INTREPID CAPITAL

1Q 2020

Index Returns	
1/1/2020 to 3/31/2020	
Dow Jones:	-22.73%
S&P 500:	-19.60%
NASDAQ:	-13.95%
Russell 2000:	-30.61%

QUARTERLY COMMENTARY

April 2020

Dear Friends and Clients,

"If you can't stop, smile on your way under."

— Bumper Sticker on Large 4-Wheel Drive Truck

In the height of the market panic this past March, I was asked to "Skype" into a CNBC Nightly Business Show. For those who may have missed it, when asked what I thought, my response was "the Federal Reserve and Central Banks of the world held rates too low for too long, giving us too much corporate debt equaling a giant margin call." From a prior letter at the end of the 3rd Quarter of 2019, I said at the time, "I believe this is an 'Emperor Has No Clothes' moment, one years hence we will look back on incredulously." Rate suppression activity by central banks around the world has encouraged all sorts of shenanigans to persist, in my opinion, from financing larger U.S. budget deficits to unicorns like WeWork, to an IPO market of largely unprofitable offerings."

Well. . .now for my "mea culpa," I wish I had better prepared our portfolios for this unforeseen global pandemic. While our portfolio results may, depending on the strategy, have "relative" outperformance, one can only eat from "absolute" returns (i.e. positive). My wife of 30 years, Rosalind, inquired recently about the performance. I replied, "nowhere to hide," with the notable exception being long maturity U.S. Treasury Bonds and gold. A ladder of these treasury bonds now has interest rates from 3 months to 30 years all less than 1.20% (30-year). I refer to them, with a touch of sarcasm, as "return free risk." It will take very little upward movement in rates to vaporize those small coupons with lost principal.

I mentioned earlier the source of "the problem," at least from my perspective, was easy and lenient credit terms for borrowers, particularly Corporate America. We entered this crisis with as heavily leveraged Corporate Sector as ever with $1 trillion of debt rated marginally investment grade (BBB). Well, when you are levered up and a new government edict is issued to suspend business activity, you now have a "Houston, we have a problem" moment. Many of these bonds' prices are now under intense pressure as leverage ratios shoot up with less cash flow to service the existing debt. As sales collapse, I have heard it said before: Stocks climb the stairs but take the elevator down. There have been 5 weeks in which the Dow Jones Industrial Average has fallen 12% or more since the fall of France in 1940. The good news is that I have been around in this business (and survived!) for almost all of them (except the one in 1940!).

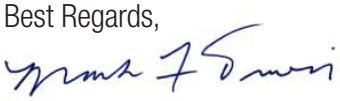
So, what are we doing about this 30% downdraft in prices? Buying! I don't know, nor does anyone here or elsewhere know where the bottom is for prices. The analogy I use is this: remember as a kid going swimming in a lake, river or ocean, and wondering, "how deep is it?" Well, you held an arm over your head, pointed a toe and started gradually letting air out to assist in your descent, knowing that if it was really deep, you didn't want to exhale all of your oxygen necessary to return safely to the surface. The portfolio management team has been taking advantage of the downdraft in prices and wild volatility to do two things: upgrade the quality of the businesses we own, looking for impeccable balance sheets (see discussion earlier) that now after this swoon in prices are much more attractively priced. Next, we are very gradually adding to companies where we already own shares and can average down our cost basis.

Lastly, in the bond market we are busily acquiring very short-term bonds with net cash (cash greater than debt) and often unused lines of credit. Our preference is the next scheduled bond in their respective maturity schedule, knowing they have the necessary liquidity to pay it off. Frankly, I think this part of the capital markets may be offering one of the better risk-adjusted returns currently, with many of these bonds fetching a low double-digit yield-to-worst.

For the quarter ended March 31, 2020, the Intrepid Balanced Portfolio (the "Portfolio") declined 19.72%, net-of-fees, compared to the S&P 500 Index's decline of 19.60% and the combined benchmark's (60% S&P 500 Index/40% Bloomberg Barclays US Gov/Credit 1-5Yr Index) decline of 11.22% for the period. The Portfolio's top contributors for the quarter were Visa (ticker: V), AmerisourceBergen (ticker: ABC), CVS Health Corp. (ticker: CVS), Mastercard (ticker: MA) and IFM US Colonial Pipeline 6.45% due 5/1/2021. The Portfolio's top detractors for the quarter were SP Plus (ticker: SP), Skechers (ticker: SKX), WNS Holdings Ltd (ticker: WNS), Copart (ticker: CPRT), and Discovery (ticker: DISCK). The Portfolio ended the first quarter with 5.4% in cash.

I know this has been scary for many of you, and as your portfolio manager, I am entirely and completely empathetic to where we find ourselves today. I won't dredge up the charts suggesting you stay invested (they are too numerous to include here), but I will leave you with this parting thought: there is opportunity in chaos and frankly we are now focused on the abundant opportunities that we haven't seen since the failure of Lehman Brothers in the fall of 2008 which ignited the Great Financial Crisis. We came through that period in fine form and I expect no different this time. As your "Captain," I will say: "Passengers, please return to your seats and buckle your seat belts, we are expecting some turbulence."

Best Regards,



Mark F. Travis
President/CEO

SMALL CAP PORTFOLIO – COMMENTARY BY MATT PARKER, CFA, CPA CO-PORTFOLIO MANAGER AND JOE VAN CAVAGE, CFA, CO-PORTFOLIO MANAGER

As I sit down to write this letter, the governor of Florida just issued a stay-at-home order for residents. Just a few weeks ago, it would have been unthinkable to see sights of empty beaches and theme parks on a sunny Saturday afternoon in the spring. Indeed, similar scenes are playing out nationwide as the country adjusts to a strange period of isolation. We hope that you and your families remain healthy throughout this challenging time.

