



Dear Fellow Shareholders,

We are pleased to provide you with the Third Avenue Value Fund's (the "Fund") report for the quarter ended January 31, 2016.

"What happened to Value investing?"

This was somewhat a rhetorical question posed to us as portfolio managers this quarter as we met with a long time client, who sees eye to eye with us on the motive and merits of Third Avenue Management's value investment philosophy. We could not help but respond with a riff on the well-known quote by Mark Twain, that "rumors of its death have been greatly exaggerated". Rejoinders aside, we understand the frankness of the concern in the question. As we wrote in our Fiscal Year end letter ninety days ago, Value investing as a style has greatly underperformed momentum driven investment styles over the last several years. As a proxy we look at the outperformance of the Russell 3000 Growth Index vs. the Russell 3000 Value index of 9.22% in 2015, 2.08% per annum for a trailing 5 year period and 1.70% per annum since the market bottom of March 16, 2009. While we can suggest contributing factors to this disparity, such as a Federal Reserve Liquidity "put" supporting more leveraged and lower quality businesses, to a market that has found perceived safety in momentum growth strategies, we cannot argue the fact that Value Investing has faced an extreme and prolonged headwind.

As we are not "macro" forecasters, we cannot divine when these headwinds will cease, and revert, but we firmly believe two things. First, that even though our investment philosophy of creditworthiness, compounding of book value and a patient buy at a discount to our estimate of net asset value may struggle over certain periods of time we believe this to be a superior way to invest over the long term. Second, that it is not "different this time." We have endured similar periods where Value styles were out of favor. We know that these periods can last longer and be of greater duration than we would expect. We have also seen the benefits of owning well capitalized companies with solid business models when metrics such as "clicks," "eyeballs" and now "earnings revisions" lose favor in rapid fashion. Said differently, the current obsession with the "primacy of the income statement," a term defined by Marty Whitman, is not a lasting substitute for a disciplined approach, i.e., the measurement of the value of the earnings ability of a business' assets and liabilities that begins with the balance sheet. Despite the backdrop for value investors in general and a tough 90-day result in performance, we remain excited about the quality of the names owned in our portfolio and the upside returns we see in these investments over our long-term horizon of three to five years. Our feeling is that the market has dramatically oversold many names that detracted from the portfolio in the quarter, and the valuation levels to us feel like a coiled-spring that will revert to the positive. We are taking the opportunity to deploy capital in some of what we believe are the most unduly punished names in the portfolio as well as in new investment opportunities.

Portfolio holdings are subject to change without notice. The following is a list of Third Avenue Value Fund's 10 largest issuers, and the percentage of the total net assets each represented, as of January 31, 2016: Bank Of New York Mellon Corp., 6.29%; Cavco Industries, Inc., 5.94%; Weyerhaeuser Co., 5.07%; Comerica, Inc., 4.80%; CBS Corp., 4.24%; PNC Financial Services Group, Inc., 4.12%; CK Hutchison Holdings Ltd., 3.70%; White Mountains Insurance Group, Ltd., 3.59%; AGCO Corp., 3.43%; Covanta Holding Corp., 3.41%.

In contrast, many companies with top weightings in broad based market indices are dramatically overpriced. Given our high active share which by definition dictates we have a significantly different portfolio than the benchmark, we like the prospects for the Value Fund much more than the indices. Indeed, all three of us added to our holdings in the Value Fund in January.

Fund Performance

The Value Fund underperformed the MSCI World Index by 283 bps in our Fiscal First Quarter (November 1, 2015-January 31, 2016), down 10.8% vs. -7.97%. Our significant weightings in financial holdings and a lack of consumer staple holdings accounted for the largest deltas to the benchmarks, as would likely be expected with the general market weakness.

