Annual Advisor's Report For the Year Ended December 31, 2007

Advisor's Report

February 20, 2008

To the Trustees of the Aegis High Yield Fund:

We are pleased to present this Aegis High Yield Fund Advisor's Report, discussing the year ended December 31, 2007. If you are new to our Fund, please feel free to study our website (www.aegisfunds.com) for more detailed information about the high-yield bond market and the Fund's investment approach. We will briefly review the objectives and strategy of the Fund:

The Aegis High Yield Fund seeks to earn consistent total returns that exceed its benchmark index over periods of three to five years, while striving for below-average risk compared to its peers. The Fund's long-term investment strategy is based on its total return objective. We use in-depth fundamental analysis of issuers to identify bonds and build a portfolio with the potential for capital appreciation due to improved company performance, ratings upgrades, or better industry conditions. We seek situations where Wall Street's appraisal of a security's value is more negative than we have determined based upon an independent study of the facts. The bonds purchased for the portfolio are not necessarily the highest-yielding issues in the market. Our goal is to maximize risk-adjusted long-term total return.

You may not be familiar with information about the high-yield bond market. If you feel that you need an introduction to the securities, please read "About High Yield Bonds" located at a tab on our Fund website, which explains some of the history of the market and its structure.

For the year ended December 31, 2007, the Fund posted a total return of 0.74%, versus a total return of 1.87% for its benchmark, the Lehman U.S. Corporate High Yield Index.For the most recent three years, the Fund had an annualized total return of 7.21% versus 5.39% for the benchmark, and from inception at January 1, 2004, the Fund's annualized total return for the four-year period is 6.37% compared to 6.80% for the Lehman Index.*

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* *Returns include reinvestment of dividends and capital gains. 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 of principal value will fluctuate so that upon redemption, an investor's shares may be worth more or less than their original cost. The Fund has an annualized expense ratio of 1.20%. Investors may call 1-800-528-3780 or go to the Fund's website www.aegisfunds.com to obtain performance data current to the most recent month end.*

The weighted average maturity of the Fund portfolio at December 31 was approximately 4.1 years. The duration of the Fund portfolio was 3.40 years, compared to 4.61 years for the Lehman Index. Duration is a measure of the sensitivity of portfolio value to changes in interest rates. The Fund's shorter duration makes it less sensitive to interest rate risk than the Lehman index.

The Fund's net asset value at December 31 was $9.93 per share versus $10.69 a year earlier. Income distributions totaling 73.71 cents per share and net capital gains of 11.89 cents per share were paid during the year. At December 31, the Fund's SEC 30-day annualized yield to maturity was 9.18%.

The Fund's mixed performance for the year was attributable to strong returns in issues such as Calpine and Del Laboratories, almost entirely offset by very disappointing results in the Fund's holdings of housing and financial issues. In addition, the portfolio suffered in the second half of the year from the general decline in prices of risky debt as market psychology turned negative.

Triggered by a decline in the value of subprime mortgage securities, the framework of what we have referred to as "New Finance" began to crumble in recent months. Many of the assumptions used to create, manage, and price complex types of structured debt securities have been shown to be far too optimistic. Eventually, these problems will be fixed and structured finance will be revived in a more robust, creditworthy form.

Unfortunately for the Fund portfolio, the widespread liquidity crunch resulting from the unwinding of New Finance spilled over into all parts of the fixed income markets, and most of the securities held by the Fund have suffered price declines. In a few cases, these declines are related to deteriorating investment fundamentals, but in many cases the lower pricing is simply a function of poor market conditions and recession worries.

As we will discuss on the following pages, the credit cycle has peaked and turned down, and we are now beginning the process of searching for bargain situations in the market. Yield spreads have widened from only 241 basis points in early June to 561 basis points at December 31. Based on the historic spreads in the market, we still have some distance to go until the opportunities can be called truly exceptional (spreads above 900 basis points), but believe that we are approaching a time to increase the Fund's average maturity and duration. This is a process that will take several quarters, but we expect to move in that direction during the remainder of 2008 and into 2009.

Current Bond Market Conditions

As we have done in the past, we will describe in more detail the environment in which the Fund is operating today. Our website material notes that the modern high-yield bond market, which dates from approximately 1980, has been characterized by pronounced multi-year market cycles. We believe that monitoring these market cycles

and adjusting the Fund's portfolio structure to each phase of a particular cycle is a key element of the Fund's performance.

We look at overall high-yield bond market conditions in a framework built from the following factors:

- Economic Conditions
- Credit Quality
- Yields
- Spreads
- Supply and Demand

Economic Conditions

The American economy continued to slow during 2007, ending the year with an anemic 0.6% GDP growth rate during the fourth quarter. For the full year, the economy expanded at a 2.5% rate, an acceptable performance considering that the credit markets suffered a nearly complete shutdown during the second half of the year.

