Intrepid Capital MANAGEMENT INC.

3Q 2017

Index Returns	
7/1/2017 to 9/30/2017	
Dow Jones:	5.58%
S&P 500:	4.48%
NASDAQ:	6.06%
Russell 2000:	5.67%
MSCI EAFE:	5.40%

QUARTERLY COMMENTARY

October 2017

"We are what we repeatedly do. Excellence, then, is not an act, but a habit."
— Aristotle

Dear Friends and Clients,

I recently picked up a copy of Joel Tillinghast's "Big Money Thinks Small." Joel is a longtime portfolio manager with Fidelity. I couldn't help but chuckle when in Chapter 1, "It's a Mad, Mad World," Joel outlines what he regards as the crucial steps to successful investing:

1. Make decisions rationally
2. Invest in what we know
3. Work with honest and trustworthy managers
4. Avoid businesses prone to obsolescence and financial ruin
5. Value stocks properly

The reason for my chuckle is that Mr. Tillinghast, in his five bullet points, outlines almost exactly what we attempt to do at Intrepid Capital, and more specifically for the purposes of this letter, in the Intrepid Balanced Portfolio (the "Portfolio"). These principles might seem like a no-brainer, but you'd be surprised how many professional investors fail to consistently follow them, in my opinion. As I once heard it said of commodity trading, "The rules are very simple. Following the rules, however, is very difficult."

One reason it's so difficult is that the market doesn't consistently recognize or reward investors who try to adhere to such a philosophy. I would love to add "earn consistently high returns" as a sixth bullet inherent to our investment process, but there are periods when behavior that goes directly against the five rules seems like the profitable path – irrational decision making is rewarded, buyers of arcane and complex strategies seem to reap all the profits, honest and dishonest managers are treated alike by the market, unsustainable businesses are propped up by cheap debt, and valuing stocks seems to be a fruitless exercise.

These are the times when following the rules can be very difficult indeed. As the portfolio manager of the Portfolio, I am attempting to deliver equity-like returns with substantially less risk than an equity index. Since inception on 4/30/1995, we have been able to deliver on that value proposition as shown in the chart to the left.

I am always amazed at the short-term mindset of the average mutual fund investor. There is a great mismatch

in this industry between the underlying term of different asset classes and the time horizon of investors in those asset classes. For instance, many yield seekers today are content to treat a high yield bond index, such as the well-known BofA Merrill Lynch US High Yield Index (the "Index"), as a nearly risk-free money market substitute in which they can put cash to work for a few months (or less). This may seem like a low-risk strategy to earn a little extra yield, but the securities that make up the Index are markedly riskier and longer-term in nature. The average bond in the Index is 6.3 years away from maturity, and according to Merrill Lynch the average issuer has a single B credit rating, which is how Standard & Poors classifies a company that currently has the ability to meet its financial obligations but is vulnerable to defaulting if business or economic conditions worsen.[1] That combination of both interest rate risk and credit risk doesn't strike me as the characteristics of a short-term, cash equivalent investment.

Even more egregious than that, I've recently heard other investment managers[2] tell stories of clients asking if they should "park some money" *in the S&P 500* for a few months. For most of the last 100 years, such a blasé mindset toward stock market risk would have been unheard of. But when the S&P has averaged a 14.2% return over the last five years and has gone almost a full year without a 3% drawdown (as of this writing, only 7 days shy of the longest such run in history), and when investors' expectations of the future are naively based on the last few years, it's natural for such myopic behavior to become popular again.

While we are of course mindful of s hort-term performance, we are much more interested in how we look over the trailing 10 years. I can hear many of you now: "That's a nice thought Mark, but we will give you three years!" Yes, that is unfortunately the time horizon over which most performance is evaluated and money is allocated in this business. I like 10 years because it is more likely to encompass a full market cycle of both a bullish phase and a bearish phase. Full market cycles are the time horizon we focus on at Intrepid and the time frame over which we think all investment managers' performance should ideally be measured. Truthfully, it doesn't take excessive skill to passively ride a bull market; a skillful manager should be able to participate in an up market while also protecting and preserving capital in a down market.

In contrasting our Tillinghast-esque philosophy to current market thinking, I have marveled for quite some time at the cult-like status of both Elon Musk and his electric car company Tesla. Wall Street analysts expect Tesla to sell 121,000 cars this year (they sold 76,000 last year). This level of production will generate an expected 2017 pre-tax loss of $1.4 billion (with a "B"), and next year's loss is forecasted at a mere $550 million. The company will likely have to continue tapping the capital markets for funding until it reaches a break-even level of production, which Wall Street believes will happen in 2019.

To clarify, I'm not disparaging Mr. Musk or the company itself, but rather the market's collective decision to value such a cash-burning enterprise at almost $66 billion and to price its recent oversubscribed debt issue ($1.8 billion of 8-year senior notes) at a 5.25% yield, which is *an all-time record low* for a B-rated issuer. To me this seems to violate, at a minimum, rule #1 above. Personally, if I were a creditor of a small, unprofitable electric car manufacturer with large, entrenched, deep-pocketed competitors and an uncertain growth runway, I would demand a much higher return than 5.25% to compensate for the chance that I might not be paid back.

On the flip side, going back to Mr. Tillinghast's Rule #2 (invest in what you know), I present the Regis Corporation 5.5% notes due 12/2/2019. Regis is a company we know well, as we at times have owned both their equity and their debt. Regis is in the business of giving haircuts, and I frequent my local Supercuts, one of Regis' brands.

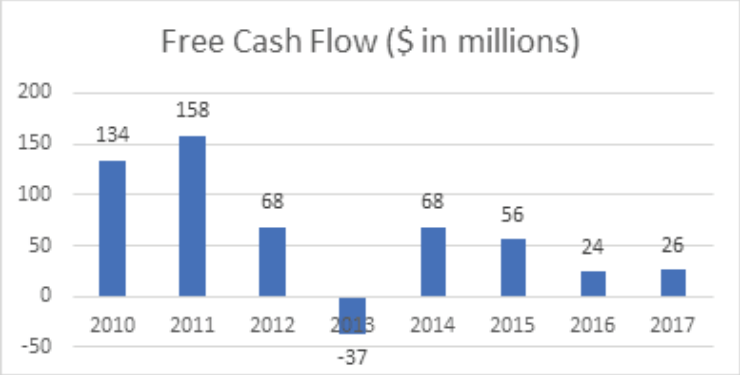
These bonds also satisfy Rule #4 (avoid businesses prone to obsolescence and financial ruin), as obsolescence is highly unlikely to occur for Regis between now and when this bond matures in December 2019. The company's operations are generating positive free cash flow (see below), and the most recent filings disclose $172 million in cash available to

1 "S&P Global Ratings: RatingsDirect." *Standard and Poors.* August 18, 2016. Web. 12 October 2017.

2 Bilello, Charlie. "Is the S&P the New Money Market?" *Pension Partners.* October 2, 2017. Web. 12 October 2017.

cover its $121 million in debt. Despite these favorable credit conditions, the bonds offer a yield of 5.5% to maturity – an attractive premium to that offered by Treasuries considering the risk assumed. Based on my past attempts to shear my own hair and the unlikely event that this business is "Amazoned," I feel more comfortable about the return of my principal in Regis than I would in Tesla.

Regis Corp



Source: Company filings

In summary, be rational, invest in what you know, and be careful with speculative business investment. Our process is built around these principles. I believe that by following this process, we will deliver attractive risk-adjusted results over a full market cycle (>10 years).

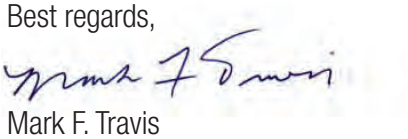
For the third quarter ending September 30, 2017, the Balanced Portfolio returned 1.31%, net-of-fees compared with an increase of 4.48% and 3.49% for the S&P 500 Index and Blended Benchmark (60% S&P 500/40% BAML High Yield Master), respectively. The Portfolio ended the quarter with a mix of 46% in equity, 32% in debt, and 23% in cash or T-bills.

This performance compares unfavorably to the rapidly rising S&P 500 and Russell 2000 equity indexes over the last three months. As they say of the weather in Florida, "Stick around, that will change." The since inception performance is closer to the blended indexes consisting of stock and bonds. In almost every case, we are attempting to take less risk.