Some of the top contributors to the Fund during the quarter were Baxalta, NVIDIA, and our new position in Ralph Lauren. We initiated a position in **Baxalta**, a biopharmaceutical company, in the prior quarter. The company was the target of a takeover bid from Shire during this most recent quarter. Under the agreement, Baxalta shareholders will receive \$18.00 in cash and 0.1482 Shire ADS for each Baxalta share. Based on Shire's closing price, this represented a value of \$45.57 per Baxalta share, resulting in an unrealized IRR of 26.0%. We are pleased that another party found Baxalta's assets as interesting as we did. The Fund has owned **NVIDIA** shares since 2012. The company has done a good job building value over the years. Demand for its graphics processing units (GPUs) has grown, driven by growth in gaming along with more computer-intensive applications such as professional graphics, automotive and artificial intelligence. We exited the position during the quarter for valuation reasons, realizing an IRR of 35.4%, and redeployed the proceeds into other investments.

We continue to be confident in the names that detracted from performance, and attribute weak performance to the excessive focus by the market on short-term earnings and disregard for long-term growth prospects of these companies. We believe that companies like Bank of New York Mellon and Comerica, which were among the largest detractors to performance, are poised to benefit as investors shift their focus towards company fundamentals.

Bank of New York Mellon (BK) and **Comerica (CMA)** have been impacted by macro concerns. Both companies would benefit greatly from higher interest rates, but fears of a slowdown in global growth have prompted questions around central banks' conviction to raise rates. This has soured investor interest in banks. BK and CMA felt the pain, each declining close to 20% this past quarter. Current operations do not support the recent declines. BK's earnings have been impressive over the past few quarters. Management is finally achieving meaningful operating leverage as costs have been contained. Despite the tangible progress, investors sold indiscriminately. We detailed our thesis on CMA in the last letter, and it has not changed. CMA reported earnings a few weeks ago and charge-offs in its highly scrutinized energy portfolio remain modest.

¹ The Fund's Institutional share class one year, five year and ten year average annual returns for the period ended January 31, 2016 were -12.25%, 0.97% and 3.17%, respectively. The Fund's Institutional share class one year, five year and ten year average annual returns for the period ended December 31, 2015 were -8.37%, 2.92% and 10.87%, respectively. Past performance is no guarantee of future results; returns include reinvestment of all distributions. The above represents past performance and current performance may be lower or higher than performance quoted above. Investment return and principal value fluctuate so that an investor's shares, when redeemed, may be worth more or less than the original cost. The Fund's total operating expense ratio, gross of any fee waivers or expense reimbursements, was 1.07%, as of October 31, 2015. Risks that could negatively impact returns include: fluctuations in currencies versus the US dollar, political/social/economic instability in foreign countries where Fund invests, lack of diversification, volatility associated with investing in small-cap securities, and adverse general market conditions. Prospectuses contain more complete information on management fees, distribution charges, and other expenses. Please read the Prospectus carefully before investing or sending money. For current Fund performance or a copy of the Prospectus please visit our website: www.thirdave.com or call 800-443-1021. M.J. Whitman LLC, Distributor. Member FINRA/SIPC.

Investors are forgetting that the energy book accounts for only 7% of loans and appears adequately reserved. We have stress-tested CMA's book many different ways and there are sparse scenarios where book value doesn't grow this year. Yet, CMA is now trading below tangible book value which makes little sense to us.

The three biggest losers last quarter were Cavco Industries, Comerica and Bank of New York Mellon. Cavco's decline is misleading as it has more to do with the calendar than operations. It has been a stellar performer over the past year, but was down in 1Q after a rapid rise at the end of last quarter. It recently reported earnings and the company is executing at a high level. Cavco maintains a strong net cash balance sheet and is growing sales and margins. With the manufactured home industry growing at high-single rates, Cavco is well positioned to take advantage.

New Positions

Ralph Lauren

Ralph Lauren (RL) is one of the crown jewels in retail. It is well capitalized with a net cash balance sheet and has historically earned a premium valuation. Given its compounding history, the premium valuation is justified. Due to short-term factors, the stock price has dropped over 40% from recent highs and now trades at absolute valuation levels last seen shortly after the financial crisis. It is a rare opportunity to buy a well-managed, well capitalized, owner-operator at an attractive price.