Banks announced significant writeoffs of bad debts and credit derivatives in the third and fourth quarters (exceeding $140 billion), stifling their ability to lend. Bank commercial paper and business loans declined by 9%, or approximately $300 billion, between August and November. This is the biggest quarterly decline ever reported by the Fed. At the same time, the virtual closing of the securitization market did not allow banks to sell off assets to free up capital. Institutions were left with no choice but to curtail their new lending. The latest Fed survey of bank loan officers shows that over half have tightened conditions on mortgage lending, and 70% expect to see deterioration in the quality of their loan portfolios during 2008.

Manufacturing and exports enjoyed a strong year due to the weak dollar, while housing construction and retail sales lagged. Consumer spending was hampered by the decline in home prices, and the negative ''wealth effect'' of lower housing values and shaky securities markets adversely affected public confidence. The American economy in the past year has been like a roaring automobile engine that is slowly losing some power from one cylinder after another. At the moment, high outlays by the federal government (primarily for defense) and the strong export growth of manufacturers are two of the cylinders that are still providing some solid forward momentum.

While there is currently a debate as to whether America can escape a recession this year, the damage in the credit markets has been so severe and future growth is so heavily dependent on credit creation that we think it is inevitable that the economy slips into recession this year. The real question is whether we experience a brief and shallow recession or a more prolonged, severe downturn.

Recent reports have been disappointing by the standards of the past several years. Holiday sales for retailers were the worst in five years, housing starts have fallen close to a 20-year low, and consumer confidence surveys are near recession levels. It is

worrying that even the high-end retailers like Nordstrom's are reporting sluggish results. Auto sales have declined from a typical 17 million unit annual pace to a 15.2 million unit pace in January.

Also in January, the ISM survey of service industries plunged from 53.2 to 44.6. A figure less than 50 indicates that business is contracting from the prior period. The ECRI index of leading indicators, one of the best gauges of future growth, fell from 143.9 in June to 131.1 in January. This is one of its sharpest declines in the past 15 years. Finally, a survey by the Business Council of corporate CEOs showed that 65% felt that economic conditions had worsened in the past six months, and 53% expected conditions to worsen over the next six months.

The Federal Reserve Board has responded vigorously, particularly in recent weeks, with a series of rate cuts bringing the federal funds rate down from 5.25% in July to 3.0% at the end of January. It also appears that the rate may be reduced to 2.5% or less by summer.

These rate reductions will help cushion the decline of economic activity. However, a rapid revival of growth might cause other problems to linger. An issue that is causing concern to bond investors is the stubborn rise of inflation. The gold price has topped $900 while prices of many other industrial and agricultural commodities have been in a huge rally, even as the American economic outlook has softened. Oil prices briefly topped $100 a few weeks ago before correcting to the $86 range, and are still far above the levels of three years ago. We expect some of the inflation indicators to cool as the U.S. slowdown spreads to other parts of the globe, but the outlook for prices is certainly far different from the mild recession of 2001, which was preceded by commodities taking a dive at the first sign of weakening economic growth.

It is clear that the financial excesses of the past several years will be gradually corrected. This complicated process will involve difficult dealings with bad credits, poor liquidity and falling asset values. Unfortunately the process will take some time, very likely hurting growth through 2008 and even into 2009. On the positive side, we expect the economy to rebound going into the next decade and return to several years of very robust growth after this period of adjustment. Long-term demand in America should be very healthy as the large "Generation X" population moves into its prime consuming years, so we expect optimism and prosperity to return over the next few years.

Credit Quality

We have mentioned in the past the long-term decline of credit quality in the corporate bond market. Now that the economy has stumbled, the staying power of corporations will be tested. While most of corporate America is in very good shape, many companies have taken on large debt loads since the last recession and are vulnerable to a prolonged slowdown.

Because the harmful effects of the credit crunch will be felt with a lag, U.S. bond defaults remained almost non-existent as 2007 came to an end, with the 0.88% year-end default rate reported by Moody's dropping further below even the prior year's exceptionally low 1.3% rate. These figures will represent the cyclical trough, as Moody's is now forecasting that the default rate in 2008 will rise to 4.8% by year-end, a level that closely compares to the 4.54% annual average default rate since 1982.

Just in recent weeks there have been several defaults caused by tightening credit conditions, and already this year the $4 billion of new defaults exceeds the total of $3.5 billion of defaulted securities for the full year of 2007.