As for the quarter ended September 30, 2017, the Portfolio's five largest contributors were Syntel (ticker: SYNT), Teradata (ticker: TDC), Verizon (ticker: VZ), Dominion Diamond (ticker: DDC), and Berkshire Hathaway Class B (ticker: BRK/B). The Portfolio's five largest detractors for the quarter were G.U.D. Holdings (ticker: GUD AU), Baldwin & Lyons (ticker: BWINB), Royal Mail (ticker: RMG LN), Leucadia National (ticker: LUK), and Patterson UTI Energy (ticker: PTEN),.

Thank you for entrusting us with your hard-earned capital, it is not a position we take lightly. If there is anything we can do to serve you better, please don't hesitate to ask.

Best regards,



Mark F. Travis

President/CEO

SMALL CAP PORTFOLIO – COMMENTARY BY JAYME WIGGINS, CFA, CIO, PORTFOLIO MANAGER

I occasionally bring my kids to the office with me on the weekend for a few hours when I need to tie up loose ends and give my wife a break. About a month ago, our four-year-old son, Asher, tagged along while I finished up a report. I noticed him looking at a framed picture of Warren Buffett and me standing in a parking lot across the street from Piccolo Pete's in Omaha. This conversation followed:

Asher (pointing to the Buffett photo): *"Who is that?"*

Me: *"He's an investor like your daddy, except he's famous and successful."*
Asher: *"Does he protect lizards?"*
Me: *"No. Why?"*
Asher: *"Because he looks like one."*

My first thought: Kids say the darnedest things. Then: Wait, does my four-year-old actually know that this guy owns the GEICO Gecko? Looking at the photo made me reminisce about the time as a teenager when I checked out *Buffett: The Making of an American Capitalist,* the biography by Roger Lowenstein, from my local library. Back then, I had an unspoiled image of the Oracle of Omaha that endured for many years. The photo in my office was taken during a business school trip in 2009, which was 14 years after I read the Lowenstein book. Mr. Buffett was incredibly generous with his time in Omaha. He answered questions from over one hundred business students at Berkshire's headquarters, bought everyone lunch, and then patiently took individual pictures with each person, with poses ranging from headlocks to mock marriage proposals. I never expected to see this 79-year-old billionaire, the second richest person in the world, get on one knee while dressed in a suit just so a female business school student could have an unforgettable Facebook profile photo. After everyone had their moment with Buffett, he walked by himself down the street to his metallic beige Cadillac DTS, got in, and promptly peeled out as we all watched in awe.

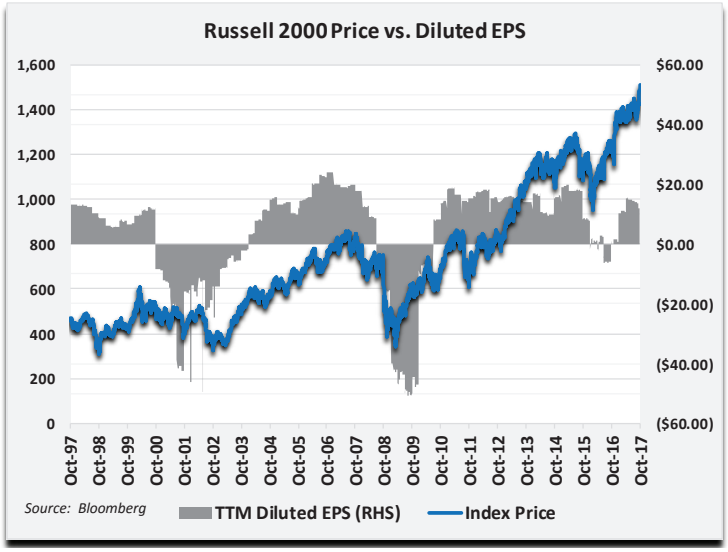
Buffett has made an indelible impact on legions of investors, but even the great ones are prone to hyperbole and bias. On August 30, 2017, Buffett was asked by a Bloomberg interviewer whether Quantitative Easing has worked, since asset prices have increased but wages for the average worker have not. Buffett replied, *"It did wonders for us coming out of 2008. Without it, we'd have gone back to the economics of 100 years ago, you know...I think the Fed has overwhelmingly done the right thing."* I'm in the camp that the inventions of the past century, including the television, the Internet, and cell phones, matter more for our economic well-being than the decisions to bail out Wall Street in 2008. Nevertheless, Buffett was once again giving his endorsement to the unprecedented government intervention we've experienced, nearly seven years after he penned a "thank you letter" to Uncle Sam for bailouts in a New York Times op-ed.[3]

In the 2016 Berkshire Hathaway shareholder letter, Buffett ridiculed as *"nonsense"* the advice of *"naysayers"* with gloomy forecasts for American stocks.[4] He said a few months ago that *"stocks are dirt cheap"* if interest rates increase only modestly over the next decade.[5] His latest prediction made a couple of weeks ago was for the Dow to hit 1,000,000…over the next 100 years.[6] Buffett is a bull on America and sanctimoniously dismisses those with a negative view of U.S. stock prices. He also has $100 billion of cash and equivalents parked at Berkshire Hathaway that is seemingly missing out on the "dirt cheap" stock opportunities he's referenced.

In our opinion, we have one thing going for us that Buffett doesn't have, and it's not brains or money. We can give it to you straight. For some, when you get to be rich and famous, your overriding concern is crafting your legacy. Buffett seems to badly want to be remembered as the folksy billionaire who cared about the little guy, the do-gooder in an industry of villains, and the patriotic buy-and-holder of blue chip American businesses. In this industry, it's easier to be an optimist. The pessimists only thrive when most everyone else is suffering, and that's a lonely celebration. Nevertheless, it's our pledge to you, our shareholders, to keep ourselves grounded in reality, not fantasy, as we execute our investment process.

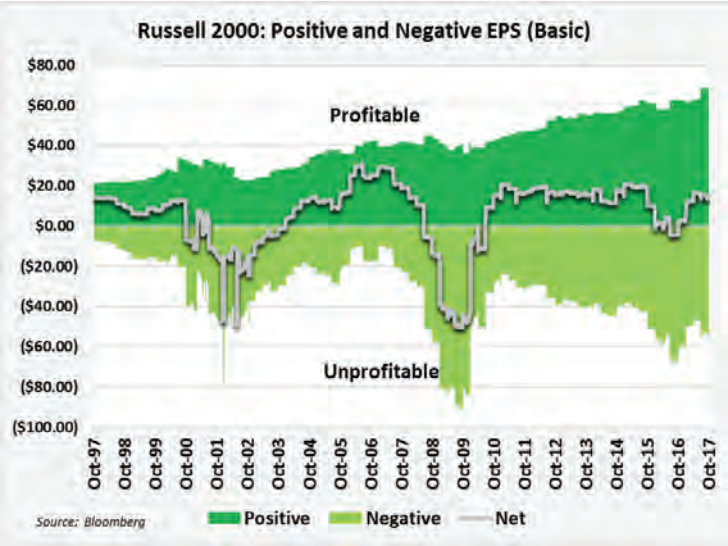
3 Buffett, Warren E. "Pretty Good for Government Work." *Nytimes.com.* 16 Nov 2010. Web. Accessed 2 Oct 2017..
4 Buffett, Warren E. "Berkshire Hathaway, Inc." *Berkshirehathaway.com/letters/2016ltr.pdf.* 25 Feb 2017. Web. Accessed 2 Oct 2017.
5 Bary, Andrew. "Buffett: Bonds 'Terrible' In Comparison to Stocks." *Barrons.com.* 8 May 2017. Web. Accessed 2 Oct 2017.
6 Gara, Antoine. "Dow 1,000,000? That's Warren Buffett's Latest Call." *Forbes.com.* 20 Sept 2017. Web. Accessed 2 Oct 2017.

The P/E of the Russell 2000 Index is currently 126x. This is derived by taking today's (10/2/17) closing price (1,509.47) and dividing by the actual GAAP diluted earnings per share of the index ($11.97). The index is 76% above the pre-credit crisis high, which occurred on Friday, July 13, 2007. The Russell has increased 340% from the credit crisis low on March 9, 2009. What an amazing run. The aggregate earnings for the Index's components have not experienced the same appreciation. Diluted EPS for the Russell's membership is down 38% from July 13, 2007.



It's very much a Jekyll and Hyde story, with those companies delivering positive earnings (68% of total) continuing to grow their bottom lines, while the unprofitable firms (32%) produce greater losses. We suppose this is one of the main bull arguments today: small cap averages are unfairly distorted by money-losing companies, and profitable businesses are reasonably valued. After all, the profitable businesses themselves sell for 22x earnings, a fraction of the overall Index multiple. This is not dramatically above the 20-year average P/E of around 18x for positive earnings companies. Why not just focus on this group? There must be value in there, right?

