AEGIS Value Fund

Portfolio Manager's Letter
First Half Ended June 30, 2020

July 23, 2020

Table 1: Performance of the Aegis Value Fund as of June 30, 2020

		Annualized				
	Six Month	One Year	Three Year	Five Year	Ten Year	Since Inception 5/15/98
Aegis Value Fund (AVALX)	-9.77%	0.55%	4.56%	6.87%	8.27%	8.82%
S&P Sm. Cap 600 Pure Value Index ^	-32.47%	-23.74%	-9.36%	-4.70%	5.78%	N/A
Morningstar Percentile Ranking *		1	1	1	23	
Funds in Small Value Category		421	413	406	352	

** Morningstar Percentile Ranking is based on total return. ^Available performance data for the S&P SmallCap 600 Pure Value Index prior to the December 16, 2005 inception date of this Index cannot be shown as display of pre-inception Index performance data is not permitted. Performance data quoted represents past performance and does not guarantee future results. Current performance may be lower or higher than the performance data quoted. The investment return and principal value will fluctuate so that upon redemption, an investor's shares may be worth more or less than their original cost. For performance data current to the most recent month end, please call us at 800-528-3780 or visit our website at www.aegisfunds.com. The Fund has an annualized gross expense ratio of 1.63% and a net annualized expense ratio, after fee waiver and/or expense reimbursement and management fee recoupment, of 1.50%. Under the waiver, the Advisor has contractually agreed to limit certain fees and/or reimburse certain of the Fund's expenses through 4/30/2021.*

Dear Aegis Investors:

The Aegis Value Fund declined 9.77 percent in the first six months of 2020, significantly outperforming its primary benchmark, the small-cap, deep-value oriented SmallCap 600 Pure Value Index, which plunged by 32.47 percent. Within Morningstar's small-cap value universe, the Fund placed in the 4th performance percentile for the first half of the 2020 and in the top one percentile over each of the last one, three, and five years.

2020 First Half Review

Small cap value stocks as a whole struggled during the first six months of the year, with the broad-based Russell 2000 Value Index of small-cap value equities declining by 23.50 percent. Large-caps were again a winner, with the S&P 500 Index declining by a mere 3.08 percent during the period. The S&Ps slight first half decline masked a period of historic turbulence which witnessed three of the twenty largest daily percentage declines and two of the largest daily percentage increases in S&P records going back nearly 100 years.

Rarely in the course of human history has an economy with such high levels of indebtedness been impacted by such a rapidly unfolding and financially devastating event. The economic dislocations caused so far by Covid-19 have been immense as consumer preferences dramatically shifted amid unprecedented government interventions and social restrictions in the wake of the global pandemic. In America alone, more than 30 million jobs were lost, sending the unemployment rate to a level rivaled only by the Great Depression as a wide variety of industries reliant on social contact essentially came to a complete halt, with impacts felt immediately across a broad assortment of industries. As the world descended into quarantine, global oil demand dropped by a massive 30 percent— nearly 30 million barrels per day— sending oil prices plunging and wreaking havoc on the already beleaguered global energy industry. The month of March brought a massive market nose-dive amid margin calls and forced liquidations, sending stocks plummeting at panic-driven rates even faster than those seen during 2008's Global Financial Crisis amid fears of an enormous coming wave of defaults and bankruptcies. When the market put in a bottom on March 23rd, the S&P 500 Index had declined 30.4 percent year-to-date, while the Russell 2000 Value Index had delivered an even more dramatic 44.2 percent year-to-date plunge.

Given the market plunge, it wasn't too surprising to see the US Federal Reserve announce a massive barrage of new monetary stimulus programs on March 23 in an effort to provide the thirsty capital markets with the liquidity required to prop up lending to the wide variety of industries impacted by the Coronavirus. These new programs extended the assets that the Fed would purchase, even including corporate bonds for the first time. Since early March, these and other Federal Reserve programs have injected a previously unimaginable $3 trillion of additional liquidity into the economy. These asset purchases increased the Fed balance sheet by a massive 70 percent in less than 10 weeks. Not to be outdone, Congress passed a historically large set of fiscal spending programs totaling in excess of $2.5 trillion, primarily in income support payments targeted at entities impacted by Coronavirus. According to analysis by GaveKal Data, the

extraordinary fiscal response to the coronavirus to-date in today's dollars is already reportedly 20 times the level of the Marshall Plan and 5.5 times that of FDR's New Deal. The unprecedented rate of combined fiscal and monetary stimulus pushed the S&P up 39.3 percent from its March 23rd low through the end of the second quarter, delivering the best quarterly performance for the S&P in more than 20 years.