One of the better leading indicators of default experience is the prevalence of "distressed securities" trading in the market. A distressed bond is defined as a security with a yield more than 1,000 basis points above the comparable Treasury issue. Distressed bonds in mid-2007 represented only about 2% of the overall high-yield market. By the end of January, the distressed segment of the market had skyrocketed to 17% of all U.S. issues. Market studies have shown that distressed securities exhibit as much as a 25% chance of default in the succeeding year. Based on current figures, it appears that the Moody's projection of a 4.8% default rate by the end of 2008 may be a bit conservative. Other analysts have suggested as much as 8-10% default rates.

Some recent media reports have made note of the fact that, based on implied equity valuations of comparable companies, a number of 2006 and 2007 buyout deals may be "underwater". In these cases, the comparables seem to indicate that current asset values in the deals might be less than the related corporate debts. An underwater deal, if in fact assets are less than liabilities, becomes very risky for bondholders because the equity investors may believe that they no longer have any value in the company and are therefore more likely to walk away than support the operation. An underwater deal might eventually revive through improved cash flows and higher asset values, and it is possible that it may be temporarily discounted in the market simply due to harsh credit conditions, but the large buyouts of 2006 and 2007 are worrisome. They represent more than $300 billion of liabilities, and could be a source of additional problems for the market.

Future credit quality will depend, as it always does, on economic performance and corporate profitability. A mild recession and slight decline in corporate profits will cause credit quality to weaken during 2008 but a deep recession and plunge in corporate profits will cause much more severe damage to the market and to investor psychology. Concerns about the outlook for credit quality are growing almost by the day.

Yields

The Lehman High-Yield Index yield jumped from 8.10% to 9.64% during the second half of 2007 as investors fled corporate credit risk and demanded higher yields. With safety becoming the focus of bondholders, Treasury note yields fell dramatically from

5.02% to 4.03%. Treasury note yields have continued to slide during 2008 and now are approaching the lows reached in 2003 as the economy was recovering from the last recession. Meanwhile, the Lehman High-Yield Index is moving in the opposite direction as investors continue to shun risk, and is yielding 10.5% as of mid-February.

Interest rate volatility has sharply increased, and recent months have seen several of the largest swings in corporate bond yields in the past twenty years. The MOVE index, which forecasts the future annual volatility of Treasury yields, has jumped from only 52 basis points last May to 145 basis points at year-end and peaked at 179 basis points in January.

In recent weeks, the Fed has picked up the pace of interest rate cuts, and the result is a much steeper yield curve. During the early months of 2007, the Treasury yield curve was *inverted* by 20 basis points, with short-term yields exceeding the yields on longer maturities as the Fed campaigned to tighten credit. Today the tightening bias has been reversed, and the yield curve is showing its normal upward slope, with 10-year yields about 140 basis points above 90-day yields and 172 basis points above 2-year yields. While it will take time to have an effect, this steep yield curve is bullish for the economy.

It is important to note, given the weak economic reports of recent months, that inflation is always a long-term concern for bond investors. Gold and commodity prices have jumped sharply in recent years, and the dollar has declined 20% or more against other major currencies. These are indications of inflationary pressures. Yet the current yield of Treasury inflation indexed securities (TIPS) reflects an anticipation of only 2.3% inflation for the next ten years, a level that is little changed from a year ago. It's our feeling that TIPS are priced optimistically, but in today's environment we are more worried about credit quality than the longer term effects of inflation.

Spreads

At the end of December, the Lehman Index had a 9.64% yield and the yield on the 10-year Treasury bond was 4.03%, resulting in a spread of 561 basis points. So far in 2008, spreads have widened further to over 600 basis points, continuing the trend of the past seven months when spreads steadily rose from only 241 basis points in June. This is one of the most rapid increases in spreads in the past 30 years.

What is worrisome in recent months is that spreads have been on a steady march higher, even as the Fed has become more aggressive on interest rate cuts. The high-yield market is saying that a few reductions of short-term interest rates will not quickly solve the damaging liquidity problems in the market, and that the complicated process of unwinding the excess leverage of the past few years may drag out for at least several quarters. Leveraged loans, the bank lines given to high-yield issuers, hit new prices in early February. These loans, which are senior and well-secured and usually trade close to face value, fell dramatically with an index of leveraged loans trading at only 88% of par value and yielding nearly 10%.

Spreads are impacted to the greatest extent by economic factors and the level of defaults, but can also be influenced to some degree by technical market factors. Spreads have widened in recent months primarily due to a darkening economic outlook, but also due to the effects of poor liquidity in the market as major players withdraw and try to conserve capital.

The "appetite for risk" that was evident a year ago has disappeared, and investors are now demanding generous yield compensation for any sort of credit or liquidity risk in this struggling market. In addition, dealers saddled with inventory and anxious to avoid trading losses have pulled back from the market. This has removed crucial buying interest and support.