Not much. Excluding financial firms, the group of profitable companies collectively trades for an Enterprise Value to Operating Profit (EV/EBIT) multiple of 19x. The Enterprise Value metric adjusts for the impact of borrowing, which depresses P/E ratios in a low-interest rate environment. A 19x EV/EBIT multiple is very rich and probably only warranted for fast-growing, high-return businesses. **Profitable small cap firms grew their revenue by 5.7% over the past year, and that's including the benefit from acquisitions. We estimate that organic revenue growth was 3.3%.**[7] That's not exactly setting the world on fire and is even less than nominal GDP growth over the same span (+3.8%). The profitable firms had an aggregate effective tax rate of 21%, although the median company's rate was close to 31%. The aggregate return on capital for this subset of companies was 8.5%. The aggregate return on tangible capital was 13.5%, excluding Goodwill and Other Intangible Assets. This probably overstates the return, since some intangibles, like software investments, are required for organic growth and do not result from acquisitions. Nevertheless, a 13.5% return on tangible capital suggests that the profitable Russell 2000 businesses are creating some value as they grow, with returns on capital that exceed their cost of capital.



7 We estimated acquired revenues by taking cash paid for acquisitions from the cash flow statement and assuming acquirers paid the same EV/Sales multiple as their own current multiple.

I apologize in advance for the formulas. Valuation is very important to us at Intrepid, so the math is germane to our day-to-day investment process. Using the data cited above, we can solve for the discount rate (required return) implied by a 19x EBIT multiple. It's 6.4%. That's basically equal to the yield on 10 year Treasuries at the turn of this century. If we used the median tax rate of 31%, which would remove the effect of outliers that dragged down the effective rate, the implied required return falls to 6%. How many investment managers would admit to using a 6% discount rate to value their holdings? If we applied what we consider to be a more reasonable discount rate of 10%, the fair EV/EBIT of the profitable non-financial companies would be ~9x, or less than half of the market's (19x) multiple. Investors today are paying 37x free cash flow for the profitable, slow-growing members of the Russell 2000 that do not belong to the financial sector. In our opinion, this is far from a bargain and radically diminishes arguments that small cap benchmarks only *look* expensive due to unprofitable businesses. They *are* expensive.

Justified EBIT Multiple =	(1 – Tax Rate) / (1 – Growth Rate / ROIC) / (Required Return – Growth Rate)

EV/EBIT of 19x =	(1 – 0.21) / (1 – 0.033 / 0.135) / (Required Return – 0.033)
Required Return =	**0.064**

EV/EBIT of 9x =	(1 – 0.21) / (1 – 0.033 / 0.135) / (**0.10** – 0.033)

Intrepid Capital's Views on Returns on Capital

The return on capital measures the ability of a company to create value relative to the amount of capital employed in the business. Intrepid Capital defines Invested Capital as Shareholder's Equity + Debt – Cash. Some analysts treat a portion of Cash as operating in nature, and they leave this amount as part of the Invested Capital figure. Investment management firms have different schools of thought on whether it is more appropriate to emphasize the standard return on invested capital (ROIC), which is calculated as Net Operating Profit After Taxes (NOPAT) divided by Invested Capital, or the return on tangible capital (ROTC). Tangible Capital is simply Invested Capital minus Intangibles, including Goodwill and Other Intangible Assets. Those favoring the standard ROIC often argue that it incorporates the impact from acquisitions, whereas the return on tangible capital does not. In our view, acquisition accounting can distort the normal ROIC metric enough to severely reduce its utility.

For example, consider a hypothetical public company with NOPAT of $10 million and Invested Capital of $50 million. The ROIC of this firm is 20%. Assume investors value this business at 15x NOPAT, or $150 million. Imagine this company finds another business exactly like it, except half of its size. In other words, the target has $5 million of NOPAT and $25 million of Invested Capital. Due to the target's private status, it can be acquired for 10x NOPAT, or $50 million. After the public company acquires the private firm, its Invested Capital will increase from $50 million to $100 million, representing the value of the transaction. Half of this value will be assigned to Goodwill. The resulting ROIC of the combined business will be 15%. Therefore, the ROIC has declined due to acquisition accounting, even though the public company made a value-enhancing transaction by acquiring a private firm for $50 million that the public markets value at $75 million. Returns on tangible capital, however, excluding the acquisition Goodwill, remain at 20%.

Public Company

NOPAT	$10 million
Invested Capital	$50 million
ROIC	*20% ($10M / $50M)*
Multiple	15x NOPAT
Firm Value	$150 million ($10M * 15x)

Private Company

NOPAT	$5 million
Invested Capital	$25 million
ROIC	*20% ($5M / $25M)*
Acq. Multiple	10x NOPAT
Acq. Price	$50 million ($5M * 10x)

Combined Company

NOPAT	$15 million ($10M + $5M)
Invested Capital	$100 million ($50M + $50M)
ROIC	*15% ($15M / $100M)*
Multiple	15x NOPAT
Firm Value	$225 million ($15M * 15x)

Combined Company: Return on Tangible Capital

NOPAT	$15 million ($10M + $5M)
Tangible Inv Cap	$75 million ($50M + $25M)
ROTC	*20% ($15M / $75M)*

At Intrepid, we believe returns on tangible capital are a better measure of the incremental value-creating potential of a business. With that said, we individually scrutinize the performance of past acquisitions and the prices paid, when data is available, to make judgments about how effective management teams are at deploying capital. Additionally, when determining ROTC, we will include intangible assets that aren't related to acquisition activity.

For the three months ending September 30, 2017, the Intrepid Small Cap Portfolio (the "Portfolio") rose 0.79%, net-of-fees, while the Russell 2000 Index increased 5.67%. Cash and Treasury bills accounted for 79.4% of the Portfolio's assets at quarter end. The Morningstar Small Cap Total Return Index jumped by 4.67% during the quarter and the S&P Small Cap 600 was up 5.96%. We are now disclosing additional benchmarks because Russell representatives want to charge us to use their benchmark. We may transition to a different small cap benchmark over the coming year.

The Portfolio acquired one new holding during the third quarter. Greenhill & Co. (ticker: GHL) is an independent investment bank that provides advice on mergers and acquisitions, raising capital, and restructurings. The stock recently fell to all-time lows due to the company's failure to participate in the latest Mergers & Acquisitions (M&A) boom. Greenhill's 2017 operating results are forecasted to be the worst ever recorded for the firm. Absent a sharp pullback in overall M&A activity, we believe 2017 will mark a trough in the company's performance and Greenhill's stock will rebound when 2018 results return to more normalized

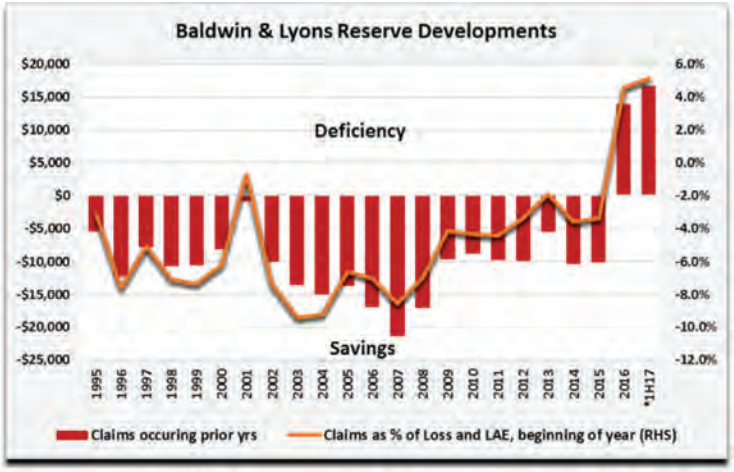
levels. We believed the shares were trading for approximately 10x adjusted free cash flow, assuming a cash impact from stock compensation, when we began establishing our stake. On September 25th, Greenhill announced a leveraged recapitalization (taking on debt to buy back its own shares) that sent the shares up by 16% before we could finish building our position. The stock is still trading below our estimated fair value, but we are not thrilled with the company's new leveraged balance sheet. With that said, investment banking is a cash-generative business, and we think Greenhill could pay off its debt in less than five years. Since our position size is small, we plan to hold the name and wait for an expected recovery in Greenhill's revenue.