We exited parts of the portfolio quite early as Covid appeared on the scene

Early in the first half of 2020, as the Pandemic was emerging, we liquidated several holdings judged likely to be exposed, selling most of our stake in aircraft leasing company Fly Leasing, and fully exiting our position in Aercap Holdings. We also sold our holdings in railcar manufacturer Greenbriar Industries and construction contractor Tutor Perini. Additionally, we liquidated our shares in homebuilder Taylor Morrison Homes, retailer Cititrends, and most of our position in apparel manufacturer Delta Apparel. In each case, these early liquidations of holdings that we believed likely to be impacted raised cash and prevented deeper Covid-related losses in the first quarter as markets rapidly deteriorated. Later, as markets appeared to bottom and the pace of Covid's progression became more determinable, the Fund reversed course, rebuilding a stake in Fly Leasing after a significant decline and additionally reestablishing an investment in Delta Apparel after Delta shares extended the turn-down under renewed selling pressure in June amid the company's ejection from the Russell 2000 Index.

We should have sold the energy stocks when we sold the others…

Unfortunately, at the time of these earlier sales, we elected to retain the lion's share of our exposure to the energy sector. The Fund had entered 2020 with nearly a quarter of our assets invested in a multitude of energy stocks, many of which we viewed as beaten down and significantly undervalued. We had been optimistic that oil prices were on the rise following America's new trade deal with China, which had the potential to stoke the global economy and fire-up oil demand. On top of the improving global-economic backdrop, the increased possibility for conflict in the Middle East following the killing of Iran's General Suleimani suggested the potential for significantly constrained oil supply, resulting in one of the strongest oil market outlooks in years. Unfortunately, the environment shifted within a matter of days as Covid spread, and many began quarantining themselves at home, leaving energy investments declining precipitously amid a search for bids as oil prices entered a nose-dive. The plunge only steepened after Saudi Arabia surprisingly reacted to the decreased demand by *increasing* production levels and flooding an already oversaturated global market with crude oil. By the end of March, WTI oil had lost 66 percent of its value at the start of the year. Fortunately, several of our energy investments experienced a partial rebound as mid-year approached after OPEC and Russia finally agreed to restrain their production output. The rebound provided us with the opportunity to exit a few of our energy holdings facing worrisome debt repayment obligations that we feared might prove challenging should the Covid-driven low oil-price environment persist for some time.

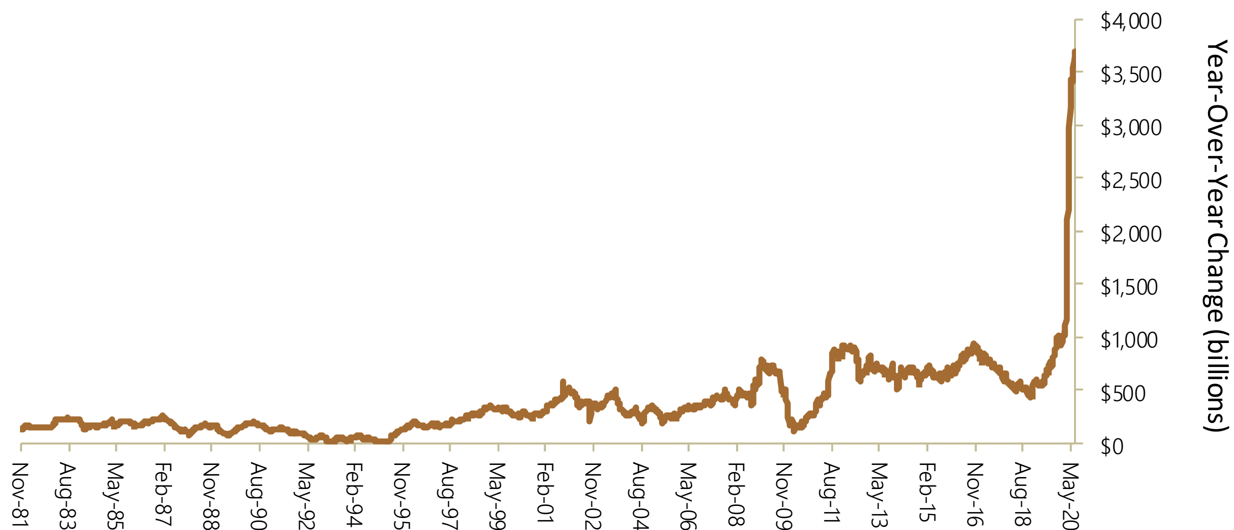
Thankfully, we managed to exit our largest energy investment at a nice profit