Although retail has historically been an area that Third Avenue Management (TAM) shies away from, RL is an exception. It meets our three pillar criteria as it is a credit worthy compounder trading at a discount to NAV. Over the past five and ten year periods, RL has grown book value (including dividends) 11% and 13%, respectively. It is a blue-chip asset with a more stable operating history than most players in the space. For example, sales only declined marginally in 2009, following the financial crisis. Although it could be categorized as a retail company, considering that roughly half of RL's sales are wholesale/licensing and its brand strength, it's more comparable to Nike than a typical retailer.

Besides macro concerns about an economic slowdown, company specific issues have soured RL's near-term outlook. We have assessed these risks and feel it is a classic case of investor short-termism. First, the strong USD has impacted sales. One-third of RL's sales are from outside the US, so currency translation has pinched sales and margins. Also, 20% of RL's sales come from foreign tourists shopping in the US. Those sales have been pinched as tourists are choosing to stay home as the costs of traveling to the US have risen with the stronger USD. RL continues to experience double digit same-store sales growth in flagship stores overseas, so it does not appear to be a brand problem.

Another major factor impacting RL is the implementation of its Global Reorganization Plan (GRP). Management is investing for growth by creating a brand based operating structure, implementing a global SAP system (US completed and Europe in-process) and expanding its global footprint and internet presence. All initiatives make sense in the long-run, but have been costly in the short-run. The slower than expected sales and additional costs have pressured margins, creating investor angst. Management projects cost savings of \$100 million per year once the initiatives are completed later this year. Investors are struggling to see through the near-term noise which has created a worst-case scenario valuation.

A final catalyst is the hiring of CEO Stephan Larsson. Larsson is a young, ambitious retail executive who had highly successful stints at H&M and Old Navy. With Ralph Lauren now 75 years old, Larsson's hiring makes strategic sense. Lauren will remain a creative force at the company, but Larsson's expertise in understanding the fast fashion landscape (H&M) and turnarounds (Old Navy) might be the shot in the arm RL needs.

In summary, we feel that the favorable long-term prospects heavily outweigh the near-term concerns embedded in RL's current valuation. Higher sales, a weaker USD and lower GRP costs can all contribute to a brighter outlook for RL's operations. With the additional benefit of a highly motivated new CEO, the pace of change has probably been accelerated.

Harman

We initiated a position in Harman International, a leading provider of in-car software solutions for infotainment, high-end audio and telematics with annual revenues of approximately \$7 billion. Harman may be better known to many of you through their brand named audio divisions serving automotive, high end consumer and professional markets under the Harman/Kardon, JBL, Mark Levinson and Bang & Olufsen brands.

We have known Harman for many years, and have taken advantage of market fears and misunderstanding about Harman as an automotive exposed stock to initiate a position. Harman has sold off from almost \$150 per share in May 2015, to the current price in the mid-\$70's as the Street has grown concerned about the current auto cycle approaching 'peak' levels. Investors, based on a primacy of the income statement mentality, have sold the stock off to approximately 10x FY2017 (June) EPS, in line with most auto suppliers. However, despite roughly 70% of Harman's revenue coming from automobiles, we think Harman can continue to grow revenues and compound earnings at double digit rates for at least the next several years. This revenue growth, in our opinion, is more secular than cyclical, as automakers accelerate both the penetration and functionality of infotainment and telematics across their vehicle fleet. Harman has historically served the higher end luxury automakers—BMW, Mercedes and VW—who were early adopters due to the price point of more luxury vehicles. However, Harman has developed a scalable platform that will accelerate adoption through the mid and low range of vehicle fleets. Indeed, Harman has won significant business with GM, Fiat Chrysler, Subaru, Hyundai and even Geely in China. We further believe, as has been stated by Harman and demonstrated with win rates, that Harman's systems will be an enabler of Apple, Google and Baidu automotive products and not a competitive offering, as Harman's software will be the platform to access these offerings, while providing the safety and security features necessary in an automotive environment. Indeed, it is our speculation that at 'only' a \$5 billion market cap, Harman would make a nice acquisition for any of these larger players.