We sold our Dominion Diamond (ticker: DDC) position in July. On July 17th, Dominion announced it would be acquired by The Washington Companies for U.S. $14.25 per share. The board had been conducting a strategic review since Washington first expressed interest earlier in the year. The takeover price represented a substantial premium to our $8.52 average cost basis in the shares, although we had partially reduced the position in March and April when the price was lower and a takeover was less certain. Our average selling price for Dominion was $13.39 per share.

For the third quarter, the largest contributors to the Portfolio's performance were Syntel (ticker: SYNT), Dominion Diamond, and Greenhill. The only position negatively impacting the Portfolio's return by more than 10 basis points was Baldwin & Lyons (ticker: BWINB). Since the Portfolio only has a handful of significant holdings, we thought it made sense to provide a general update on our investment rationale for each as opposed to trying to account for modest price movements that are more related to market direction than security-specific factors. The Portfolio's top six holdings are Corus Entertainment (ticker: CJR/B), Baldwin & Lyons, Syntel, Amdocs (ticker: DOX), iShares Gold Trust (ticker: IAU), and Primero Mining's 5.75% Convertible Notes (CUSIP: 74164WAB2).

Before this year, Corus Entertainment's earnings had been adversely impacted by declines in advertising revenue on the company's television networks. As a result of the company's increased bargaining power due to being the largest operator of cable networks in Canada, management has now stabilized advertising. Going forward, Corus's performance is likely to reflect overall television advertising trends, which are currently soft. Canada's advertising market has migrated toward digital even faster than in the U.S, as Google and Facebook consume a growing portion of the global advertising pie. Although we expect digital players to account for the vast majority of advertising growth in the medium-term, trees don't grow to the sky, and there have been many questions about the effectiveness of digital advertising compared to other mediums.

In order for Corus to better compete with streaming services like Netflix and protect and grow its advertising revenue, we believe the company must further enhance the on-demand television viewing experience. Traditional television networks must become more like Netflix by offering full seasons on-demand and reducing ad loads. Advertising is a material revenue contributor and subsidizes the price of TV for users. The best way to reduce ads while preserving the revenue stream is through more targeted advertising that is enabled by the latest cable technology. Advertisers will pay a higher price per viewer if they know their ads are reaching their target audience. We expect low-single digit revenue growth, at best, for Corus in the near-term. The stock is trading for about 9x free cash flow, which is a multiple that fully reflects the business's tepid growth outlook. As the company deleverages, we believe value will accrete to the stockholders.

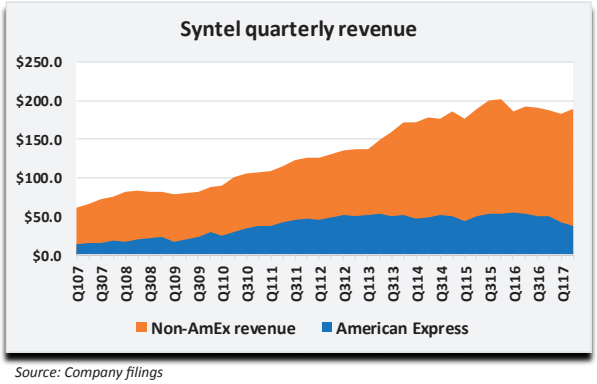


Source: Company filings
*1H17 = 1st half of 2017

Baldwin & Lyons, the property and casualty insurer, is trading at a multiyear low Price to Book multiple near 0.8x. This is less than half the median multiple of other small cap P&C insurance firms. Baldwin specializes in commercial trucking policies, like FedEx contractors. According to Fitch, the commercial auto industry is experiencing its worst underwriting performance since 2001 as a result of accidents caused by texting and unexpectedly high jury awards. These factors have

recently led to unfavorable reserve developments at Baldwin, which previously had an unblemished history of conservative reserving. In response, the company and other insurers are increasing premiums and promoting technology to monitor and control smartphone usage in an attempt to reduce accident rates. Competitors like AIG and Zurich have pulled back from certain markets. We believe Baldwin will restore its profitability, which will lead to a recovery in the stock price. Insiders have been buying shares.

We believe the prescription to fix Syntel is simple: the company needs to grow revenue. Syntel has been disproportionately affected by a reduction in IT spending by American Express, its largest customer. However, the business has also been starved of new relationships due to an overly lean business development budget. Syntel is addressing these issues through increased marketing spending and a greater involvement from executives in closing deals. The company showed modest progress on this front in the second quarter, as revenue excluding American Express increased 3% sequentially. It's too early to call a recovery. Nonetheless, immigration-related rhetoric has noticeably decreased, possibly indicating less of a headwind to Indian IT outsourcers from regulatory changes. Furthermore, the Indian rupee has weakened against the dollar over the past month, which relieves some pressure on the cost side for outsourcers. The stock is selling for approximately 11.5x expected free cash flow.



Source: Company filings

Amdocs is probably the best business the Portfolio owns. It's also fully valued. Amdocs' customer relationships are sticky and its revenue is largely recurring. It is the premier company for handling customer care and billing software and system transformations for leading telecommunication and cable firms. The company's market capitalization excluding nearly $1 billion in cash is equal to 15x Amdocs' average free cash flow over the past three years.

The Portfolio has a modest position in the iShares Gold Trust. We believe that the Fed will halt its current path of tightening at the first sign of any market trouble. Central banks around the world remain extremely accommodative, and geopolitical risk seems more palpable than it has been in years. Such conditions are historically favorable for gold. President Trump will soon nominate the next Chair of the Federal Reserve. He has spoken to both John Allison, the former CEO of BB&T and staunch Fed opponent, and Kevin Warsh, a previous governor of the Federal Reserve and later a critic of the Fed's loose money policies. We would cheer the selection of Allison, and Warsh would probably be an acceptable pick as well. Nevertheless, given the President's proclivity to celebrate new stock market highs on Twitter, we expect a more conventional choice like Janet Yellen, Jerome Powell, or Gary Cohn. But hey, who knows—Trump likes to surprise.

We see an impressive bubble forming in cryptocurrencies. No, we don't know the value of Bitcoin. Yes, we like the idea of a currency that isn't controlled by a government. Just don't lose your private key, or you can kiss your funds goodbye forever. While one of the original premises for Bitcoin was that only a finite amount could be mined, the explosion of Initial Coin Offerings is saturating the market with speculative cryptocurrencies. We wonder how many people would praise Bitcoin, Ethereum, Ripple, Bitcoin Cash, Litecoin, Dash, Ethereum Classic, etc. for their "scarcity" and would happily commit funds to these interesting blockchain technologies at today's skyrocketing prices, yet would scoff at the idea of owning gold. Gold is harder to transact than Bitcoin, but it has been a store of value for centuries, can't be hacked (but it can be stolen)[8], and they aren't creating any new versions of it.

Speaking of gold, let's discuss the Portfolio's stake in the convertible bonds of Primero Mining. Primero owns the San Dimas gold and silver mine in Mexico. San Dimas has a silver stream attached to it, for which the vast majority of silver is sold to Wheaton Precious Metals at $4.30 per ounce. Primero's liquidity is evaporating and it has told investors that it needs the stream to be relaxed in order for the mine to continue operating. With a reduced stream, the cost structure of the mine can

8 The hacking of cryptocurrencies has so far been largely tied to the exchanges where they trade as opposed to the underlying blockchain technology.

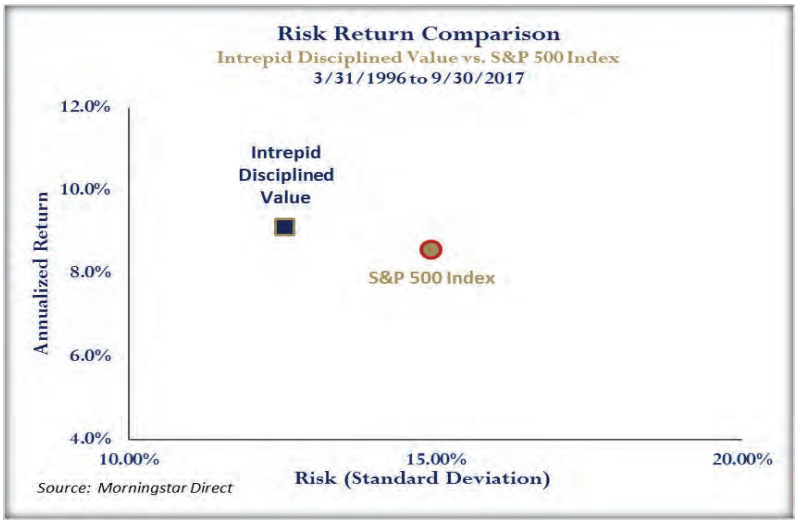
be vastly improved. The company has received multiple takeover bids that are contingent on a restructuring of the stream. The management of Wheaton Precious Metals has stated it is willing to modify the San Dimas stream if it is appropriately compensated. It is unclear exactly what form of compensation they would require. Our bonds are currently marked in the low 60s. We believe it is in Wheaton's best interest to work with Primero to modify the stream now. We anticipate an announcement on this front sometime during the next couple of months.

