Intrepid Capital Funds
the constant pursuit of value

INTREPID INCOME FUND

2nd QUARTER 2015 COMMENTARY

2Q 2015

JUNE 30, 2015

PERFORMANCE

		Total Return			Average Annualized Total Returns as of June 30, 2015		
	Inception Date	Qtr.	YTD	1 Year	3 Year	5 Year	Since Inception
Intrepid Income Fund - Inst.^	08/16/10	0.87%	2.33%	-1.11%	2.52%	3.88%	4.05%
Barclays US Aggregate Bond Index		-1.68%	-0.10%	1.86%	1.83%	3.35%	4.88%
BAML High Yield Master II Index		-0.05%	2.49%	-0.55%	6.80%	8.41%	7.66%
BAML US Corporate Index		-2.66%	-0.46%	1.01%	3.54%	5.25%	5.92%

^Institutional Class shares of the Intrepid Income Fund commenced operations on August 16, 2010. Performance shown prior to August 16, 2010 (5-Year and Since Inception) reflects the performance of Investor Class shares, which commenced operations on July 2, 2007, and includes expenses that are not applicable to and are higher than those of Institutional Class shares.

Effective January 31, 2014, the Investor Class shares of the Fund were closed, and any outstanding Investor Class shares were converted into Institutional Class shares.

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 expenses (gross) for the Institutional Share Class is 0.95%. 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 0.90% through 1/31/16. Otherwise, performance shown would have been lower.

July 1, 2015

Dear Fellow Shareholders,

All eyes are on Greece in these first few days of July as a potential exit from the European Union ("Grexit") has become a real possibility. The country had been negotiating with bailout providers for the last several weeks, but talks fell through last week, and Greece went on to miss its loan repayment to the International Monetary Fund on June 30. Greek banks and the stock market have been closed all week, and Greeks are only allowed to withdraw €60 ($66 USD) per day from ATMs. Photos have circulated on social media showing empty grocery store shelves and long lines of cars waiting for fuel. Still, many still believe everything will be fine. They declare that even a Grexit would not be meaningful to the European Union given the nation's tiny contribution to the Eurozone's GDP. This might be true, but what is readily apparent in the global market reaction to the stalemate is that Greece *does* matter.

Puerto Rico is experiencing a similar crisis due to the immense amount of debt the Commonwealth is carrying. According to the *Wall Street Journal*, the Commonwealth's debt-to-GDP ratio is 66%, several times greater than the most indebted U.S. state, Massachusetts, at 18%. Puerto Rico's governor has publicly declared that its debt is unsustainable, and he is pursuing relief from creditors. Prices of Puerto Rico's municipal debt have cratered, highlighting the dangers of reaching for yield in a world where central banks have forced savers to invest in ever-riskier securities to meet income needs.

Meanwhile, back at home, the prospect of a Fed rate hike later this year continued to rattle the high-grade bond market. Ten-year Treasury yields steadily declined throughout 2014 and plunged early in 2015 to 1.6%, then violently shot higher in February and March before settling at 1.9% at the end of the first quarter. Yields have moved steadily higher since and are currently around 2.4%. The specific causes of the unusual level of volatility are not completely understood, but according to a *Bloomberg Business* article, some are citing a change in market structure and the presence of high-frequency traders. This has led to concern among Fed officials and the launch of investigations aimed at determining the causes. The Department of Justice has also launched an investigation into potential manipulation of Treasury markets.

Top Ten Holdings	(% of net assets)
Regis Corp., 12/05/2017, 5.750%	4.7%
Pitney Bowes International Holdings, Inc.	4.7%
Caleres, Inc., 05/15/2019, 7.125%	4.6%
Ruby Tuesday, Inc., 05/15/2020, 7.625%	3.8%
Ezcorp, Inc., 06/15/2019, 2.125%	3.7%
AuRico Gold, Inc., 04/01/2020, 7.750%	3.5%
Northern Oil and Gas, Inc., 06/01/2020, 8.000%	3.5%
PHI, Inc., 03/15/2019, 5.250%	3.0%
First Cash Financial Services, Inc., 04/01/21, 6.750%	2.4%
SpartanNash Co., 12/15/2016, 6.625%	2.2%

Top ten holdings are as of June 30, 2015. Fund holdings and sector allocations are subject to change and are not recommendations to buy or sell any security.

To lend some perspective to how such moves in interest rates have impacted bond prices, consider the 2.25% Treasury bond due 11/15/2024, which is the most recently issued ten-year bond that was outstanding during the first six months of 2015. The bond's duration is around eight years, which means the bond price should change by about 8% for every 1% parallel shift in the yield curve. It's unlikely we would experience a perfectly parallel shift, but we are only seeking to approximate the price change. In January, the 10-year yield fell a little more than 50 basis points, and the bonds rose 4.8%. The yield then rose 60 basis points by March, and the bonds fell 5.2%. In the second quarter, 10-year yields rose 43 basis points to 2.4%, which resulted in a 3.6% drop in the 2.25% Treasury. It has been a bumpy ride for the Treasury bond investor, who, including coupons, lost 2.5% in the second quarter.

