Intrepid Capital Funds
the constant pursuit of value

INTREPID INCOME FUND

4TH QUARTER 2016 COMMENTARY

4Q 2016

DECEMBER 31, 2016

PERFORMANCE

	Inception Date	Total Return: Qtr.	Total Return: YTD	Total Return: 1 Year	Average Annualized Total Returns as of December 31, 2016: 3 Year	5 Year	Since Inception
Intrepid Income Fund - Inst.^	8/16/10	0.16%	8.37%	8.37%	1.93%	3.07%	3.89%
BofA Merrill Lynch US High Yield Index		1.88%	17.49%	17.49%	4.72%	7.35%	7.41%
Barclays US Aggregate Bond Index		-2.98%	2.65%	2.65%	3.03%	2.23%	4.45%
BofA Merrill Lynch US Corporate Index		-2.88%	5.96%	5.96%	4.22%	4.25%	5.58%

^Institutional Class shares of the Intrepid Income Fund commenced operations on August 16, 2010. Performance shown prior to August 16, 2010 (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.

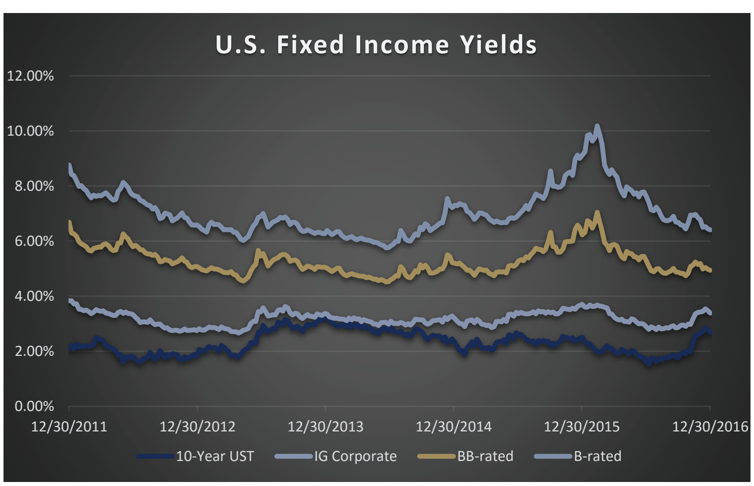
Performance data quoted represents past performance and does not guarantee future results. *Investment returns and principal value will fluctuate, and when sold, may be worth more or less than their original cost. Performance current to the most recent month-end may be lower or higher than the performance 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 0.96%. 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 1/31/17. Otherwise, performance shown would have been lower.

January 3, 2017

Dear Fellow Shareholders,

Last quarter, we wrote to you about plummeting government bond yields, $12 trillion in negative-yielding sovereign debt, and the 10-year U.S Treasury bond yield hitting an all-time low of 1.36%. We noted how the global search for yield continued to force investors to into higher-yielding securities by assuming more credit risk. Today, we write to you from a very different position. The unexpected Trump victory resulted in one of the most dramatic shifts in interest rates since 2011. The 10-year yield (shown in dark blue in the chart to the left) nearly doubled from the July lows, reaching 2.6% in December before closing the year at 2.4%. While the bump in rates appears to be merely a blip, the price impact to longer-maturity fixed income securities was considerable. For perspective, the 10-year Treasury issued on 8/15/2016 lost 7.3% in the fourth quarter, equal to nearly *five years* of coupon payments.



Source: Bloomberg

Our fixed income portfolios were not greatly impacted by the jump in rates due to our shorter-duration focus. In the fourth quarter the Income Fund (the "Fund") returned 0.16% compared to the 1.88% posted by the BofA Merrill Lynch High US High Yield Index. Investment grade corporates, as measured by the BofA Merrill Lynch US Corporate Index, declined 2.88%. The Barclays Aggregate, which measures the broader investment grade bond market including government securities and mortgages, dropped 2.98%. High-yield bonds were able to produce positive returns in spite of the jump in risk-free rates due to significant spread tightening. The Trump win improved market participants' views of the economic outlook, which significantly reduced the perceived credit risk of high-yield businesses, particularly at the riskiest end of the credit spectrum. Additionally, energy bonds benefited from the continued stabilization of oil prices. The better-quality high-yield issues that we seek to invest in rose much less than the index. Investment-grade bonds performed significantly worse due to the longer durations and already tight credit spreads. While high-grade bond spreads did tighten slightly, it was not nearly enough to overcome the jump in government bond rates.