"Price is what you pay. Value is what you get."
"Be fearful when others are greedy and be greedy when others are fearful."
"Rule No. 1: Never lose money. Rule No. 2: Never forget Rule No. 1."

These widely known quotes represent the classic wisdom of Warren Buffett. The Russell 2000 Index is up 11% in just the past six weeks—a jaw-dropping rally first inspired by a "no man left behind" mentality as small caps had relatively underperformed year-to-date, but which accelerated on renewed hopes of corporate tax reform. Over this stretch, the Russell only declined more than 24 bps on one day. This is during a period when three major destructive hurricanes hit the U.S. or its territories, North Korea successfully tested long-range missiles and threatened the U.S. with nuclear annihilation, the national debt officially topped $20 trillion, and Russell 2000 earnings expectations for 2017 descended to a year-to-date low. While some of these developments are more impactful to the economy than others, the near total absence of downside volatility in the stock market suggests a lack of fear and surfeit of greed. The Russell is up 340% from its March 2009 trough, while the profitable companies in the Index have grown earnings by 73% since then. Investors are paying record high prices for small cap equities, but are they getting commensurate value? Paging Mr. Buffett: Have we all forgotten Rule No. 2? Thank you for your investment.

DISCIPLINED VALUE PORTFOLIO – COMMENTARY BY MARK TRAVIS, CEO, PRESIDENT, PORTFOLIO MANAGER

I feel like the ancient mariner: "Water, water, everywhere, nor any drop to drink."[9] For us, as your fellow shareholders and fund managers, a market that keeps going up, up and away can be frustrating. It's easy to become myopic in an industry where everyone appears to be making easy money. The annualized S&P 500 returns for the trailing 1-, 3- and 5-years are all very compelling at the moment, but they are a relative anomaly historically and are only one side of the market cycle equation. Would you be as comfortable with a five-year string of double-digit returns if you knew they would be followed by a 30% - 50% reduction of your capital?



Well, here we are again! Our refusal to overpay for high-quality, cash-generating businesses has left us with more than ample cash balances in the Intrepid Disciplined Value Portfolio (the "Portfolio"). As of September 30, 2017, the Portfolio consisted of 64% in stock and 36% in cash and T-bills. For the year-to-date period, the Portfolio increased 5.2[illegible] net-of-fees. The return for the third quarter was an increase of 0.6[illegible] net-of-fees. Since inception, the Portfolio has an annualized return of 9[illegible], net-of-fees, which compares favorably to the S&P 500 Index's return of 8.57%. In addition, the Portfolio has taken considerably less risk (see chart to the left).

The Portfolio's five largest contributors during the quarter were Teradata (ticker: TDC), Verizon Communications (ticker: VZ), Apple (ticker: AAPL), Oaktree Group (ticker: OAK), and Dollar General (ticker: DG). The Portfolio's five largest detractors for the

9 Coleridge, Samuel Taylor. "The Rime of the Ancient Mariner." *Poetry Foundation.* June 2015. Web. 4 October 2017.

quarter were Leucadia National (ticker: LUK), Alamos Gold (ticker: AGI), Northern Trust (ticker: NT), Contango Oil/Gas (ticker: MCF), Coach (COH).

We continue to broaden our search geographically to find attractive investments for the Portfolio. Thank you for investing with us. If there is anything we can do to serve you better, please ask.

INCOME PORTFOLIO – COMMENTARY BY JASON LAZARUS, CFA, PORTFOLIO MANAGER

Global financial markets continued to appreciate nearly unabated in the third quarter ended September 30, 2017. Nearly every major asset class posted gains in the period. The most followed U.S. stock indexes garnered mid-single-digit returns. Major fixed income indexes posted more modest gains in the low-single-digits. The markets have experienced historically low volatility as stocks notch record after record. By the end of September, the S&P 500 reached 41 straight weeks without moving up or down by more than 2%. There are only two periods with longer streaks; the mid-1960s and the mid-1990s.[10]

The yield curve shifted slightly higher across most tenors, but the move was more pronounced at the front end of the curve as the probability of a December 2017 rate hike increased. Treasuries provided positive returns despite higher interest rates. The Bloomberg Barclays US Aggregate Bond Index, which represents the broader U.S. investment grade bond market with roughly 9,500 bond issues, returned 0.85%. Exposure to credit risk was rewarded in the quarter. Corporate bond spreads across all ratings tightened in the quarter, and lower-rated bonds generally outperformed. The BAML U.S. Corporate Index, which comprises investment grade corporate bonds, returned 1.37% in the quarter. The BAML High Yield Index rose 2.04%, and the BAML 1-5 year BB-B Index, which we believe is most representative of the Intrepid Income Portfolio's (the "Portfolio") investment style, increased 1.44%.

In contrast, the Portfolio returned 0.73%, net-of-fees. The Portfolio's cash and Treasury bills allocation, which averaged about 15% of assets in the quarter, was partially responsible for the performance drag. Additionally, approximately 38% of assets were held in short-term investment grade corporates, which underperformed longer-duration issues. Our strategy has always been to focus on making calculated credit bets while minimizing interest rate risk, hence our short-duration posturing. High-yield rated corporates accounted for roughly 30% of the portfolio, most of which were BB-rated issues. Our high-yield positioning has been very defensive as yields have been near all-time lows, which also contributed to the underperformance. It's also important to note that a large number of the Portfolio's holdings are not included in our primary benchmarks. In the third calendar quarter, the Portfolio's largest contributors were Regis's 5.5% notes due 12/02/2019 (ticker: RGS) and Consolidated-Tomoka Land's 4.5% convertible notes (ticker: CTO), both of which are discussed below. There were no material detractors in the quarter.

Several of our short-duration investment grade holdings matured in the quarter ended September 30, 2017. Only one core high-yield position was called; Sally Beauty's 5.75% notes. We sold the remainder of our Dominion Diamond stock after the previously announced buyout offer from The Washington Companies was increased. Our purchase activity was mostly limited to new short-term investment grade holdings and additions to existing positions. We purchased two new high-yield issues that are likely to be called in the near-term, and therefore aren't worth detailing here, but we expect our initial work on these two companies to pay dividends as both are likely to be high-yield issuers for the foreseeable future.

Last year we owned the bonds of three different publicly-traded pawn shop operators – EZCORP (ticker: EZPW), Cash America (ticker: CSH), and First Cash Financial (ticker: FCFS). First Cash acquired Cash America in September 2016 and retired the Cash America bonds at a significant premium as required by the make-whole covenant. At the time, Cash America and a bond investor were engaged in a long-running lawsuit related to the retirement of $103.5 million of the notes after Cash America spun off an online lending business in 2014. Despite the notes being non-callable at the time, CSH did not pay a make-whole premium on this partial retirement. Summary judgement was completed on September 19, 2016, and the judge ruled in favor of the bondholders. The only disagreement was the amount of compensation that would be awarded to bondholders. After several short

10 "Could this be the Least Volatile September Ever?" *LPL Financial Research*. 27 September 2017. Web.

delays, the parties came to an agreement. On January 13, 2017, the Portfolio received payment of the settlement proceeds.

Consolidated-Tomoka is a Florida-based owner of office and retail income producing properties located across the United States. It also owns several thousand acres of undeveloped land near I-95 in Daytona Beach, which it has been monetizing over the past few years. The notes pay a reasonable 4.5% coupon to the March 2020 maturity and are also convertible into common stock. We believed the yield offered by the bonds was attractive before considering the value of the convertible option. Nevertheless, the option contributed to the Portfolio's performance in the fiscal year as CTO's shares have appreciated materially since our purchase of the bonds.

The Portfolio's largest position is Regis Corp.'s 5.5% notes. We have been a lender or equity owner of the company on several occasions in the last ten years. Regis is the country's largest owner and franchisor of hair salons. The most recognizable banners are Supercuts, MasterCuts, and SmartStyle/Cost Cutters locations in Wal-Mart stores. Regis has struggled over the last several years, and management turnover has been high as the company continues to search for skilled turnaround executives. Nevertheless, we continue to believe the notes offer an attractive risk-adjusted yield with a very short duration. While the company has performed poorly operationally for some time, the balance sheet remains very clean.