Financial markets pivoted perhaps just as hard as everyday life during the quarter. Investors entered the year cheering on the longest ever bull market expansion with bold predictions of ever-higher stock prices, valuations be damned. Since there was no clearly identifiable catalyst for a recession, why wouldn't stocks continue to grind higher? However, after the full potential impacts of the coronavirus came more clearly into focus, stocks suffered the fastest drawdown in history. We find it interesting that most market participants seem to believe they will spot the signs of a bear market before others, and safely head for the exits before them. In our view, it is precisely this collective confidence that helps fuel bull markets on the way up and produce violent selloffs on the way down. The coronavirus, like the catalysts of other bear markets before, did not exactly repair the herd's reputation of predicting recessions and smoothly heading for the exits.

As we have discussed in countless letters before this, it has been our opinion that stocks have been broadly overvalued, over leveraged, and did not compensate investors well for bearing the risk of ownership. The Intrepid Small Cap Portfolio (the "Portfolio") had a 39% position in cash & treasuries coming into the year and a 34% position immediately prior to the significant sell-off which began on February 20th. In that respect, the Portfolio was positioned relatively well for the 41% plunge in the Russell 2000 over the next eighteen days. We should emphasize here that this defensive positioning was due to the valuations

of the stocks in our opportunity set rather than predicting how the events of the virus might unfold. Like many other investors, we closely followed news related to the virus, but could not reasonably anticipate the economic shutdown and related damage it could create until prices had already begun to reflect this risk.

The historic selloff and related volatility created some great opportunities to deploy much of the Portfolio's war chest of cash & treasuries. The Portfolio is designed to endure by remaining flexible and holding cash when valuations are not attractive and then allocating this cash into businesses that can endure in any environment. Over the duration of the quarter, approximately 19% of the 39% position in cash was invested, or about half. Our approach to investing in this crisis was not to dive directly into the "middle of the storm," but rather to scrape along the edges for higher quality businesses caught up in the selloff. By this we mean, we did not concentrate our efforts at investing in hotels, cruise lines and restaurants that bore the brunt of the carnage. Many of these businesses were highly leveraged and may depend on government bailouts for survival. Instead, we focused on identifying stocks of good businesses selling off due to temporary setbacks, but whose long-term value we believed was intact.

From a trading perspective, the Portfolio was the most active it has been in many years. We increased our position sizes of several existing names and purchased new positions in several others. As discussed before, our additions tended to be businesses with strong cash flows, good balance sheets and ample liquidity to endure through this period. Rather than provide a detailed description of each, we think it would be helpful to highlight a few areas where we concentrated a meaningful portion of our activity:

1) **Professional Sports Franchises (BATRK, MSG, MANU)** – We have written about sports franchises before. These franchises are brands that have been around for decades and have accrued massive brand value in the process (generations of fans and followers). In addition, due to the proliferation of Netflix and other on-demand entertainment, sports are one of the few forms of video content that are primarily consumed live, which has caused them to be very attractive advertising properties and thus generate increasing value in media distribution rights deals. These franchises also have tremendous scarcity value and usually change hands in private transactions at large premiums to estimated valuations – which historically have not been impacted much by recessionary environments. Unsurprisingly, these stocks sold off after sports leagues suspended their seasons, making short-term ticket and TV revenue more uncertain. We are confident that consumers will eagerly begin consuming sports entertainment again once the virus is safely behind us, and that these franchise values, based on decades of brand-building, remain strong.

2) **Outsourcers (WNS, SYKE, G, DOX, ICLR)** – We added exposure to a few outsourcing companies during the q uarter. It's likely that these companies will have reductions in profitability this year as their clients either seek price concessions, have lower volumes of activity, or the outsourced companies are simply unable to mobilize their workforce to provide service due to government lockdown orders. However, the businesses in which we have invested are leaders in their respective niches (for example: accounting, pharmaceutical research, call centers, telecom billing, etc.) and their customers have permanently shifted these functions to outsourced providers. In general, their customers simply are no longer equipped to do this work themselves, and the longstanding relationships often make it expensive to switch to a competing outsourcer. We think the value of high-quality outsourced providers of business services remains intact despite the near-term economic volatility. In fact, some of these businesses could emerge stronger if the global economy goes through a more extended downturn. Many businesses turn to outsourcers as a way to cut costs in tough times, and some of these companies have a demonstrated history of growing volumes through recessionary periods.

3) **Discount Retailers (BURL, OLLI, FIVE)** – Retailing is a notoriously tough business that has been made only tougher by the proliferation and adoption of e-commerce and omni-channel competition over the last ten years. However, there are certain physical retailing businesses that have thrived despite the intensifying competition – specifically models that can consistently provide consumers excellent value and a positive shopping experience. Within this space, we

purchased the stocks of a few off-price and "value" retailers. This is one of the few categories of brick & mortar retail that have performed well operationally over the last decade, proving to be structural market share gainers that earn attractive returns on capital. Forced store shutdowns due to the coronavirus and the fact that these businesses have little to no online presence likely drove investors to dump them in favor of e-commerce businesses. However, it is the lack of an online presence that draws bargain hunters into these stores in the first place, thereby insulating them well from companies like Amazon. Similar to what we have mentioned above, we think life and consumer behavior will mostly go back to normal after this virus inevitably runs its course, and we viewed the selloff as an opportunity to scoop up shares of these great businesses at a discount.