Top Ten Holdings	(% OF NET ASSETS)
Regis, 12/02/2019, 5.500%	5.0%
Nathan's Famous, 03/15/2020, 10.000%	4.5%
FirstCash, 04/01/2021, 6.750%	4.4%
Multi-Color, 12/01/2022, 6.125%	4.0%
Tech Data, 09/21/2017, 3.750%	4.0%
Alamos Gold, 04/01/2020, 7.750%	3.8%
Total System Services, 06/01/2018, 2.375%	3.1%
PHI, 03/15/2019, 5.250%	2.9%
Starz LLC / Starz Finance 09/15/2019, 5.000%	2.8%
Dollar General, 07/15/2017, 4.125%	2.5%

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

Q416 Fixed Income Returns	
CCC and lower*	5.90%
B*	2.10%
High Yield*	1.90%
BB*	0.70%
Investment Grade*	-2.90%
Barclays Aggregate	-3.00%
US Treasury Due Aug 2046	-14.90%

**Corporate indexes provided by BofA Merrill Lynch*

The Income Fund's performance in the quarter did not mirror the high-yield or investment grade corporate indexes for several reasons. Our allocation to high-yield-rated bonds is skewed toward the higher-quality issues, which broadly underperformed lower-rated bonds. Regarding our investment-grade holdings, all of our holdings are short-duration. Our longest-duration investment-grade bond matures in the summer of 2018. As a result, these holdings were not greatly impacted by the dramatic increase in interest rates. It's also noteworthy that only about 26% of the Fund's holdings in the fourth quarter were included in either of these indexes. In the full year, the Income Fund returned 8.37%. This performance bested the investment grade corporate index's 5.96% gain and was significantly better than the Barclays Aggregate's 2.65% return. However, the Fund materially underperformed the high-yield index's spectacular 17.49% gain due to our higher-quality bent and large holdings of cash and short-term investment-grade bonds. Our invested assets performed quite well, but this was offset by an average cash position of about 26% of the Fund's assets.

The top contributor in the fourth quarter was Unit Corp 6.625% due 5/21/2021 (ticker: UNT). Unit was our last remaining energy exploration and production (E&P) company. The bonds fell precipitously early in the year as the price of crude dipped below $30, but as oil prices recovered the Unit bonds trailed the dramatic price improvements of peer companies. In the fourth quarter, the valuation gap righted itself. Unit's bonds have traded nearly back to par ($100) after dropping below $50 early in the year, which seems premature considering the still relatively depressed state of oil prices at less than $55 per barrel. We took the opportunity to exit the position.

The Fund's second largest contributor was Corus Entertainment common stock (ticker: CJR/B CN), which in past periods has been a detractor. The stock recovered materially in 2016. We believe the company remains undervalued, and we are attracted to the 8.8% dividend yield.

Alamos Gold 7.75% due 4/01/2020 (ticker: AGI CN) was the Fund's third largest contributor. The gold miner continues to plow ahead with the ramp-up of its flagship asset in Canada. Higher gold prices for most of the year allowed the company to generate significant cash to invest in its mines, which has left the company with an enviable balance sheet.

There was one material detractor (greater than 10 basis point impact) in the fourth quarter, which was Primero Mining's 5.75% convertible bonds due 2/28/2020. This issue is a new purchase for the Fund. Primero is a small gold miner with a key project in Mexico. The company is working through some labor issues with this mine, as well as trying to rectify a tax situation with the Mexican government. As if these issues weren't enough, Primero also has somewhat limited liquidity and is attempting to renegotiate its credit facility. There are clearly some risks to the position, but at 60 cents on the dollar, the yield is 24.8%. We believe we are being fairly compensated to assume these risks, and ultimately we think the company will be able to work through these near-term issues.

In the fourth quarter, we initiated positions in several short-term, investment-grade corporate bonds as higher risk-free rates provided attractive entry points. These securities all have a duration of less than one year. We also invested a large portion of our cash balance in U.S. Treasury bills. Regarding higher-yielding securities, we identified three bonds that we believe offer attractive risk-adjusted yields. Our investment in Carrols Restaurant Group 8% notes due 5/01/2022 is discussed below. Primero mining was our second purchase, and the third purchase will be discussed in a future letter.

Carrols Restaurant Group (ticker: TAST) is the U.S.'s largest franchisee of Burger King restaurants with 734 stores in 16 states as of the company's last quarterly filing. The store count is closer to 800 including recent transactions. The firm's restaurants are primarily located in the Northeast, Mid-Atlantic, and Midwest. Carrols has grown over the last five years due to a consistent acquisition strategy and an improvement in Burger King's image. In 2010, Burger King corporate was acquired by Brazilian private equity group 3G Capital. 3G is well-known for its superior operating ability, and Berkshire Hathaway has partnered with the firm on several large deals, including Tim Hortons, H.J. Heinz, and Kraft Foods. In 2012, Burger King corporate sold its company-owned stores to Carrols and entered into a partnership, which essentially made Carrols the franchisee of choice. Burger King also made an investment into Carrols (via a portfolio company called Restaurant Brands International) and placed two directors on the board.