Dominion Diamond (ticker: DDC) is the world's third largest diamond producer. The company owns interests in two mines located in Canada, which is one of the most stable political jurisdictions in the world. While the diamond industry is not recession-resistant, the long-term supply and demand fundamentals appear to be supportive of prices. Diamond mines can take over a decade to construct from start to finish, which tends to stabilize the supply side of the equation. Furthermore, because just four producers account for roughly 75% of global production value, the industry has historically been quite rational in pulling back supply in the face of weak end-market demand. The firm has a very strong balance sheet that includes a large cash balance and sizeable inventory of diamonds. Shortly after we purchased the shares, Dominion received an unsolicited buyout offer at a 36% premium to the prior closing price.

Our investments in two bonds issued by rent-to-own operator Rent-A-Center (ticker: RCII) detracted from the Portfolio's performance in the fiscal year. We trimmed the positions late in calendar 2016 and exited completely in early 2017 when the business started to deteriorate significantly. Rent-A-Center's issues at first appeared to be transitory, but subsequently the business did not improve as we expected. Readers can find more commentary on our view in the Portfolio's Q117 commentary. Primero Mining's 5.75% convertible notes were the largest detractor in the twelve months ended September 30, 2017. We invite readers to review the Intrepid Small Cap Portfolio's quarterly commentaries for more detail on Primero. Portfolio manager Jayme Wiggins distills the situation with much more clarity than I can hope to provide.

Over the past few quarters we have reported on a number of specific events or securities that appeared to indicate excessive risk-taking behaviors. We wish we could report to you that some level of normalcy has returned to the financial markets, but unfortunately that isn't the case. Consider the following recent bond issuances:

- Austria issued 100-year bonds that pay 2.1% annually.
- Tesla secured a 5.3% coupon on its $1.8 billion B- rated bond issue due in 2025. This is the lowest coupon ever for its maturity and rating. The company is expected to burn $3.3 billion in cash in 2017.
- HD Supply Waterworks, a distributor of water, sewer, and fire protection products, was able to issue bonds at a coupon lower than the firm's leverage ratio. The bond received orders that totaled ten times the size of the offering.

These are just a few of many instances where downside risks appear to be completely ignored. Most fixed income subsectors are offering the lowest spreads since 2007. Absolute yields are at or near record lows. Nevertheless, there is evidence that credit qualities are deteriorating. Covenant quality, as measured by Moody's, is near the weakest on record. Corporate leverage ratios are extended beyond levels experienced before the credit crisis. In fact, a recent study concluded that 80% of large

corporations have debt-to-EBITDA ratios above 4x, and half have debt-to-EBITDA ratios greater than 5x. In addition, recent recoveries on defaulted bonds have been lower than historical levels, a condition we believe could continue and lead to larger capital impairments than in past cycles.

It should not come as a surprise when we say we are having difficulty discovering securities that offer adequate risk-adjusted yields. We will not deploy your capital into high-risk securities promising just a few percentage points in annual returns. In the absence of attractive opportunities, the Portfolio will continue to hold Treasury bills and short-term investment grade bonds. We are diligently searching for pockets of value in what may be under-explored corners of the market, including bonds with small issue sizes, convertible bonds and preferred stock. Thank you for your investment.

INTERNATIONAL PORTFOLIO – COMMENTARY BY BEN FRANKLIN, CFA, PORTFOLIO MANAGER

"Extrapolation is instinctive, while mean reversion is not."
— Tobias E. Carlisle, *Deep Value*

During the quarter, the Intrepid International Portfolio (the "Portfolio") outperformed the MSCI EAFE Index (the "Index") on the upside. In the past, we have warned that this would not likely be the case. However, we have also stated that we expect our performance will be a result of movements in specific individual stocks rather than a broad change in global market performance. Such was the case this quarter, with a few individual holdings pulling the portfolio higher. For the quarter, the Portfolio returned 6.64%, net-of-fees, compared to the Index's return of 5.40%. Every currency we are invested in appreciated during the quarter; however, we did not participate due to our hedging policy, which we estimate reduced performance by over 2%. In fact, during the quarter the euro rallied to its highest level since 2015. The MSCI EAFE Hedged Index returned only 3.74% during the quarter. Something else we have preached in the past is to eschew paying attention to one quarter's performance; however, we understand that reporting results this frequently makes it difficult not to do so. To help, we will ignore any more discussion on quarterly performance and instead review individual positions.

Extrapolating recent results, be it mutual fund performance, a company's earnings, stock market performance, roulette odds, or your favorite college football team's wins is a distinct, built-in instinctual bias. It is also difficult to overcome. However, when declining earnings are extrapolated into the realm of forever, any valuation calculation will result in a low assessment of value. In the book *Deep Value*, author Tobias E. Carlisle explains this in more detail:

"We make cognitive errors. They are easy to make because the incorrect decision—rejecting the undervalued stock—feels right, while the correct decision—buying stocks with anemic, declining earnings feels wrong. Extrapolation is instinctive, while mean reversion is not. And when we extrapolate the fundamental performance of stocks with declining earnings, we conclude that the intrinsic value will ultimately become less than the price paid. But, that is not what the data show. The research shows, first, that valuation is more important than the trend in earnings. Cheap, low, or no-growth portfolios systematically outperform expensive, high-growth portfolios, and by wide margins."

Our three largest contributors in the quarter could easily be put in the camp of "cheap, low, or no-growth." The first, Coventry Group (ticker: CYG AU), was a top detractor last quarter but returned over 90% during the third quarter. The second, Programmed Maintenance Services (ticker: PRG AU), returned nearly 70% due to a buyout offer. And our third highest contributor, Noranda Income Fund (ticker: NIF CN), was also a large detractor last quarter.

Our largest detractors in this quarter were Quarto Group (ticker: QRT LN), GUD Holdings (ticker: GUD AU), and HNZ Group (ticker: HNZ CN). New purchases in this quarter include Baldwin & Lyons (ticker: BWINB), Mediagrif Interactive (ticker: MDF CN), and Gattaca PLC (ticker: GATC LN). During the quarter we sold our entire Mytilineos position (ticker: MYTIL GA), and our Spotless Group (ticker: SPO AU) holding was acquired by another firm.

Coventry Group is an Australian wholesaler of fasteners (nuts and bolts). It is a simple business, but due to mismanagement has suffered declining performance. We have discussed the investment in the prior few quarterly commentaries. Last quarter we

stated, "we have had a productive conversation with the Chairman of the Board. We believe he understands the urgency required, and we think he will take the necessary steps if the business does not quickly turn around." An Australian activist firm has come to a similar conclusion regarding the required urgency, and has taken tangible steps to aid with the change. Despite what we believe are the beginning stages of a turnaround, revenue is still declining. However, the stock price had fallen to such low levels relative to our estimate of intrinsic value that any positive change was likely to send the stock higher. We believe the *relative* improvement in results (despite still being negative), coupled with an increased stake by activists, resulted in this significant rebound in price. We still believe the intrinsic value of this investment is higher than its current trading price.

Programmed Maintenance Services is a long-standing holding in the portfolio. The Australian firm, which provides property maintenance services, as well as other facility management and staffing functions, announced on July 14th that PERSOL HOLDINGS, a Japanese staffing firm, has entered a Scheme Implementation Deed under which PERSOL will acquire Programmed for a 68% premium to the closing price the day before. The acquisition price was far above our estimate of intrinsic value, and we attribute the performance above our valuation as just plain luck. We have not fully exited the position in an effort to minimize short-term capital gains taxes for our shareholders. Many of our purchases occurred within the past year, and waiting for the deal to go through should result in gains being taxed at the long-term rate. We do not typically let the tax tail wag the investment dog, but in this case, we felt it was worth it.

Noranda Income Fund is a Canadian zinc smelter that has been going through the bottom arc of the cycle for zinc smelting treatment charges, meaning they will not earn much money in this environment. This is another example of a company that is on our "cheap, low, or no growth" list. To add insult to injury, half of their workforce is on strike. Due to the low treatment charges, the loss of the workforce is not causing them to give up a substantial portion of earnings. Meanwhile, zinc metal prices have been increasing, and are up over 20% year-to-date. Noranda receives a fixed fee for smelting 85% of the zinc metal recovery gains, but the portion above this they can sell at these higher market prices. We believe this is one reason for the stock's performance during the quarter. Additionally, we believe the cycle for zinc is shifting towards favoring the smelters over the mining companies, which should bode well for Noranda's long-term earnings profile.