4) **Salvage Auto (IAA, CPRT)** – There are a number of players within the salvage auto industry, but the most lucrative position is the owner of the auctions in which totaled cars are sold. There are two companies that dominate this space and they compete rationally in a duopoly structure. These businesses have ridden a tailwind of (a) more vehicles and distracted drivers on the road leading to more accidents, and (b) a growing proportion of these damaged cars that end up totaled due to expensive replacement costs for increasingly complex parts (cameras, sensors, etc.). Earnings for these companies are expected to be hurt in the short-term as fewer people are driving during the nationwide lockdowns, leading to fewer car accidents. Some have suggested that earnings could be more structurally impacted as people may permanently cut down on driving and work remotely more often. We don't fall in this camp. While it is quite possible that there could be more work done remotely after the virus, we doubt this will be material enough to impair the long-term values of these excellent businesses.

To summarize, we found a good deal of opportunity as stock prices went into free-fall in some high quality, market-leading businesses within already attractive industries. Like all businesses, we expect their operations to take a hit with the sharp slowdown to come near-term in the economy. But in many cases, we expect the companies we purchased within these categories to come out in an even stronger competitive position than they went into this crisis.

While most of the additions to the Portfolio fit into the categories above, there were a few exceptions that the Portfolio purchased which we will briefly highlight:

- **Brown & Brown Inc. (BRO)** – Brown and Brown is one of the largest insurance brokerages specializing in the middle-market (small businesses). We are attracted to Brown & Brown's industry leading profitability, high insider ownership, and robust and consistent free cash flow generation, which we balance with the company's outsized exposure to its small business customers – many of which will struggle in the near term.
- **Fabrinet (FN)** – Fabrinet is a manufacturer of electronic components used in telecom equipment and several other industries. It is a high-quality industrial business that we have owned in the past and took advantage of the recent selloff to once again purchase the stock. We expect future investment in 5G infrastructure and related technologies to support robust future growth for their business.
- **Ryanair Holdings (RYA ID**) – Ryanair is a discount airline that primarily operates in Europe. We are not fans of the airline business in good times, and with almost all flights grounded until further notice, things could not be worse for the industry. But Ryanair is the rare exception in terms of i) airline business quality, and ii) instances where we found opportunities in the "middle of the storm." The company has perhaps the best management in the industry, with a low-cost model that has helped it gain tremendous share from other legacy European carriers while producing ample and consistent profits and free cash flow. In addition, the company has maintained a strong and liquid balance sheet and has recently revealed that it can survive an entire year without any revenue. We don't think their competitors can accomplish this, and believe Ryanair is positioned to come out of this period in an even stronger competitive position absent widespread European airline bailouts. While our position in Ryanair is relatively small, we believe it is a good example of the Portfolio's ability to be opportunistic and search overseas for value when it becomes attractive.

Despite all this buying activity, it's worth mentioning that the Portfolio still has a bullet in the chamber, so to speak, in the remaining 20.5% position in cash. Despite a historic crash in prices, we still do not believe small cap stocks are screaming bargains – a testament to how stretched we think valuations had gotten before the selloff. Proclaiming that we are in a recession right now is not controversial. More debatable, however, is how long this period will last. Will it be a V-shaped recovery that snaps back when the economy is re-opened? Or will this be a more drawn out period of weakness? While we obviously don't know for certain, we would argue the odds of the latter scenario have increased meaningfully – there is simply a tremendous amount of debt for the economy to deal with as it processes this exogenous blow. In our opinion, there are still many stocks that are not adequately pricing in this risk. There are a number of high-quality stocks in our "on-deck" circle, but we are still waiting for more attractive entry prices. To play off an old Warren Buffett-ism, we are still picking up falling stocks with a thimble and have not yet reached for the bucket.

For the quarter ended March 31, 2020, the Small Cap Portfolio returned -21.37%, net-of-fees. As absolute return-oriented investors, we are frustrated to have lost money during the quarter. Unfortunately, there were few places to hide amidst the selloff and the stocks that the Portfolio owned were not immune from the selling pressure. While it pains us to have to report that your capital suffered a loss, we think it's recoverable. Swings in prices are a reality of investing in the stock market, but we are confident in the long-term intrinsic values of the businesses that the Portfolio holds. We also view the selloff as an opportunity to deploy more of the Portfolio's cash and position itself to capture more upside when prices recover.

The Portfolio's return was more palatable compared to the -31.61% return of the Morningstar Small Cap Index benchmark. And better still when compared to value-oriented small cap indices, such as the Morningstar US Small Value category which fell 36.97%. It was yet another period in which small value indexes lagged those of larger and more growth-oriented companies. If the last two recessions are a guide, then we might expect to see a sharper recovery from small caps coming out of this bear market than large caps. The Russell 2000 suffered a larger drawdown than the S&P 500, Dow Jones Industrial and Nasdaq averages during the financial crisis, but recovered to its prior peak faster than the S&P and Dow (the Nasdaq recovered equally quickly). In the recovery following the bust of the tech bubble in the early 2000s, the Russell 2000 also led the recovery.

The top three contributors to performance were:

- **Burlington Stores (BURL)** – Burlington is one of the off-price physical retailers mentioned earlier that was purchased during the quarter. The company has improved its business meaningfully over the last decade by increasingly adopting the off-price model, jettisoning excess stores, and improving inventory turns and efficiency. We purchased the company in the midst of the panic during mid-March at very opportunistic prices, and the stock rebounded into the close of the quarter.