Beyond infotainment, Harman has increased its offerings in its home audio lineup, and is now entering high end earphone markets. Even more exciting is Harman's new Connected Car division, which incorporates its recent Symphony Telca and Red Bend acquisitions, which enable 'over-the-air' software updates for any connected device, whether a car, or perhaps a turbine or a dishwasher, and thus is an emerging leader in the nascent 'Internet-of-things' space. This division now has over \$735 million in revenues and 15% EBITDA margins, with mid-teens revenue growth and 20% EBITDA margin targets.

We believe Harman is a compelling addition to the portfolio as it meets all three tenets of our investing philosophy. From a creditworthiness standpoint, Harman has a strong balance sheet with a 21.5% Debt to Capital Ratio, made up of approximately \$1.0 billion in debt and \$438 million in cash. Harman refinanced its senior debt in 2015 into two tranches, \$390 million due in 2022 at a rate of 2% and \$400 million due in 2025 at 4.15%, providing long-term maturities at low rates. Debt to expected FY16 EBITDA is .74. Harman is returning excess cash to shareholders with a dividend yield of about 2% and has \$463 million remaining on its share repurchase authorization; it is looking to step up repurchases on current share price weakness.

Harman has compounded book value growth over the trailing 5 years at 18.2%, when adding back dividends. More importantly, we see Harman well positioned to continue this growth as it has a \$23 billion backlog, revenue growth estimated at 14% for 2016 and likely double digit over the next few years, and continued margin expansion driven by price mix and sales leverage. At our average purchase cost of \$77, Harman offers over 30% upside to our mid-case NAV of \$100, and as such we look to continue to build the position size opportunistically on market weakness.

Looking Forward

We are investing for the long term with management teams that have an aligned long-term vision and capital allocation strategy. Over time, we believe that strong balance sheets coupled with thoughtful financing and capital allocation will win and create attractive returns for our shareholders. We are taking advantage of the recent volatility in the markets to deploy capital into companies which have the most attractive risk/return profiles. We are also seizing this opportunity personally; the three of us have increased our positions in the Fund over the last quarter.

Finally, Third Avenue has been in the news of late. We refer you to our Management Committee's letter which discusses events regarding the Focused Credit Fund and importantly the capital strength and durability of Third Avenue as a firm.² We also note that since our September sale of the Lehman SIPA claim, the Third Avenue Value Fund has no overlapping positions with the Focused Credit Fund. As a firm, we have developed a reputation of open and honest communications. It is your money and we try to help you understand how it is invested. The by-product of our openness is attracting the right types of investors. We have investors who understand our approach and think long term. We are grateful to have a like-minded investor base. We care very much about the Value Fund because we want to reward our shareholders. In addition, a significant percentage of our wealth is invested in the Fund alongside you.

Sincerely,

The Third Avenue Value Team

Chip Rewey, Lead Portfolio Manager

Yang Lie, Portfolio Manager

Victor Cunningham, Portfolio Manager

²The Third Avenue Management Committee's letter to Shareholders dated December 23, 2015 is available on our website <http://thirdave.com/commentary/a-letter-from-the-management-committee/>

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If you should have any questions, please call 1-800-443-1021, or visit our web site at: www.thirdave.com, for the most recent month-end performance data or a copy of the Funds' prospectus. Current performance results may be lower or higher than performance numbers quoted in certain letters to shareholders.

M.J. Whitman LLC, Distributor. Date of first use of portfolio manager commentary: 2/19/2016

About Third Avenue Management

Third Avenue Management LLC is a New York-based global asset manager that has adhered to a proven value investment philosophy since its founding in 1986. Third Avenue's disciplined approach seeks to maximize long-term, risk-adjusted returns by focusing on corporate financial stability, and price conscious, opportunistic security selection throughout the capital structure.

If you would like further information about Third Avenue Funds, please contact your relationship manager or email clientservice@thirdave.com



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