Quarto Group, a UK-based illustrated book publisher, had a challenging first half to its fiscal year. In early July, the company announced that market expectations for profitability were set too high. This is a seasonal business, and many of their retail customers have been buying closer to the holiday shopping season. This fundamental shift has been happening over several years, although this year the change was exacerbated by the company selling many adult coloring books in the first half of the prior year, which concealed the seasonal impact in last year's first half earnings performance. One month after the profitability warning, the company announced they were approached by a potential buyer of the entire firm at what the Board considered "to be attractive and reflective of the inherent value of the business." Later, it was announced that the talks had fallen through, but we believe there is still a possibility of a buyout at some point in the future.

The Australian aftermarket automotive parts wholesaler, GUD Holdings, did not perform well in the quarter with a share price decline of 12% in US dollars. This firm has been on a recent upward trajectory in earnings. Prior to this quarter, the stock had appreciated significantly, and we reduced our position. We believe the recent trend in earnings resulted in other market participants extrapolating even better results. When the company *reported* results in-line with reported expectations, the stock began its reversal.

HNZ Group is a global helicopter operator based in Canada. Approximately 40% of the company's revenues are derived from the oil/gas industry. Low oil prices have pressured these customers, which has squeezed margins for companies like HNZ. Unlike major competitors, however, the majority of HNZ's revenues come from onshore business and other ancillary services that are less dependent on oil prices. With one of the strongest balance sheets in the industry, we believe HNZ can withstand an extended period of industry gloom. We believe the long-term value is significantly higher than where the stock is currently trading.

Baldwin & Lyons is a property and casualty (P&C) insurer specializing in underwriting policies for trucking companies. Intrepid first invested in Baldwin over a decade ago, and we are very familiar with the business. The company's recent results have been lackluster and reflect industry-wide challenges for commercial auto insurers. Settlements awarded to defendants in trucking accidents have skyrocketed in recent years, and the pricing of premiums has not kept up. The insurance industry tends to be cyclical, and we expect Baldwin to soon deliver results more consistent with historical norms. We are comforted by the company's long-term history of conservative underwriting and a very strong balance sheet. The International Portfolio opportunistically purchased shares when Baldwin's P/B multiple reached lows not seen since 2010. Several Baldwin executives also purchased stock while we were buying.

Mediagrif International was a new purchase for the Portfolio. Based in Canada, the company owns and operates a collection of B2B (business-to-business) websites. Some of the legacy websites are becoming outdated, while more recently acquired sites are helping offset the decline from older sites. The market seemed to sour on the stock as challenges with organic growth persisted. Although legacy sites have struggled, the company is generating excellent free cash flow that we believe is under-appreciated by other investors. We expect this cash flow to be deployed wisely by Mediagrif's CEO, Claude Roy. Having founded and sold a web-based business himself, Mr. Roy understands the industry well and has invested the company's capital in faster-growing websites. Mr. Roy owns 24% of the company, so his interests are well aligned with ours. The stock has a free cash flow yield of 10%, and we believe there is potential for significant upside as legacy websites become a smaller piece of the overall picture.

Gattaca is the number one UK engineering recruitment firm, and the number five technology recruitment firm. Brexit has weighed on results, but the company recently expanded internationally, which should help minimize the challenges in their domestic market. Since Brexit was announced last June, all their public peers' stock prices have recovered significantly; however, Gattaca has fallen and remains at a cheap price relative to earnings and cash flow.

Mytilineos, our first (and perhaps last!) investment in Greece, was discussed in more detail last quarter. We exited the position with a tidy profit; however, to be completely candid, this had more to do with luck than superb analysis. Spotless Group announced in the first quarter that competitor Downer EDI (DOW AU) made a takeover offer for their shares. We accepted their bid for our shares, which was completed during this quarter.

As we look forward, we believe we will be able to source interesting one-off ideas, but are not excited about "the market." Many times, these potential holdings look like they were beaten by the ugly stick, but that is one of the opportunity sets we investigate, and the only one where we are currently finding any value. In spite of recent weakness in many of these investments, we believe in a reversion to the mean. However, we do not blindly assume this; rather, we analyze each situation and give an assessment on whether the problems are fundamental or evanescent. We will continue to research stocks the market views as repugnant, which we hope will result in pretty returns. Thank you for your investment.

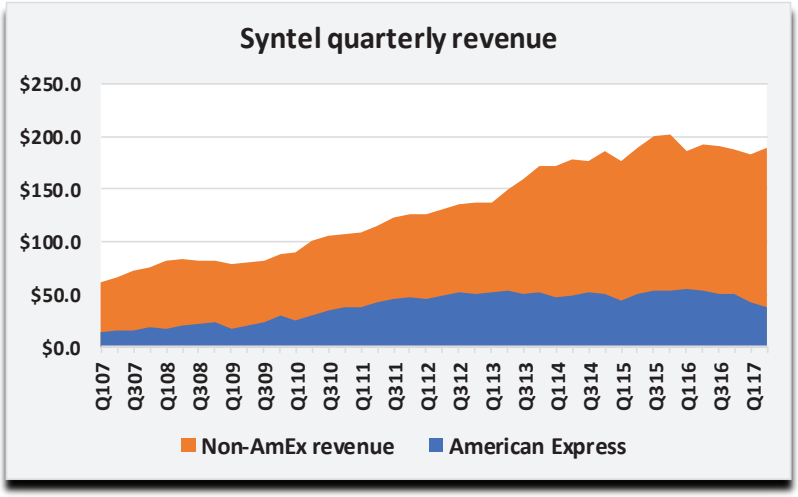
SELECT PORTFOLIO – COMMENTARY BY JAYME WIGGINS, CFA, CIO, PORTFOLIO MANAGER

The Intrepid Select Portfolio (the "Portfolio") increased 2.71%, net-of-fees, for the third quarter ending September 30, 2017, while the Russell 2000 increased 5.67%. The S&P MidCap 400 rose 3.22% during Q3. The Morningstar Small Cap Total Return Index jumped by 4.67% during the quarter. We are now disclosing additional benchmarks because Russell representatives want to charge us to use their benchmark. We may transition to a different small cap benchmark over the coming year. Cash accounted for 10.8% of the Portfolio's assets as of September 30th.

The Portfolio acquired one new holding during the third quarter. Greenhill & Co. (ticker: GHL) is an independent investment bank that provides advice on mergers and acquisitions, raising capital, and restructurings. The stock recently fell to all-time lows due to the company's failure to participate in the latest Mergers & Acquisitions (M&A) boom. Greenhill's 2017 operating results are forecasted to be the worst ever recorded for the firm. Absent a sharp pullback in overall M&A activity, we believe 2017 will mark a trough in the company's performance and Greenhill's stock will rebound when 2018

results return to more normalized levels. We believed the shares were trading for approximately 10x adjusted free cash flow, assuming a cash impact from stock compensation, when we began establishing our stake. On September 25th, Greenhill announced a leveraged recapitalization (taking on debt to buy back its own shares) that sent the shares up by 16% before we could finish building our position. The stock is still trading below our estimated fair value, but we are not thrilled with the company's new leveraged balance sheet. With that said, investment banking is a cash-generative business, and we think Greenhill could pay off its debt in less than five years. We currently plan to hold the name to wait for an expected recovery in Greenhill's revenue.

The largest contributors to the Portfolio's performance in the third quarter were Syntel (ticker: SYNT), Teradata (ticker: TDC), and Dominion Diamond (ticker: DDC).



Source: Company filings

We believe the prescription to fix Syntel is simple: the company needs to grow revenue. Syntel has been disproportionately affected by a reduction in IT spending by American Express, its largest customer. However, the business has also been starved of new relationships due to an overly lean business development budget. Syntel is addressing these issues through increased marketing spending and a greater involvement from executives in closing deals. The company showed modest progress on this front in the second quarter, as revenue excluding American Express increased 3% sequentially. It's too early to call a recovery. Nonetheless, immigration-related rhetoric has noticeably decreased, possibly indicating less of a headwind to Indian IT outsourcers from regulatory changes. Furthermore, the Indian rupee has weakened against the dollar over the past month, which relieves some pressure on the cost side for outsourcers. The stock is selling for approximately 11.5x expected free cash flow.