Our largest energy holding, Canadian mud-mat provider Strad, Inc., was sold to its management team at a significant premium in late April in a deal that was struck and announced before the market's collapse. It was by far the Fund's largest position exit in the first half. The completion of the deal, which had appeared to be in jeopardy as markets froze, helped generate strong Fund returns in April and drove Fund cash levels nearly ten percentage points higher. While Strad gains certainly helped offset a portion of our other losses in the energy sector, energy sector investments overall cost the Fund a difficult 14 percentage points of performance in the first half of 2020. Despite the disappointing turn of events, we realize that the sector today trades at quite distressed levels. Consequently, we continue to monitor the landscape for energy-related investments with durable balance sheets and attractive risk/reward ratios. Most recently we purchased a position in seismic engineering firm Geospace Technologies as shares in the debt-free, asset rich company were discarded in the second quarter after this company was also purged in June's Russell 2000 Index reshuffle. At the end of June, the Fund held 6.3 percent of its assets in energy-related equities.

And we found a worthy replacement

Our largest addition in the first half of 2020 was Kenmare Resources, an Ireland-based natural resource company which owns and operates the world-class Moma Titanium Minerals Mine, located on the northeast coast of Mozambique. The $270 million market-cap company is a major producer of ilmenite, a titanium dioxide-rich feedstock primarily used in the manufacture of pigments and paints, supplying approximately seven percent of the world's titanium dioxide requirements. The company also produces zircon, a feedstock used in the manufacture of ceramics. Kenmare exited the year with $80 million of cash and held only $61 million of debt on the balance sheet, generating $93 million of EBITDA in 2019. The company, trading at just 30 percent of its $890 million book value, has been under stress after Covid struck the country just as the company was in the process of embarking on a critical $110 million reconfiguration project to transport a portion of its massive sand-mining dredging equipment out of an area where reserves have been depleted and into a new higher-grade region. While we realize that a financially costly project delay is a risk, we believe that concerns around the fully funded project are overly discounted in Kenmare's price today. Furthermore, once the project is complete, which is estimated by year-end, annual maintenance capex should drop into the $25 million range and ilmenite production is expected to increase by nearly 50 percent, dropping production costs into the industry's competitive top quartile. We estimate Kenmare should generate approximately $150 million in EBITDA in 2021 at today's ilmenite pricing levels. Furthermore, the mine has multiple decades of economic life ahead of it, with minimal future equipment moves required. Kenmare represented 2.65 percent of Fund assets at mid-year.

Figure 1: Year-Over-Year Change in M2 Money Supply



Source: Federal Reserve Bank of St. Louis (Data from 11/02/1981 to 07/06/2020)

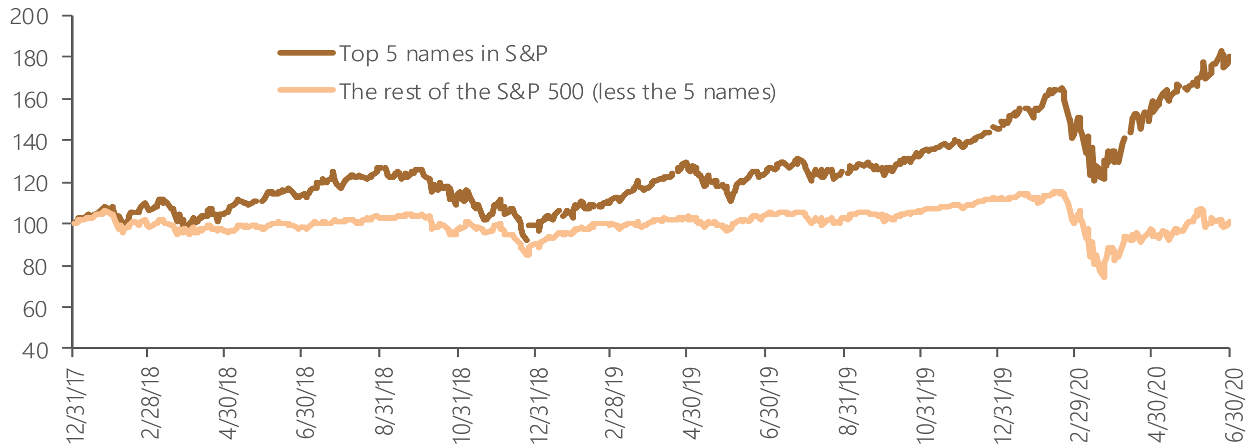
Our precious metals mining investments were the star performers in 2020's first-half market drama