Rising risk-free rates had a significant negative impact on investment-grade markets. The Barclays US Aggregate, which represents the broad investment-grade market and comprises Treasury and agency bonds, mortgage-backed securities, and corporate bonds, declined 1.68% in the second quarter ended June 30, 2015. High-grade corporates, as measured by the BAML US Corporate Index, dropped 2.66% in the second quarter due to the index's longer duration of around seven years. High-yield bonds were somewhat immune to the pain of higher interest rates due to the asset class's shorter duration of closer to four years. Rates at the shorter end of the yield curve did not shift upward to nearly the same extent as the long end. High-yield spreads were essentially unchanged, and the BAML High Yield Master II Index (the "Index") declined 0.05% in the quarter. The asset class performed well in April and May, but reversed course in June amidst significant outflows from high-yield mutual funds and ETFs. The weakness was broad across ratings and sectors, but distressed issues experienced significantly more pain that the average bond, particularly those in the mining and energy sectors.

In contrast, the Intrepid Income Fund (the "Fund") posted a positive return of 0.87% in the second quarter. The outperformance was attributable to security selection. Most of our positions beat the benchmark handily, including all but one of our energy names. 85% of our average invested assets outperformed the benchmark in the quarter, and there were only three material detractors. Our larger than normal cash position tempered the results somewhat. Cash averaged 39% of the Fund's assets. The top three contributors to the Fund's performance were PetroQuest Energy 10% due 9/01/2017 (ticker: PQ), our combined position in two Rent-A-Center bonds (6.625% due 11/15/2020 and 4.75% due 5/01/2021, ticker: RCII), and Regis Corp 5.75% due 12/05/2017 (ticker: RGS). While we only discuss these three companies below, several others contributed materially to the Fund's quarterly performance, including the bonds of AuRico Gold, Ruby Tuesday, PHI Inc., Smith & Wesson, and Northern Oil and Gas. All of these issues outperformed the Index by several percentage points.

PetroQuest was one of the first energy bonds we purchased for the portfolio. The 10% notes were one of the Fund's core positions from 2011 to 2014. We became wary of the credit quality after management overpaid for Gulf of Mexico properties in 2013 and financed the transaction with debt. We cut the position in half last summer as the call date neared and the bond price held near its highs. Not surprisingly, the bonds fell along with all high-yield E&Ps late in 2014 as oil prices plummeted, but we maintained the position due to the firm's relatively higher exposure to natural gas. The bonds rebounded significantly as oil prices stabilized, at which point we began to consider at what price we would exit the position completely. The impetus came early in June when PetroQuest announced it would be selling its largest asset. The price was favorable to the company, and it generated gobs of liquidity. The bonds jumped several points on the news, but we have a less favorable view of the transaction. PetroQuest sold a key asset that supported the company's credit quality and will use the funds to drill in a largely unproved play in East Texas. While the well returns are better in this area, we were uncomfortable underwriting such a drilling campaign. The 10% bonds were the Fund's top contributor in the holding period beginning March 31, 2011.

The two Rent-A-Center bonds we own rallied after the first quarter earnings report was better than expected. Management's turn-around plan seems to be taking hold, and the core rent-to-own business is stabilizing. The bonds were yielding much more than the Index despite our opinion that the business has a higher-than-average credit quality. Despite the recent jump in bond prices, we believe the notes offer an attractive return for the risks, and we plan on maintaining the positions.

Our position in the Regis 5.75% bonds was established in late 2013 through a private placement. We and another investor were the only two owners of these bonds until recently. A third party indicated its interest in the notes two months ago and was able to complete a purchase more than two points higher than the level we had the bonds marked. We believe the credit quality of this hair cutting business is strong, and therefore we intend to maintain our position in the short-dated notes.

As for detractors, EZCORP 2.125% due 6/15/2019 (ticker: EZPW), EXXI 8.25% due 2/15/2018 (ticker: EXXI), and Corus Entertainment common stock (ticker: CJR/B CN) were each a material drag on the Fund's performance. EZCORP was the Fund's biggest detractor in the first quarter as well, and we had hoped the bond price was nearing a bottom. Like Kevin Bacon's character in *Animal House*, we should have toughened up and exclaimed "Thank you, sir! May I have another?" The company wasn't done with us yet. In late April, EZ announced it had discovered accounting errors in its Mexican unsecured loan business, Grupo Finmart. The firm delayed its earnings release to investigate, and at the time of this writing has still not released full financials or its 10-Q SEC filing. EZCORP's stock is down at least 20% since the announcement, and the convertible bonds we own have fallen from the mid-80s to around 79. Our analysis indicates the bonds are covered even excluding EZ's U.S. payday operations and the entire Mexican business. The notes are offering a yield materially higher than the Index, with better credit quality (in our opinion), lower duration, and a potentially valuable equity option. We think the bonds are very attractive at these levels, and we added to our positions on the weakness.