- **iShares Gold Trust (IAU)** – The Portfolio has maintained a small position in an ETF that tracks the price of gold for several years. The purpose of the holding has been to maintain some exposure to the precious metal as a hedge against the unprecedented monetary policy we have witnessed over the last decade. We increased our holding during the quarter (4.9% of Portfolio as of 3/31/20) after observing the government's economic response to the virus.

- **Net 1 UEPS (UEPS)** – The Portfolio sold its small remaining holding of UEPS during the quarter after the company completed the sale of its South Korean payment services business.

The top three detractors to performance were:

- **SP Plus (SP)** – SP is the nation's largest operator of parking lots, managing the parking operations for airports, commercial properties, hotels and others. While it is normally a remarkably stable business, the shutdown of the economy, particularly in sectors like air travel and hotels, will have a significant impact on parking revenues. Fortunately, the business earns about 80% of its profits from fixed contracts in which they earn a fee regardless of the lot's

occupancy. The company is one of the few owned by the Portfolio which has a meaningful amount of debt on the balance sheet, but we think the company's characteristics – stable cash flows and highly variable cost structure – can support this debt. We have increased our position size as the stock has fallen.

- **Skechers (SKX)** – Skechers is the Portfolio's second largest position behind video game publisher Take Two (TTWO). About a quarter of the company's earnings come from China, and the country is a meaningful growth engine for Skechers. We believe the impact in China will prove to be mostly temporary and that people will once again start buying Skechers brand shoes. If Nike is a good representation, the damage may not be so bad. In their most recent quarter, they reported only a 4% decline in footwear sales in China during a period (November – February) which coincided with China's peak impact from the virus. Skechers has a fortress balance sheet with cash that significantly exceeds its debt.

- **IAA Inc (IAA)** – IAA is one of the two salvage auction businesses discussed earlier. Earnings will undoubtedly be impacted from the fewer car accidents expected to take place during the shutdowns, but we think the selloff in IAA's shares may have been exacerbated by their leveraged balance sheet. While the company does have a significant amount of debt, the principal payments on this debt are not due until 2026. We expect their earnings to normalize and that the company can easily pay this back out of their operating cash flows. Like SP, we are willing to accept the financial risk of this business due to the strength of the operating business. We increased the position size as the shares fell.

The Portfolio sold out of six positions during the quarter:

- **Cabot Oil & Gas (COG)** – Cabot is one of the largest producers of natural gas, which has been in a long bear market that Cabot has navigated well due to its strong balance sheet and its position as a low-cost producer. However, due to what will likely be a significant decline in natural gas demand on top of an already over-supplied market, we have decided to reduce our overall energy exposure until we see how other producers react to the current environment. The energy industry has been dominated by irrational behavior for years, and until we have confidence that other players will begin to act more rationally about supply, we have reduced our exposure to the sector in general. As a result, we have sold our position in Cabot.

- **Garrett Motion (GTX)** – Garrett is the turbocharger manufacturing business that has unfortunately been a material detractor to performance since purchase. While we think the quality of the business is high, the balance sheet was simply too levered. We were willing to tolerate this upon initial purchase because of their highly variable cost structure, figuring that they would be able to scale back sufficiently to stay afloat if there was a global recession. We did not, however, expect that there could be a significant period in which auto production would completely grind to a halt. While the stock still appears extremely cheap on equity multiples, we believed there was simply too much financial risk and sold the stock.

- **Hilltop Holdings (HTH)** – This is a regional bank out of Texas which was sold after reaching our calculation of intrinsic value.

- **Protective Insurance (PTVCB)** – We consider ourselves to be patient investors but admit to losing patience over the five years we have owned this business. This commercial auto insurer has been trying to weather brutal industry conditions for years, but premium rate hikes have simply not kept up with skyrocketing costs to settle claims. We expect the industry will eventually become profitable again but have lost confidence in this timing. While we have confidence in the new CEO, we would need to see a clearer improvement in underwriting profitability before owning again.

- **Net 1 UEPS (UEPS)** – As noted above, we sold this holding after the business monetized its interest in a South Korean payment processing company.

- **Protector Forsikring (PROTCT NO)** – We purchased this Norwegian P&C insurer in late 2018 after some underwriting challenges led to a decline in the stock price. We judged that these issues were most likely temporary given the company's history of good results and the extremely profitable industry structure in the Nordic market. Unfortunately, underwriting continued to disappoint and there emerged a pattern of actual results that differed substantially from what the company's management had suggested. Our thesis no longer held, and we sold the shares shortly after the company's Q4 results were released.

Despite the carnage in the markets, the current investing landscape is a more favorable environment for the Portfolio's strategy than we have seen in years. Prices are cheaper, bargains are far more plentiful, and the extreme volatility has created attractive opportunities. The Portfolio is now positioned for much more upside should stocks rally higher and stands ready to deploy the remainder of its cash should volatility continue. This valuation driven approach has served well in periods such as this, and we are working diligently to assess the best opportunities in which to invest your capital for attractive long-term appreciation.

In closing, we want to express our sincere appreciation for the patience of the long-term clients of the Portfolio. Its positioning has been unconventional, leading to lackluster returns during the later stages of this record long bull market. We are hopeful that the current environment – with far lower prices and heightened volatility – will allow us to position the portfolio for much more desirable results looking forward. Thank you for your investment.