The Fund entered 2020 with holdings in nine precious metals and mining companies. We calculate that our precious metals mining positions, aggregating to just 26 percent of Fund assets as the year began, were responsible for contributing an estimated 14.4 percentage points to total Fund performance in the first half. Clearly, this sleeve of the Fund's portfolio materially outperformed the conventionally followed Market Vectors Junior Gold Mining Index, which gained 16.5 percent in the half, and gold itself, which gained 17.4 percent over the period. The strong performance of the Fund's precious metals mining positions drove the Fund's first half outperformance. While precious metals mining equities sold-off along with the rest of the market as investors raced for liquidity in March, these investments rebounded and soared in the second quarter as the Federal Reserve stepped in with its unprecedented monetary stimulus efforts.

Despite the impressive 2020 performance to-date, we continue to believe our precious metals equities, now at 40 percent of Fund assets, have further to run. Most mining companies have been able to remain operationally effective in an environment of social distancing, and many are also now benefitting from cheaper energy costs and higher precious metals prices. Over the last several years, the gold mining industry has been one of the few that has actually been paying down debt in recent years. Mining balance sheets today are generally in good shape, with debt-to-capital ratios amongst the lowest in the market. Given the rapid rise in the gold price, the miners still remain attractively valued when measured against future cash flows or reserves presuming $1,800 gold, even after recent equity gains. The mining stocks in our portfolio typically trade at low valuations of three-to-five times our projected future-year cash flow, a huge discount to the valuations projected for the S&P 500. Furthermore, the gold miners have the clear potential to surge significantly higher should gold prices continue their Fed-induced surge.

Fundamentals are certainly looking more favorable for gold pricing. In response to the Coronavirus, the Fed has been engaging in a dramatic money-printing expansion of its already bloated balance sheet, adding liquidity at one of the most rapid rates on record in an all-out effort to support asset values, stabilize banks and provide a lifeline to overly levered financial institutions that might otherwise fail. As a result of the money printing, US monetary growth (M2) (see Figure 1) has been expanding in the first half of 2020 at a breathtaking 40 percent clip, a pace more than six times faster than in 2019 and at a rate materially faster than other industrialized nations. Furthermore, the Fed's money printing monetization efforts are increasingly being used to support massive Federal Government deficit spending, which has gone into overdrive in 2020, resulting in a projected spending deficit of close to $4 trillion. Increasingly, this Federal spending is now of the "helicopter money" variety in which individuals and entities viewed to be victims of coronavirus are receiving direct income support. The spending levels have been so profligate and carelessly rushed that millions of unemployed Americans are now purportedly receiving aggregate federal and state unemployment benefits that exceed their previous wages. Many populist politicians are now openly arguing for a universal basic income to be funded by money printing. While these so-called Modern Monetary Theory proponents suggests that money printing to support helicopter money is a productive policy, history has made clear time and time again that such policy is an abject failure,

Figure 2: Cumulative Performance of top 5 names in S&P 500 Vs the rest of the S&P 500 (less the 5 names)



Source: Bloomberg (Data from 01/01/2018 to 06/30/2020)

generally leading to the destruction of the currency and a disaster for the economy. As government debt levels rise relative to the size of the economy, the likelihood that debt can be outgrown or reined-in through higher tax rates drops, leaving default or monetization as the only real long-term options. Historically, monetization has been far more prevalent than default given its political expediency. While timing is never easy to predict, with government debt-to-GDP near all-time high levels, we suspect the growing temptation for monetary mischief increases the potential for serious inflation. Under such a scenario of accelerating inflation, the dollar has the possibility of rapidly losing its reputation as a good store of value with gold having the potential to be a big beneficiary of flight-to-safety capital flows.