EPL Oil & Gas was the only energy-related detractor in the second quarter, negatively impacting the Fund's overall performance by a little more than 0.1%. The bonds turned in an impressive performance early in the quarter, rising to the highest level since December of last year as oil prices stabilized and market participants believed bondholders were in a strong negotiating position to push for a refinancing. Recall that EPL was purchased by Energy XXI (ticker: EXXI) in 2014, but EPL remained a standalone subsidiary that did not guarantee any of EXXI's debt. As discussed in our fourth quarter 2014 commentary, we believed the parent had a strong incentive to refinance these bonds. However, our confidence in the thesis weakened recently as it became more obvious that taking the bonds out was not a priority of management's, so we decided to exit the position.

The portfolio had a fair amount of activity in the second quarter. We reached our target positions in four new ideas and added to two positions. The new purchases include First Cash Financial Services 6.75% due 4/01/2022, Multi-Color Corp 6.125% due 12/01/2022, Tech Data 3.75% due 9/21/2017, and Baldwin & Lyons common stock. We will highlight First Cash since it is the largest of the four positions.

First Cash Financial Services (ticker: FCFS) is one of three large publicly-traded pawn shop operators. We discovered FCFS when completing work on EZCORP and Cash America, the other two pawn operators. First Cash is differentiated in that it has a significant presence in Mexico and is the pawn shop of choice in that country. Further, only a small portion of the firm's earnings are attributable to payday loan operations. This is important because the U.S. government's Consumer Financial Protection Bureau (CFPB) has come down hard on payday loan practices and will heavily regulate the industry, which will dramatically reduce the size of the payday loan market and the profitability of companies offering such loans. First Cash is very conservatively leveraged, in our opinion, with a debt-to-EBITDA ratio of just 1.5 times, and the notes make up nearly all of the firm's debt. Additionally, we believe the bonds are well covered by the asset value of the stores. The three major pawn operators have consistently acquired stores for a minimum of $1 million per store, and in some cases beyond $3 million per store. At $1.5 million per store, the domestic stores alone (which generate less than half of the company's sales) cover the firm's *total* liabilities by 150%. We believe the 400+ basis point spread the bonds offered at the time of purchase was more than adequate compensation for the risks.

Two of the Fund's core positions were called in the quarter, Teleflex 6.875% due 6/01/2019 and Smith & Wesson 5.875% due 6/15/2017. We expected the Teleflex bonds to be called, but the Smith & Wessons were a surprise. We also sold three positions. The sales of the PetroQuest and EPL bonds were discussed above. We also exited our position in Quality Distribution 9.875% due 11/01/2018. The bonds were a long-time holding of the Fund, but unfortunately it was announced that the firm would be acquired by a private equity buyer. No details were given about the prospective capital structure, but the bonds will likely be refinanced as part of the deal. The yield to the expected refi date was very low, so we decided to preemptively exit the position.

At Intrepid, we don't pretend to know what will happen with Greece or Puerto Rico. Maybe one or both of these situations is the catalyst for a global re-valuation of financial assets, but more likely the catalyst will be some future "unknown unknown."

What we do know is that the future is unpredictable. To mitigate the risks of the unknown, we look at securities through the lens of valuation. To bear the risks of a specific security, we must be appropriately compensated. We will not force your capital into securities when we don't believe we are paid to assume the risks. We continue to believe ideas that will potentially provide attractive risk-adjusted returns are scarce, and therefore the Fund's cash balance remains elevated at 45% of the Fund's assets. Additionally, as stated in our letters for the last several years, we believe interest rates are well below normalized levels. At the end of the quarter, the Fund's effective duration was 1.4 years. We will maintain the Fund's short-duration posture until we believe we are being paid to extend further along the yield curve.

Thank you for your investment.

Sincerely,

Jason Lazarus, CFA
Intrepid Income Lead Portfolio Manager

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 present 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 Fund may invest in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods

The Bank of America Merrill Lynch High Yield Master II Index (BAML High Yield Master II Index) is Bank of America Merrill Lynch's broadest high yield index, and as such is comparable with the broad indices published by other investment banks. Bank of America Merrill Lynch US Corporate Index (BAML US Corporate Index) is an unmanaged index of U. S. dollar denominated investment grade corporate debt securities publicly issued in the U.S. domestic market with at least one year remaining term to final maturity. Barclays Capital U.S. Aggregate Bond Index is an index representing about 8,200 fixed income securities. To be included in the index, bonds must be rated investment grade by Moody's and S&P. You cannot invest directly in an index.

Free Cash Flow measures the cash generating capability of a company by subtracting capital expenditures from cash flow from operations. EBITDA is calculated as the company's Earnings, Before Interest, Taxes, Depreciation and Amortization. Debt-to-EBITDA is a measurement of leverage, calculated as a company's interest-bearing liabilities minus cash or cash equivalents, divided by its EBITDA. E&P (Exploration and Production) is a type of company in the oil and gas industry focused on discovering and extracting crude oil and natural gas from underground reserves. A Risk-Free Rate represents the interest an investor would expect from an absolutely risk-free investment over a specified period of time. Duration is an approximate measure of the price sensitivity of a fixed-income investment to a change in interest rates, expressed as a number of years. Basis Point is a unit that is equal to 1/100th of 1% and is used to denote the change in a financial instrument. Investment Grade is a bond with credit rating of BBB or higher by Standard & Poor's or Baa3 or higher by Moody's.

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

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