Carrols has not generated meaningful free cash flow over the last few years due to heavy investment in store remodels. However, these are necessary expenditures to ensure the long-term viability of the business. As the remodeling program nears completion, Carrols should generate strong free cash flow. While the restaurant business is highly competitive, we like that Carrols operates in a segment of the industry that appears to be less susceptible to trends and fads. The Burger King brand is over 60 years old and is well-established. Furthermore, we believe the partnership with 3G is a valuable enhancement to Carrols's credit quality.

Several of the Fund's holdings were called, sold, or matured in the fourth quarter. Investment grade bonds representing roughly 6% of the Fund's assets matured in the quarter. One of our largest positions, Pitney Bowes International Holdings preferred stock, was called by the company. We've written about this position in the past, but to quickly recap, this was a unique security issued by a subsidiary of Pitney Bowes, which provides integrated mail and document management systems. The preferred had a feature called a step-up coupon. In October 2016, the 6.125% coupon was set to increase by 50% twice per year going forward. While the security technically never matured, the step-up coupon effectively forced the company to redeem the preferreds or pay onerous coupons to investors. The security was called in October as we anticipated it would be.

We sold our positions in the bonds of Era Group, Unit Corp (discussed above), and Ruby Tuesday. These were smaller positions. Era Group (ticker: ERA) is a provider of offshore helicopter services to energy companies. The company was recently required to fully consolidate the financials of a Brazilian subsidiary into its publicly reported financials. In our opinion, this action significantly muddies the ability of investors to assess the cash generative ability of the business. This is particularly concerning to us in the context of the firm's deteriorating domestic business. We concluded the small position was consuming too much of our analytical workload to warrant holding.

Ruby Tuesday (ticker: RT) owns and operates its namesake restaurants across the United States. The company is well-known as one of the first purveyors of the salad bar, which it calls the "Garden Bar." The restaurant industry is extremely competitive, which typically steers us away from these businesses. However, while most restaurants are leased by the operators, Ruby Tuesday owns a significant number of its stores. Over the years, it has been successfully monetizing underperforming stores. While the brand was struggling through a turnaround, the real estate-backed asset value allowed us to be comfortable lending to the firm. Fast forward more than four years – restaurant performance has still not stabilized, and the company is again implementing a menu refresh in an attempt to stem the bleeding. If the concept can't succeed in the slowly improving economic environment of the last few years, it's difficult to imagine a scenario in which store performance will stabilize. While RT's asset value is still adequate, we see the notes as fully valued close to par.

The commodity rebound and Trump-induced spread tightening have pushed high-yield corporate bond yields back near all-time lows. We are treading very carefully this far into the cycle. As the global hunt for yield continues, we want to be cautious of the potential for a reset in risk profiles. Not everyone can fit through the door at the same time. We believe the portfolio is well-positioned to withstand such a scenario.

We wish you a happy New Year. Thank you for your investment.

Sincerely,

Jason Lazarus, CFA
Intrepid Income 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 BofA Merrill Lynch US High Yield Index tracks the performance of US dollar denominated below investment grade corporate debt publicly issued in the US domestic market. Qualifying securities must have a below investment grade rating (based on an average of Moody's, S&P and Fitch), at least 18 months to final maturity at the time of issuance, at least one year remaining term to final maturity as of the rebalancing date, a fixed coupon schedule and a minimum amount outstanding of $250 million. 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. BofA Merrill Lynch U.S. Corporate Index (Corporate) 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. You cannot invest directly in an index.

Bond ratings are grades given to bonds that indicate their credit quality as determined by private independent rating services such as Standard & Poor's, Moody's and Fitch. These firms evaluate a bond issuer's financial strength, or its ability to pay a bond's principal and interest in a timely fashion. Ratings are expressed as letters ranging from 'AAA', which is the highest grade, to 'D', which is the lowest grade.

Basis Point is a unit that is equal to 1/100th of 1% and is used to denote the change in a financial instrument. Yield is the income return on an investment. It refers to the interest or dividends received from a security and is usually expressed annually as a percentage based on the investment's cost, its current market value or its face value. Investment Grade (IG) is a bond with credit rating of BBB or higher by Standard & Poor's or Baa3 or higher by Moody's. Yield to Maturity is the total return anticipated on a bond if the bond is held until the end of its lifetime. Dividend Yield is calculated by dividing the dollar value of dividends paid in a given year per share of stock held by the dollar value of one share of stock. Free Cash Flow measures the cash generating capability of a company by subtracting capital expenditures from cash flow from operations.

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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