<u>The Aegis portfolio is generally well situated in stocks with robust balance sheets and strong upside potential</u>

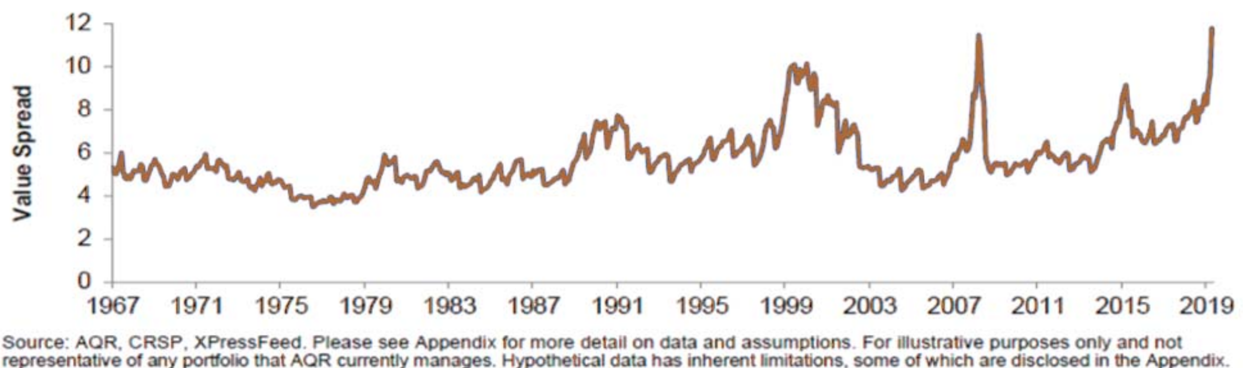
Outside of precious metals, the Fund continues to hold a variety of special situation stocks judged to be undervalued. These include approximately 7.5 percent held by the Fund at mid-year in pulp/paper/lumber stocks, including Mercer International, Resolute Forest Products, and Conifex. Fundamentals in this segment have been on the upswing as lumber pricing soared by nearly 70 percent in recent months, although weaker pulp and paper prices continue to weigh on sentiment. At mid-year, the Fund continued to hold a 6.4 percent stake in Alaska Communications, one of the last remaining independent telecommunications companies in the rapidly consolidating industry. Despite recent gains, Alaska shares trade well beneath the value of the company's Alaskan fiber network replacement cost. In the industrial materials segment, the Fund recently increased its significant stake in Amerigo Resources, a Chilean copper producer, as copper prices fell just as the company was struggling with the operational impact from a 50-year drought last year. Fortunately, there has been more rain in the region this year, and copper prices have recently recovered to two-year highs. While Amerigo's price drop cost the Fund about 2.1 percentage points of performance in the first half, we are optimistic that the Fund's 4.8 percent mid-year position could more than double if processing conditions at Amerigo's plant normalize back to pre-drought levels.

<u>The Fed has distorted values of the tech-heavy S&P 500 and dislocated share prices from reality</u>

In the second quarter, the Federal Reserve's reflationary superstorm stoked a massive speculative resurgence in conventional large-cap equities. At the epicenter of this speculative behavior has been the technology stocks perched at the top of the S&P 500 Index. As can be seen in Figure 2, the five largest stocks in the S&P 500, now comprising one-fifth of the value of the entire Index, have soared 81 percent since the start of 2018. Without these five stocks, the S&P 500 would have essentially traded flat over the last 2 ½ years, according to Bloomberg. These stocks are Apple ($1.7 T mkt-cap/30x trailing EPS/3.7x Sales), Microsoft ($1.6 trillion/35x trailing EPS/8.2x Sales), Amazon ($1.5 trillion/147x trailing EPS/3.4x sales), Alphabet/Google ($1.0 trillion/31x trailing EPS/4.2x sales) and Facebook ($680 billion market cap/33x trailing EPS/5.8x sales). These nosebleed high valuations should speak for themselves, particularly given that the five together grew aggregate revenue by only 12.2 percent last year and two of the five failed to grow profits. The economic backdrop in 2020 should prove to be far more challenging. Furthermore, many of these companies have now become such mammoths that their ability to find ways to continue growing at the above-market rates necessary to justify today's high valuations should prove quite difficult. Clearly, the political climate is not helping either, as Washington has become increasingly antagonistic towards perceived anticompetitive monopolistic behavior by these huge technology firms.