Teradata's stock continued to exhibit its normal earnings-related volatility. This time, the shares reacted favorably to the numbers, even though revenues and margins fell again. We think the company is making progress on its transition to a subscription-based model. Recurring revenue grew by 7% in constant currency during the quarter and now represents half of total revenue. Management projected that overall revenue will grow in 2018, marking a key inflection point. While the company's results are far from clean, we maintain our positive view of Teradata's trajectory.

On July 17th, Dominion announced it would be acquired by The Washington Companies for U.S. $14.25 per share. The board had been conducting a strategic review since Washington first expressed interest earlier in the year. The takeover price represented a substantial premium to our $9.03 average cost basis in the shares, although we had partially reduced the position in March and April when the price was lower and a takeover was less certain.

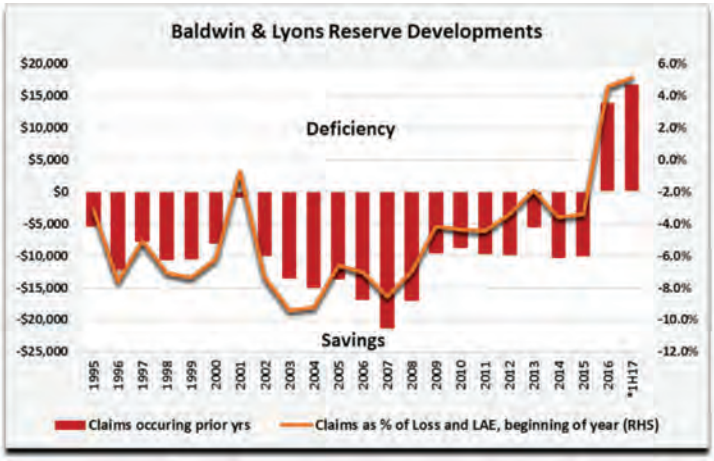
The largest detractors to the Portfolio's performance in the third quarter were Coach (ticker: COH), Baldwin & Lyons (ticker: BWINB), and Leucadia (ticker: LUK).

Coach's stock dropped sharply after the company's fiscal Q4 earnings release, in which management provided softer-than-expected guidance. We think investors were expecting too much. The fourth quarter results were decent compared to the prior year, with rising operating margins and stronger free cash flow. Looking ahead, the company forecasted low-single digit organic growth for fiscal 2018, which reflects reduced square footage. The company will attempt to turn

around the recently acquired Kate Spade using the same approach it used to revive Coach's own performance. This includes a pullback in certain distribution channels like online flash sales.

Baldwin & Lyons, the property and casualty insurer, is trading at a multiyear low Price to Book multiple near 0.8x. This is less than half the median multiple of other small cap P&C insurance firms. Baldwin specializes in commercial trucking policies, like FedEx contractors. According to Fitch, the commercial auto industry is experiencing its worst underwriting performance since 2001 as a result of accidents caused by texting and unexpectedly high jury awards. These factors have recently led to unfavorable reserve developments at Baldwin, which previously had an unblemished history of conservative reserving. In response, the company and other insurers are increasing premiums and promoting technology to monitor and control smartphone usage in an attempt to reduce accident rates. Competitors like AIG and Zurich have pulled back from certain markets. We believe Baldwin will restore its profitability, which will lead to a recovery in the stock price. Insiders have been buying shares. So have we.

Leucadia's shares declined by a few percent during the quarter, which was enough to qualify it as the third largest detractor to the Portfolio's performance. We believe the firm's second quarter results were reasonable. Jefferies, which makes up the largest share of Leucadia's results, showed decent performance in trading, with strong results in equities offset partially by lower fixed income revenue. Investment banking revenues at Jefferies were up significantly from the prior year. Jefferies also benefited from the buyout of one of its holdings, the high frequency trading firm KCG Holdings. National Beef's results improved from higher selling prices and more cattle processed. Thank you for your investment.



Source: Company filings

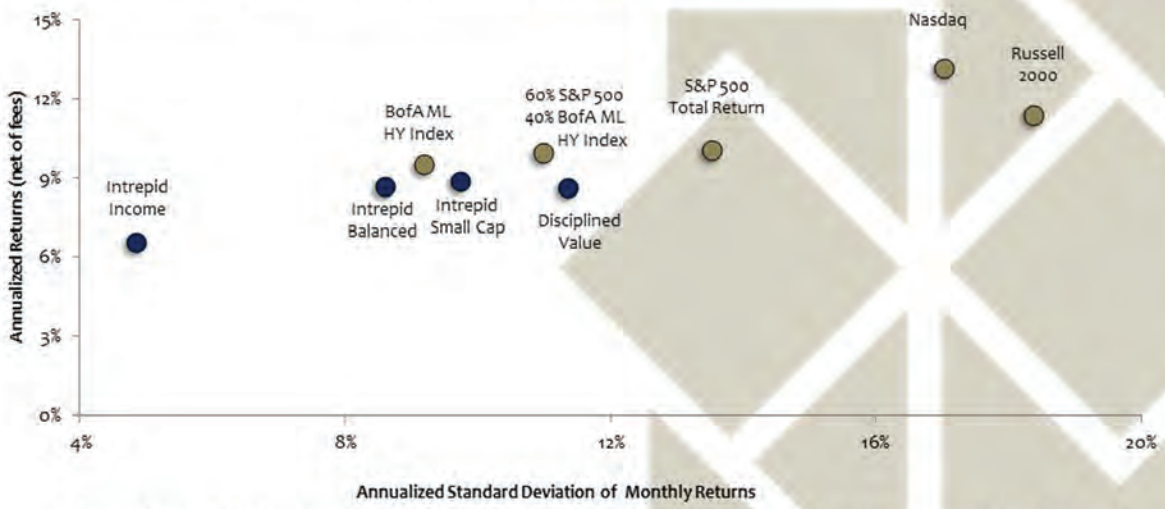
*1H17 = 1st half of 2017

Risk Adjusted Returns

Intrepid Capital

Trailing 15 Year risk/return

September 30, 2002 to September 30, 2017



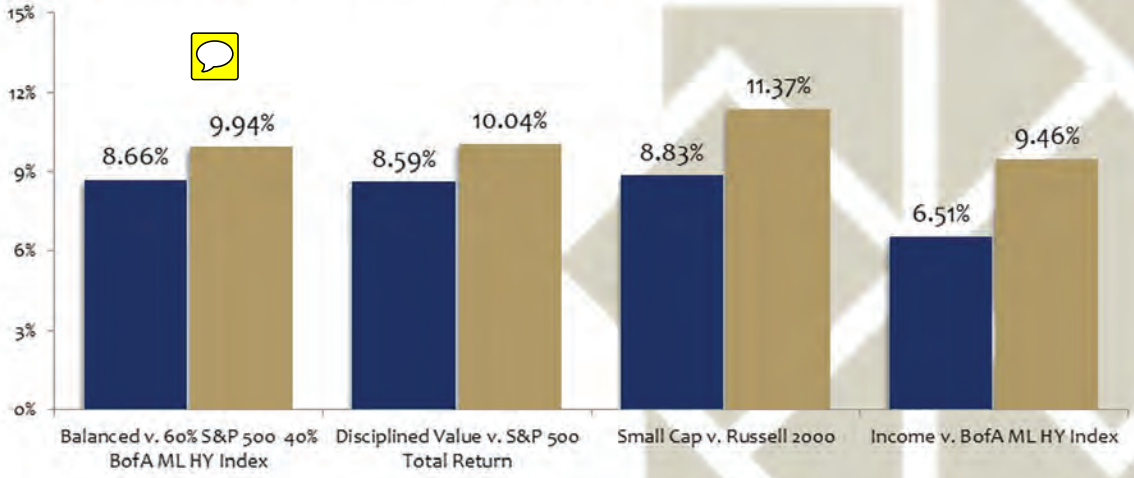
- Past performance is no guarantee of future results. Intrepid composite returns are presented net of investment advisory fees and all returns are presented annualized for the 15-year period ending September 30, 2017. Returns reflect the reinvestment of dividends and other earnings. The volatility of the listed benchmarks may differ materially from the volatility of any Intrepid composite. As of December 31, 2004, the firm changed its fixed income benchmark from the Salomon High Yield Short-Term Index to the Merrill Lynch High Yield Master II Index which, in 2016, had a name change to the BofA Merrill Lynch High Yield Index.

Annualized Performance

Intrepid Capital

Trailing 15 Year risk/return

September 30, 2002 to September 30, 2017



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