entire quarter, the S&P 500's Asset Management & Custody Bank subindustry declined 5.08%. In addition, Northern Trust's Q4 results, reported in January, indicated that management must keep a tighter control on noninterest expenses. Finally, Unit Corp has seen its share price trade down virtually in lock-step with the price of West Texas Intermediate (WTI) crude. The Fund's position is relatively small at less than 50 bps. We view it as a call option on the price of oil.

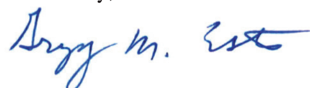
Activity during the quarter was muted. As mentioned above, we trimmed our Alamos position on the strength of gold prices. We also sold out of our Microsoft (ticker: MSFT) position entirely. We felt that, although its cloud business growth has been strong and CEO Satya Nadella has the company on the right track, the stock price has outpaced the actual operational gains. As the stock price moved beyond our intrinsic value estimate, we sold. We also added to

some of the unloved stocks in our portfolio. We mentioned Northern Trust's reasons for declining in the quarter. We take a contrarian view of asset managers, and in the case of Northern Trust, we believe that management can get better control of expenses and that there is value in being a custodial bank that the market is overlooking. Along a similar line, we added to Oaktree Capital (ticker: OAK), which is a premier distressed debt investor. They manage nearly $98 billion and have $21.7 billion in dry powder. For them, heightened uncertainty means more opportunities to put that capital to work, as they have done in the past. OAK also has a 20% stake in DoubleLine Capital, which is headed by renowned investor Jeffrey Gundlach. At the end of 2015, DoubleLine managed $85 billion. This asset is carried at cost on OAK's books, not at its fair market value. The original investment into DoubleLine was $18 million. For 2015, DoubleLine accounted for $52 million in distributable income to Oaktree.

In other news, our SanDisk (ticker: SNDK) holding will be acquired by Western Digital (ticker: WDC) by the end of the second quarter. The original all-cash deal, backed by Chinese investor Tsinghua Unispendour, fell through after concerns arose from the Committee on Foreign Investment in the U.S. The secondary arrangement, in which Western Digital had no equity partner, received shareholder approval. We will be receiving $67.50 in cash and 0.2387 shares of Western Digital for each share of SanDisk. At the current price of WDC, that translates into a total buyout of $78.60 per share of SNDK.

We will close this letter as we always do by noting the average intrinsic value discount. Every stock we own has a corresponding intrinsic value that we calculate and compare to the underlying stock price. Stocks that are trading below our intrinsic value have what we believe is a discount. Stocks trading above our intrinsic values have a premium. The average discount within the Fund was 18%. That's a little bit narrower than at the end of Q4. We are hopeful that increasing market volatility will enable us to find more opportunities in which the underlying value of the investment is mispriced. We thank you for investing alongside us.

Sincerely,



Greg Estes, CFA
Intrepid Disciplined Value Fund Portfolio Manager

**Mutual fund investing involves risk. Principal loss is possible. The Fund is subject to special risks including volatility due to investments in smaller and medium sized companies, which involve additional risks such as limited liquidity and greater volatility. The Fund is considered non-diversified as a result of limiting its holdings to a relatively small number of positions and may be more exposed to individual stock volatility than a diversified fund. The Fund may invest in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods.**

Prior to April 1, 2013, the Fund was named the Intrepid All Cap Fund.

The S&P 500 Index is a broad based unmanaged index of 500 stocks, which is widely recognized as representative of the equity market in general. The Russell 3000 Index is an index representing the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market. You cannot invest directly in an index.

West Texas Intermediate (WTI), is a grade of crude oil used as a benchmark in oil pricing. Basis Point is a unit that is equal to 1/100th of 1% and is used to denote the change in a financial instrument. Call Option is an option to buy assets at an agreed price on or before a particular date.

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