DISCIPLINED VALUE PORTFOLIO – COMMENTARY BY CLAY KIRKLAND, CFA, PORTFOLIO MANAGER

We at Intrepid Capital have long admired volatile markets as those periods (which have been few and far between over the past 10 years) tend to be when we are most active in our portfolios. The first quarter of 2020 was one for the record books as volatility spiked to all-time highs and the S&P 500 descended into bear market territory in just 16 days, less than half the time it took for the previous record back in 1929, which set off the Great Depression. As COVID-19 spread across the globe forcing governments to put measures in place that effectively shut down economies, uncertainty ensued.

The S&P 500 has moved over 1% in 24 of the last 25 trading days, which has only occurred two other times, both of which were during the Great Depression. Volatility presents opportunity. Opportunity to put cash to work and opportunity to upgrade the portfolio to more attractive investments. Volatility often results in price moves that far exceed a corresponding change in value, and that is exactly what we witnessed in the first quarter.

All domestic equity indices were off materially for the quarter across the board with large caps continuing their outperformance versus small and mid-caps. The S&P 400 Midcap Value Index was absolutely pummeled, dropping a whopping 47.50% from its high in January to its low in March. It ended the quarter with a 35.09% decline compared to The Disciplined Value Portfolio (the "Portfolio") which declined 20.53%, net-of-fees. The Russell 2000 was off 30.61% for the quarter while the S&P 500 was the most resilient with just under a 20% decline.

The Portfolio's stock selection aided its performance in the quarter as the portfolio ex-cash outperformed its midcap benchmark. Many of the larger positions going into the crash held up quite well like Dollar General which benefited from having 16,000+ stores across the country where people went to stock up on goods. Cash levels varied in a wide range of zero to over 20% during the quarter as we navigated through the volatility. At quarter end cash was 9.9%.

We added five new positions during the quarter: Americold Realty Trust (ticker: COLD), Cable One (ticker: CABO), Visa (ticker: V), Mastercard (ticker: MA), and Facebook (ticker: FB).

Americold Realty Trust is the second largest operator of temperature-controlled warehouses in the U.S. and globally. It controls 178 warehouses that have a total capacity of 1.1 billion cubic feet. It is the only pure-play publicly traded cold storage REIT. We like the cold storage business due to its "mission critical" nature as well as the overall stability of the industry. The company has a demonstrated ability to grow organically at a reasonable rate in addition to having a long runway of further consolidation opportunities to drive growth. We view Americold as a way to participate in the growth of cold food/grocery delivery over the long term.

Cable One is a cable operator that was very early in the adoption of shifting focus to its high margin internet business at the expense of its video business. This has resulted in expanding margins and organic growth that far exceeds its peers. The company's size is in the sweet spot to where it can acquire small operators and still realize meaningful accretion. We suspect Cable One may be an acquisition target as there are limited opportunities for the large players to further consolidate.

Visa and Mastercard are the two largest electronic payment processors in the world. Their large scale provides competitive advantages over peers and we anticipate continued transaction and volume growth over a very long period of time. The businesses will of course be negatively impacted by pullbacks in consumer spending due to the coronavirus, but we felt that the share price had more than reflected the risks at the time of our purchases.

Facebook is much more than its namesake as past acquisitions like Instagram and WhatsApp have proven to be massively successful. The company's reach to billions across the globe allow it to garner the second largest market share of the fast-growing digital advertising industry. Pullbacks in advertising budgets this year have caused earnings expectations to come down by over 20% and the share price had dropped even further. When advertising spend rebounds Facebook should be a large beneficiary. We purchased shares at an all-time low multiple on what we believe will be depressed earnings.

Activity in the portfolio went beyond these new positions—we adjusted many of the existing positions to become aggressive as valuations became more attractive. In other words, we aimed to upgrade the portfolio to have more exposure to businesses that were both the highest quality and whose stock price had fallen the most.

The Federal Reserve and our lawmakers did their best to prevent us from doing so by introducing unprecedented measures to help stem losses in the stock market and shore up the economy. In a series of moves, the Federal Reserve slashed interest rates by 150 basis points, introduced unlimited quantitative easing, and said it will buy corporate bonds and bond ETFs. Congress introduced a $2 trillion stimulus package and quickly thereafter signaled that there would be more to come. The Federal Reserve's balance sheet ballooned in late March and the equity markets followed suit.

We can't help but be deeply concerned with the recent jobless claims data. About 16 million people have filed for unemployment over the past three weeks, shattering prior records each week by a long shot. Will these jobs all come back like flipping a switch when the economy is "reopened?" We tend to think not.

We mentioned Cable One and Facebook as new positions. They also were two of the top three largest contributors to performance during the quarter along with AmerisourceBergen (ticker: ABC). Kroger (ticker: KR) was also a strong performer during the quarter. We exited our Cable One position shortly after the end of the quarter as the stock rocketed up above our estimate of intrinsic value. We still own the other businesses.

AmerisourceBergen is one of the largest drug distributors in the world. It has been the subject of much controversy in recent years for its role in the opioid crisis. Uncertainty around the potential liabilities has acted as an overhang on shares, but recent developments have helped alleviate some of these concerns. We have viewed Amerisource as a defensive security all along and its shares exhibited these traits during the market turmoil. We continue to value shares materially higher than where they currently trade and expect the multiple to expand as we move past the current issues.

Kroger is the largest traditional grocer in the U.S. and is one of the few beneficiaries of the coronavirus outbreak. With restaurants shutting down and residents across the country being ordered to shelter in place, consumers rushed to stock up on goods. Kroger is a natural destination as it is a one-stop shop where consumers can get food, alcohol, paper products, and fill their car up with gas in addition to picking up medication from its network of nearly 2,200 pharmacies. The company disclosed on April 1 that identical store sales ex-gas were up 30% for the month of March. While we may see gross margin pressure due to the nature of these sales and demand will surely taper off, we remain optimistic and believe shares continue to be undervalued.