Driven, in part, by the technology sector's massive 37 percent weighting in the S&P 500, the valuation of America's most popular index appears to have become quite inflated, with Goldman Sachs recently reporting the price-to-forward earnings ratio at 23.2 times, putting valuation in the 99th highest percentile historically. Its price-to-sales ratio of

Figure 3: Price-to-Book Spread, Academic Style (December 31, 1967 - March 31, 2020)



2.5 times is reportedly in the 98th highest percentile historically. While massive growth in passive allocations to the S&P 500 Index have helped propel these stocks into the stratosphere in recent years, we anticipate that the many "set it and forget it" passive investors who today own the S&P 500 may not realize that the future is likely to look quite different than the recent past.

But there is an attractive alternative

Fortunately, investors wishing to maintain exposure to equities currently have an attractive alternative to holding the bloated, tech-heavy S&P 500. While the technology stocks and other stocks trading at high valuations have grown even more expensive in recent years, stocks previously trading at low valuations have actually become even cheaper, a trend that has accelerated over the last 12 months. We suspect this growing disparity is the result of the continued trend towards indexing as well as capital flows exiting value managers to chase performance. In a May 2020 paper titled "Is (Systematic) Value Investing Dead?," quantitative investing firm AQR found that the spread of the most cheaply-valued third of the market to the most expensive third of the market had recently blown out to historic levels. As can be seen in Figure 3, AQR found that stocks expensive on price-to-book were 12 times more expensive than those cheap on price-to-book. This compares to a historical median of only being 5.4 times as expensive and was purportedly a 4.5 standard deviation event.

The Aegis Value Fund has been intensely focused on investing within this deeply undervalued universe of securities now trading at record discount valuations when compared to the broader market. In fact, in December 2018 (National Bureau of Economic Research, Working Paper 25381, "Characteristics of Mutual Fund Portfolios: Where are the Value Funds"), Aegis was cited as one of the few alternatives in the mutual fund space that has truly remained focused on this deep value segment of the market. As can be seen in Figure 4, stocks in the Aegis Value Fund trade at just 61 percent of book value, putting the Fund's valuation near twenty-two year lows, and at a significant discount to the S&P 500 Index, which now trades at 355 percent of book value. Historically, whenever the Fund has been near these valuation levels, the probability of competitive forward returns has been quite high.

Not surprisingly, as the Covid crisis struck the market in March, the number of stocks on our discount-to-book watchlist blew out to levels not seen since the Global Financial Crisis (see Figure 5). Many of these investment candidates have been fundamentally impacted by the Coronavirus, and more than a few look financially weak and prone to eventually fail. We have been carefully sifting through the list, working diligently to find stocks with good risk/reward ratios and robust balance sheets that can survive the slowdown and deliver competitive returns as the world adjusts to the Coronavirus shock. It is not likely to be easy to maintain solid investment footing amid the tumultuous and indeterminate terrain increasingly determined by the whim of the Federal Reserve bankers. The forces of populist politics are also clearly making the investment terrain more treacherous. Furthermore, the changing pace of the viral pandemic as well as the potential emergence of treatments and vaccines are additional wildcards that have the potential to rapidly shift the financial setting, leaving one at severe risk of being caught flat-footed. Determining a prudent path across the investment terrain is never an easy process, but these days it can be particularly daunting.

Please know that we are continuing to work diligently to mitigate these emerging risks and deliver strong re-

Figure 4: Aegis Value Fund, and S&P 500 Index Historical Price-to-Book Ratio

Source: Aegis Financial Corp and Bloomberg (Data from 9/30/1998 to 6/30/2020)

Figure 5: Number of Stocks Selling Below Tangible Book Value (Market Cap. Greater Than $70 Mil)

Source: U.S. public equity market statistics from Stock Investor Pro (Data from 4/30/2002 to 06/30/2020)

turns. Employees and our families have in excess of $25 million invested in the Fund, and we are watching over the portfolio carefully. Should you have any questions, our shareholder representatives are available at (800) 528-3780. You are also welcome to call me personally at (571) 250-0051. I wish you good health and a strong constitution during these unusual and disconcerting times.

