Intrepid Capital Management

- Founded in 1995 by Forrest and Mark Travis
- Location: Jacksonville Beach, FL
- $550 million AUM
- Independent/bottom-up fundamental research
- Above-average performance with less risk
Why Small Caps?
Deeper Pond = More Opportunities

- 95% of companies over $1 billion have analyst coverage.
- 91% of companies with $1 billion to $500 million in sales have analyst coverage.
- 28% of companies below $500 million in sales have analyst coverage.

Bar chart showing the number of companies and analyst coverage across different sales ranges.
## Russell 2000 vs. Mega Caps

<table>
<thead>
<tr>
<th>Market Cap of Russell 2000</th>
<th>Market Cap of Top 5 Mega Caps</th>
</tr>
</thead>
<tbody>
<tr>
<td>$1.3 Trillion</td>
<td>GE $371 billion</td>
</tr>
<tr>
<td></td>
<td>Exxon Mobil $330 billion</td>
</tr>
<tr>
<td></td>
<td>Microsoft $279 billion</td>
</tr>
<tr>
<td></td>
<td>Citigroup $249 billion</td>
</tr>
<tr>
<td></td>
<td>Wal-Mart $225 billion</td>
</tr>
<tr>
<td></td>
<td><strong>Total $1.5 Trillion</strong></td>
</tr>
</tbody>
</table>
Intrepid Small Cap Philosophy and Guidelines
Intrepid Capital Management
Small Cap Investment Philosophy

1. Buy stocks selling at discounts to their businesses’ underlying intrinsic values.

2. Buy established businesses with excess free cash flows and strong balance sheets.

3. Invest in good businesses – high barriers to entry, market leader, rational management, predictable cash flows, and stable or improving margins and returns.

4. Reduce risk by understanding your business – focus on fundamental analysis.

5. Think independently and avoid investment fads – focus on absolute returns.
Intrepid Capital Management
Small Cap Valuation Guidelines

1. Valuations calculated via discounting cash flows, asset valuations, and transaction multiples

2. Use realistic cash flow, discount rate, and growth rate assumptions in our valuation models.

3. Avoid businesses that cannot be valued with a high degree of confidence.

4. Minimum discount to intrinsic value = 20%

5. Operating catalyst is needed to close valuation gap
Return Opportunity of Buying a Business for 50 cents on the Dollar

<table>
<thead>
<tr>
<th>Price</th>
<th>Value</th>
<th>Return Opportunity</th>
</tr>
</thead>
<tbody>
<tr>
<td>$20</td>
<td>$40</td>
<td>100%</td>
</tr>
</tbody>
</table>

Valuation Gap
Valuation Gap = Margin of Safety
Margin of Safety

“A favorable difference between price on the one hand and appraised value on the other.”

-Benjamin Graham
Business Value and Stock Price

Annualized Return (assuming valuation gap closes)

Year 1: 117%
Year 2: 53%
Year 3: 36%
Year 4: 29%
Year 5: 25%
Closing of the Valuation Gap
Gorman Rupp (GRC)

Business Appraisal Value

Valuation Gap

Stock Price

Bought
10/31/98

Sold
4/18/02
Be Patient

- Small caps are illiquid
Alamo Group
Be Patient

- Small caps are illiquid
- Small caps are volatile
Lufkin Industries
Be Patient

- Small caps are illiquid
- Small caps are volatile
- Small cap market is not efficient – easily influenced by flow of funds.
Communication Systems
Be Patient and Wait for Your Pitch
(Ted Williams Batting Avg.)
What Does a Good Pitch Look Like?

It’s simple…

Good Business at a Good Price
Example of a Good Pitch
Good Business at a Good Price: Grolsch

**Good Business**
- Market Leader
- Competitive Advantages
- High Margins and Returns
- Consistent Revenues and Cash Flows
- High Free Cash Flow
- Growth Without Leverage
- Pricing Power

**Good Price**
- Selling at Discount to Calculated Value
- Selling at Discount to Transaction Valuations
- High Free Cash Flow Yield
- Above Average Dividend
- Consolidating Industry
Small Caps Now?

Be careful…and be very, very selective.
Current Small Cap Market

RTY  611.08Y as of close 1/21

Line Chart  RTY Index

Range 12/31/99 - 1/21/05  Period Daily  Base Currency: USD
Upper Chart: 3 Line Chart  Moving Averages
Lower Chart: N No additional graph(s)  Moving Average

Close/USD
Last  611.08
High 12/28/04  654.67
Average  491.03
Low 10/09/02  327.04
### Russell 2000

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>2004 Top Performers</th>
</tr>
</thead>
<tbody>
<tr>
<td>P/E 66x</td>
<td>Alloy Inc +79%</td>
</tr>
<tr>
<td>P/B 2.3x</td>
<td>Genelabs +69%</td>
</tr>
<tr>
<td>Div % 1.2%</td>
<td>Circle Group +68%</td>
</tr>
<tr>
<td></td>
<td>CMGI +67%</td>
</tr>
<tr>
<td></td>
<td>Nanogen +63%</td>
</tr>
</tbody>
</table>
## Characteristics of Top Performers

<table>
<thead>
<tr>
<th>Company</th>
<th>Mkt Cap</th>
<th>EBIT</th>
<th>Free Cash Flow</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alloy Inc</td>
<td>$305 mil</td>
<td>-$18 mil</td>
<td>-$54 mil</td>
</tr>
<tr>
<td>Genelabs</td>
<td>$90 mil</td>
<td>-$21 mil</td>
<td>-$20 mil</td>
</tr>
<tr>
<td>Circle Grp</td>
<td>$46 mil</td>
<td>-$5 mil</td>
<td>-$1.3 mil</td>
</tr>
<tr>
<td>CMGI</td>
<td>$886 mil</td>
<td>-9 mil</td>
<td>-$25 mil</td>
</tr>
<tr>
<td>Nanogen</td>
<td>$241 mil</td>
<td>-31 mil</td>
<td>-26 mil</td>
</tr>
</tbody>
</table>
A Few Operating Risks
Alloy Inc

• Negative free cash flow
• Financial flexibility – debt accumulation
• Volatile advertising revenues
• Seasonality of merchandise sales
• No barrier to entry
• Ability to attract new and repeat visitors to web site
• Converting viewers into customers
• Merchandise returns
• Uncertain marketing initiatives
• Generation Y fashion and lifestyle trends
• Reliance on outsourcing (software, fulfillment center, content providers, etc)
• No switching costs for customer
• Inventory obsolescence
• Internet tax
• Retail demand in general
Intrepid Small Cap Performance
Intrepid Capital vs. Market
5-Year Annualized Return*
December 31, 2004

Intrepid Small Cap: 16.5%
Russell 2000: 6.6%
S&P 500: -2.3%
NASDAQ: -11.8%

* Past performance is no guarantee of future results. Intrepid composite returns are presented gross of investment advisory fees and all returns are presented annualized for the five year period ended December 31, 2004.
*Past performance is no guarantee of future results. Intrepid composite returns are presented gross of investment advisory fees and all returns are presented annualized for the five year period ended December 31, 2004. Risk is the annualized monthly standard deviation.
Questions?