The three largest detractors included Discovery (ticker: DISCK), Cubic (ticker: CUB), and Alpine Income Property Trust (ticker: PINE).

Discovery fell victim to advertisers slashing budgets as they are under significant pressure due to little consumer demand. It was also widely expected that the Olympics would be cancelled or delayed which would further hurt Discovery's profitability. It became official in late March that the Summer Games would not take place this year. Despite this, Discovery will still generate significant free cash flow in 2020. We would like to see the company pay down some debt as we believe elevated leverage also played a role in the poor share price performance.

We had always thought of **Cubic** and its businesses as defensive, so we were surprised to see shares act as poorly as they did. Much of the transportation segment's revenue is contracted so ridership at the large metropolitan clients should not be a factor. These municipalities are undoubtedly under pressure, but we believe they will honor their contracts. The company's debt profile may have played a role in the share price performance, but Cubic took steps to address this in late March when it announced it had entered into a new term loan and expanded its revolver. Leverage is still high, but its borrowing capacity increased by 30%, interest rates are now lower, and new covenants provide more flexibility.

Alpine Income Property Trust is a REIT with primarily single tenant triple net lease properties; however, many of its tenants are in the retail and entertainment subsectors being impacted the most by the lockdowns. There have been reports of many businesses, even those that appear to be on solid financial footing, asking for rent concessions. We believe that some of this is posturing given the potential handouts (forgiven loans, etc.) that may come their way, but it is negatively impacting landlords including Alpine. Shares in Alpine are much less liquid than we prefer which likely exacerbated the moves in the stock. We reduced our position to manage risk but believe that the company's net asset value is well in excess of where shares trade today.

Could we look back a year from now and all of this be just a distant memory, or is there more volatility to come? Whichever the case, we are more optimistic about the portfolio's positioning today than we have been in years. Thank you for entrusting us with your capital.

INCOME PORTFOLIO – COMMENTARY BY HUNTER HAYES, CO-PORTFOLIO MANAGER AND MARK TRAVIS, PRESIDENT/CEO, CO-PORTFOLIO MANAGER

"The more stable things become, and the longer things are stable, the more unstable they will be when the crisis hits. Success breeds a disregard of the possibility of failure."
— Hyman Minsky

Credit markets screeched to a halt in March and bond prices plummeted as debt investors crammed for the exit. The uncertainty around the COVID-19 pandemic froze out even the most creditworthy borrowers from issuing new debt. Grandiose stimulus promises did little to abate the rampant panic, at least initially. It felt to us like a Minsky Moment.

The term "Minsky Moment" was coined in 1997 to describe the Asian Debt Crisis. It would later be used to describe the Great Financial Crisis in 2008. Hyman Minsky, whose work inspired this phrase, was a prolific 20th century economist. Minsky believed that long periods of stability bred periods of instability. For instance, when the economy is humming and there seems to be no bust in sight, investors and companies take on more and more debt to maximize their participation in the economic boom. This behavior eventually leads to a tipping point, or a Minsky Moment, when the debt is no longer serviceable and there is a rapid decline in asset prices.

If we have just experienced a Minsky Moment, it is ostensibly unlike prior ones. Both the Great Financial Crisis and the Asian Debt Crisis were directly caused by excessive risk taking. This time around, an unforeseen global pandemic served as the tipping point. We would argue that although COVID-19 served as the catalyst, excessive leverage in the system exacerbated the depth and rapidness of the selloff.

Regardless, we believe the pain in debt markets is likely to get worse before it gets better. Even assuming we can get the economy back up and running over the next couple of months, which seems optimistic, the toll from months of foregone revenue will be enough to shutter many debt-laden businesses. Bankruptcies, which we have seen few of so far, would send shockwaves through the system and possibly lead to renewed panic selling. In order to avoid this, we anticipate the government printing trillions of additional dollars for fiscal stimulus and bailouts. This remedy could cause inflationary headaches down the road, but we doubt any politician will mention that. Considering all of this, we remain cautious as we search amid the junk bond rubble for attractive bargains.

Despite the beating that bonds took in March, longer duration government bonds served as a buffer for some indices as rates plummeted to new lows. Accordingly, the Bloomberg Barclays US Aggregate Index (the "Barclays Aggregate Index") returned 3.15% for the quarter ended March 31, 2020 and the ICE BofAML US Corporate Index (the "Corporate Index") lost 4.05% over the same period. Riskier debt took a walloping in the first calendar quarter, with the ICE BofAML High Yield Index (the "HY Index") losing 13.12%. The shorter-duration Bloomberg Barclays US Govt/Credit 1-5 Year Total Return USD Index (the "1-5 Year TR Index") gained 2.17% over the same period. The Intrepid Income Portfolio (the "Portfolio") lost 6.52%, net-of-fees, in the quarter ended March 31, 2020.

The Portfolio did not have any material contributors for the three months ended March 31, 2020. However, we had several credits that held up well, generating slightly positive total returns for the quarter despite the battering that the credit markets took. Despite this, many of these credits, most of which are maturing soon, traded hands at surprisingly low dollar prices. We believe this was due to technical market factors.