Sincerely,

Scott L. Barbee
Portfolio Manager
Aegis Value Fund

Please see the following page for important information.

The Aegis Value Fund is offered by prospectus only. Investors should carefully consider the investment objectives, risks, charges and expenses of the fund. The Statutory and Summary Prospectuses contain this and other information about the Fund and should be read carefully before investing. To obtain a copy of the Fund's Prospectus please call 1- 800-528-3780 or visit our website www.aegisfunds.com, where an on-line version is available.

Mutual fund investing involves risk. Principal loss is possible. Investments in foreign securities involve greater volatility and political, economic and currency risks and differences in accounting methods. Investments in smaller and mid-cap companies involve additional risks such as limited liquidity and greater volatility. Investment concentration in a particular sector involves risk of greater volatility and principal loss. Value stocks may fall out of favor with investors and underperform growth stocks during given periods.

The Fund's top ten holdings are Equinox Gold Corp., Minera Alamos Inc., Dundee Precious Metals Inc., Alaska Communications Systems Group Inc., Amerigo Resources Ltd., Geodrill Ltd., Roxgold Inc., Mercer International Inc., Alio Gold Inc., and Ezcorp Inc. As of June 30, 2020, the stocks represent 12.2%, 8.0%, 6.6%, 6.3%, 4.8%, 4.7%, 4.5%, 3.7%, 3.7%, and 3.7%, of total Fund assets respectively. Fund holdings are subject to change and should not be considered a recommendation to buy or sell a security. Current and future portfolio holdings are subject to risk.

Morningstar Rankings represent a fund's total-return percentile rank relative to all funds that have the same Morningstar Category. The highest percentile rank is 1 and the lowest is 100. It is based on Morningstar total return, which includes both income and capital gains or losses and is not adjusted for sales charges or redemption fees.

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Price to Book: A ratio used to compare a stock's market value to its book value. It is calculated by dividing the current closing price of the stock by the latest quarter's book value per share. Book Value: A company's common stock equity as it appears on a balance sheet. S&P 500 Index: An index of 500 stocks chosen for market size, liquidity and industry grouping, among other factors. The S&P 500 is designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe. Russell 2000 Value Index: measures the performance of small-cap value segment of the U.S. equity universe. It includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. Cash Flow: A revenue or expense stream that changes a cash account over a given period. MVIS Global Junior Gold Miners Index: The modified market cap-weighted index tracks the performance of the most liquid junior companies in the global gold and silver mining industry. Market capitalization: The total dollar market value of a company's outstanding shares. Debt-to-GDP ratio: the ratio between a country's government debt and its gross domestic product (GDP). WTI: West Texas Intermediate is a grade of crude oil used as a benchmark in oil pricing. EBITDA: Earnings before interest, taxes, depreciation and amortization expenses. The S&P SmallCap 600 Pure Value Index: An index maintained and selected by the S&P Index Committee. It contains companies with market caps in the range of US$ 300 million up to US$1.4 billion and with public floats of at least 50% and with strong value characteristics. Price-to-Sales: a valuation ratio that compares a company's stock price to its revenues. It is an indicator of the value placed on each dollar of a company's sales or revenues. Forward price to earnings (forward P/E): a measure of the price-to-earnings (P/E) ratio using forecasted earnings for the P/E calculation. M2: is a broader classification of money than M1. Economists use M2 when looking to quantify the amount of money in circulation and trying to explain different economic monetary conditions. The Russell 2000 Index: measures the performance of the small-cap segment of the U.S. equity universe and is constructed to provide a comprehensive and unbiased small-cap barometer. The Russell 2000 Index is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership. OPEC: The Organization of Petroleum Exporting Countries is a group consisting of 12 of the world's major oil-exporting nations.

Diversification does not guarantee a profit or protect from loss in a declining market.

An investment cannot be made directly in an index.

Earnings growth is not representative of the Fund's future performance.

Opinions expressed are subject to change at any time, are not guaranteed and should not be considered investment advice.

References to other investment products should not be interpreted as an offer of these securities.

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