As money managers scramble to raise cash for redemptions or to reposition their portfolios, they are more likely to sell short-dated paper than longer-dated paper. This is because the short-dated credits sell off less than bonds that don't mature for a while, and the money manager can realize less of an absolute loss by selling these front-end bonds. In March, this dynamic led to a strange situation in which some companies' short-dated paper yielded more than its longer-dated paper. This is known as an inverted yield curve and it sometimes occurs during periods of financial stress.

The silver lining to this inverted yield curve is that we were able to scoop up additional short-dated investment grade bonds at eye-popping yields, often in the double digits. These purchases included debt from issuers like Sherwin Williams, Expedia, American Tower, and Fiat Chrysler. Most of these were bought towards the end of March at significant discounts to par and with maturity dates in the next 1-6 months. Hence, we believe we will see the fruits of these purchases soon.

To be clear, we believe that all the issuers we mentioned have enough cash on their balance sheets and/or access to credit to pay down their upcoming maturities many times over. In fact, we performed various stress tests assuming, in some cases, the total absence of revenue for these issuers until their bonds mature. Even in these unlikely scenarios, we still believe the various issuers will be able to pay down the issues we purchased.

The Portfolio's top detractors for the three months ended March 31, 2020 were energy related. We still own these positions and believe the issuers have the balance sheet strength to weather this extraordinary environment for commodities. These positions represent a small percentage of the overall portfolio but offer compelling returns at current levels:

- **EQM 4.75% Notes due 7/15/2023** – EQM Midstream is a gas gathering and pipeline focused MLP with assets in the Marcellus and Utica basins. The company's debt was recently downgraded from investment grade to high yield, creating a buying opportunity for us. EQM has contracts in place for ~70% of its revenue with no volume or commodity price exposure and we believe the strength of these contracts will carry EQM through this tough environment.

- **MUR 6.875% Notes due 8/15/2024** – Murphy Oil is an exploration and production (E&P) company with assets in Canada, the Gulf of Mexico, and the Eagle Ford Shale. In our opinion, Murphy has one of the best balance sheets among high yield E&P companies with ~1.5x net leverage and no borrowing base facility on the $1.6 billion of undrawn lender commitments that comprise its credit facility. Combined with a decent cash balance, strong oil hedges in 2020, and a very manageable maturity schedule, we believe Murphy has a long runway to endure the unprecedented supply/demand shock in oil markets. As we were writing this letter, Murphy announced cost cutting measures that include a capex cut, a dividend cut, and executive salary reductions. We believe these actions will further bolster Murphy's strong credit profile.

The Income Portfolio had six corporate bond positions that were called or matured in the first calendar quarter. We also rebalanced several positions. The proceeds from the bonds that matured or were called were redeployed into short-term paper of investment grade issuers that we believe offer attractive yields in excess of government securities. Additionally, we added to several of our existing high yield positions and bought a couple positions from new issuers, including:

- **MagnaChip Semiconductor Corporation** – MX is a South Korean semiconductor designer/manufacturer with a broad array of solutions for communications, consumer, industrial, and automotive applications. The company recently announced the sale of its Foundry business, which will generate roughly $300 million of cash after taxes; more than enough for MagnaChip to pay down the notes that we own. If the Foundry business sale falls through, which we view as unlikely, the company has a strong existing balance sheet with over $150 million of cash and has several other options to pay down the looming 2021 bond maturity

- **Teekay Corporation** – TK is a provider of marine transportation services to the oil and liquefied natural gas (LNG) industry. Through ownership stakes in its daughter companies as well as a few ships of its own, TK should continue to generate substantial amounts of cash flow that it will mainly use to pay down its debt. Most of this cash flow comes from long term LNG contracts, often lasting 10 years or more, with stable counterparties like Shell, BP, and ConocoPhillips. TK also has exposure to tanker ships, which should benefit from a potential oversupply of oil since these ships can be used as floating storage. We view TK as being well positioned to endure through today's tough energy market. We are holders of TK's convertible notes due in 2023.

Portfolio activity was otherwise subdued as we brace ourselves for this brave new world. In our opinion, nothing is certain in the near term except for more uncertainty which will likely translate into more volatility in financial markets.

The Federal Reserve continues to do everything in its power to remedy this uncertainty with heaps of liquidity and even a bit of razzle dazzle, recently announcing its intent to purchase certain junk bonds. These developments hardly surprise us, but they do concern us as we wonder where the intervention ends, or if there is any contemplation of the consequences. Consumers, companies, and industries are already lining up for bailouts which will prompt endless philosophical discussions around what makes this or that essential and why we are choosing to save this company over that municipality and so on.

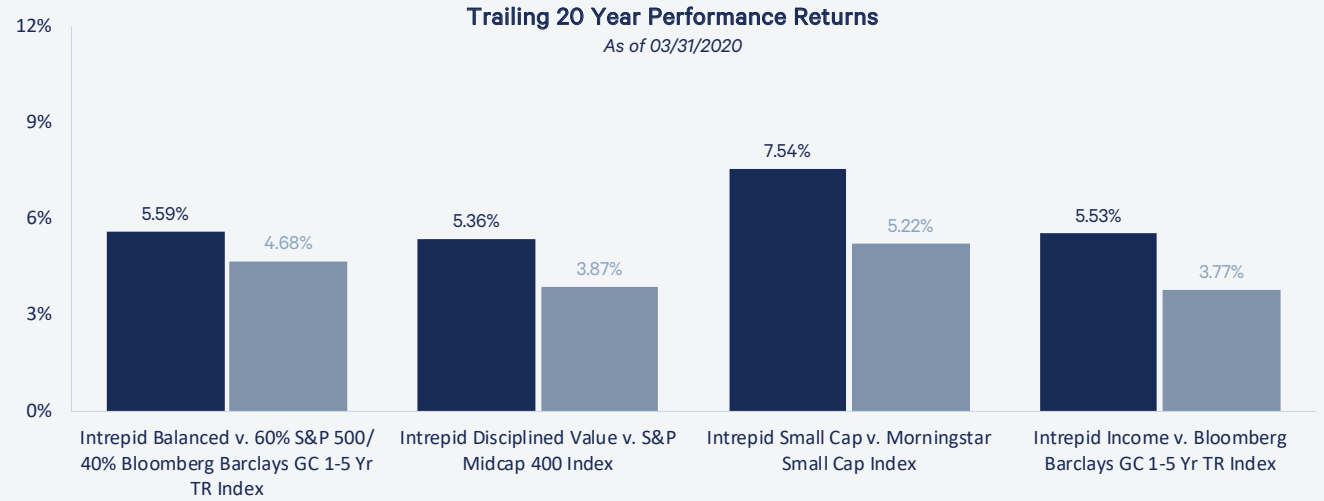
Progress is hardly ever linear, and every boom eventually has its bust. When it can operate freely, this boom and bust cycle creates a stronger, more resilient system. Our past couple dozen or so commentaries have cautioned investors about an overleveraged financial system characterized by artificially repressed interest rates, excessive risk taking, and weak covenants on leveraged buyouts that might one day inspire a sequel to *Barbarians At The Gate.* Already, many of the private equity sponsors that engineered these loans have met privately with President Trump and are surely arguing for their portfolio companies to receive some stimulus dollars.

The COVID-19 pandemic deserves a massive governmental response and we have been awed at how quickly and effectively task forces and healthcare professionals across the world have responded to this unprecedented crisis. However, we do not believe that every business deserves to survive this difficult period despite the inevitable refrain of "this time is different."

There are plenty of well-run businesses that entered this period with conservative amounts of leverage, access to liquidity, and prudently managed balance sheets despite the siren call of low rates and the seemingly sanguine state of the economy a couple months ago. Then there are businesses that borrowed as much cheap debt as possible and assumed growth would continue forever, leaving themselves very little margin for error. Both types of companies will likely struggle through this turbulent period, but which company deserves to survive? And, to ask an eerily familiar question, what sort of signal will it send to future borrowers if we bail out both?

Amid all this uncertainty, we continue to diligently search for attractive opportunities to lend to resilient companies with conservative amounts of leverage, adequate liquidity, and robust balance sheets. Thank you for your investment.

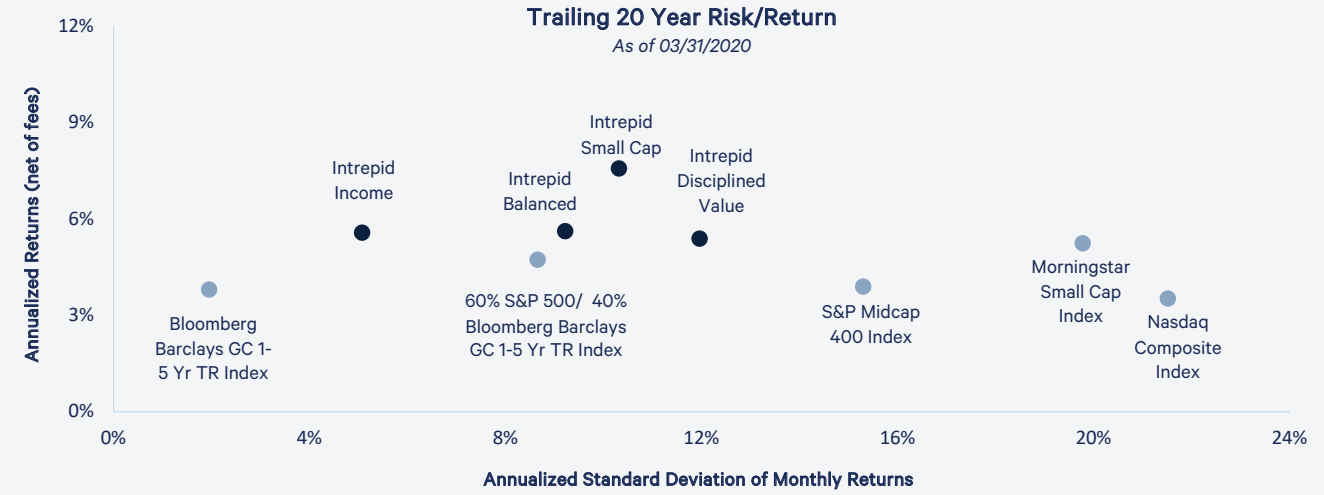
Annualized Performance



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 20-year period ending March 31, 2020. 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 January 1, 2019, the Intrepid Small Cap changed its benchmark from the Russell 2000 Index to the Morningstar Small Cap Index. As of January 1, 2019, the Intrepid Disciplined Value changed its benchmark from the S&P 500 Index to the S&P MidCap 400 Index. As of January 1, 2019, the Intrepid Balanced and Intrepid Income changed their fixed income benchmarks from the ICE BofAML US High Yield Index to the Bloomberg Barclays Gov/Credit 1-5 Year TR Index. The benchmarks for the Intrepid Small Cap and the Intrepid Disciplined Value have not been changed retroactively. The benchmarks for the Intrepid Balanced and the Intrepid Income have been changed retroactively.

INTREPID CAPITAL

Risk Adjusted Return



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INTREPID CAPITAL