The current environment is one that has been experienced only once or twice a decade. The history of the high-yield market has been represented by cycles of 4-6 year periods between default peaks. The most recent cycle was stretched out by particularly easy credit conditions, so this cycle will likely run seven or even eight years. We are at the point in the cycle when credit conditions are tightening and spreads are widening. We don't know how long this process will take, or how high the spreads might eventually go, but spreads tend to peak at a time close to the reported peak in defaults. That will almost certainly not be in 2008, but more likely in 2009.

Supply and Demand

After a sizzling first half of 2007, when over $100 billion of new high-yield bond issues came to market, the second half of the year was muted by widespread problems in the credit markets, and the final tally of new issues for the full year came to $148 billion. This still enabled 2007 to go into the books as the second biggest year on record for high-yield underwritings, surpassed only by 2006. Leveraged loans also had a strong year, particularly in the first half, with new financing of $688 billion versus $612 billion of lending in 2006.

During the second half of the year, the market virtually shut down, except for a brief window of better conditions during September and October. After that quick respite, new worries swept the market and financings of corporate debt nearly disappeared for the remainder of the year.

Mergers and buyouts also fell dramatically later in the year. Buyouts reached $438 billion in 2007, far below the $600 billion forecasts early in the year. In addition to the decline in new deals, many pending deals from prior months collapsed due to financing problems and business uncertainties. Banks were holding approximately $300 billion of deal debt on their books at mid-year. They managed to reduce that backlog to around $220 billion in recent weeks, though current conditions would indicate that disposing of the remaining debt will be a very difficult process.

While supply is collapsing, demand is also shrinking. The problems in the CDO and CLO markets have removed a source of what had been very steady demand for new

bond issues in recent years. FitchRatings reports that CLOs bought about 60% of leveraged loans during 2007. These entities have almost completely exited the market and likely won't reappear until their structures have been improved. At the same time, traditional fixed-income investors like mutual funds and insurance companies have been tilting toward more safety, reducing allocations to risky credits and holding larger amounts of high-grade or Treasury issues.

As we look ahead to the remainder of this year it appears that, barring a substantial improvement in market conditions, new supply will be well under $100 billion for the year. Demand will also be lower, but will be helped by two factors. First, American high-yield investors receive nearly $80 billion of interest payments each year, most of which needs to be reinvested in the market. Second, with the increase in distressed issues, a number of ''vulture funds'' specializing in troubled companies will be looking for opportunities to pick up bargains in the market. Granted, these buyers don't appear until prices are close to rock bottom, but they will provide a new source of demand for bonds.

Another market characteristic that will help this year is that there are few issues reaching maturity. Many companies took advantage of the favorable market conditions between 2004 and 2006 to issue debt that will be coming due in the 2011-2016 timeframe. This refinancing activity reduced the number of bonds due over the next three years. FitchRatings is estimating that U.S. high-yield bond maturities in 2008 will approximate just $23 billion of issues, followed by approximately $37 billion in 2009 and $33 billion in 2010. These figures are much smaller than the $60-80 billion annual numbers in the outlying years.

Finally, the extremely low yields on Treasury securities and much higher available spreads on corporate securities will, we believe, eventually prod investors to begin taking more credit risk. We would not expect this in the very near future, but it will probably develop slowly in the coming quarters as the economic outlook becomes less bleak.

Fund Portfolio Strategy

The Fund had a very difficult second half of 2007, showing a negative total return of 4.38% versus a 0.97% decline in the Lehman Index.* As we mentioned in our last report, the Fund suffered significantly from its holdings in housing and financial issues. We were aware of the risks in these areas, but did not anticipate such a sharp and widespread decline in the sector. While we did somewhat reduce our real estate and financial holdings as the market turned down, we still were not able to avoid damage to the Fund's value.

The portfolio also was hurt by the extreme ''flight to safety'' in the credit markets. We had a significant portion of the Fund's assets in short-term and medium-term issues,

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** See performance disclosure on page 2.*

hoping to maintain stability in a market decline. As the credit crunch hit, these shorter maturities did not do as much as we hoped to help the portfolio maintain its value because investors fled all issues on credit fears, even those that would be maturing in the near future. Nevertheless, we believe that these issues will eventually work out well as a group.

What might have been lost in the tough market of recent months is that most of the issues held in the Fund portfolio are performing to expectations or even exceeding expectations. A number of companies are growing revenues, building cash flow and improving their balance sheets. We have had a couple of issues that have been strengthened by 2007 stock offerings that added equity to the corporate balance sheet while improving credit ratios. The majority of the issues in the portfolio, those not tied to the housing or mortgage sectors, have been solid performers.

At the moment, the high-yield market is trying to estimate how quickly and how far defaults will rise. Contrary to the attitude of a year ago, the feeling today is one of resignation to deteriorating credit fundamentals and continuing difficult conditions. Much depends on the economy's performance over the next year. If a recession is mild and brief, then the return on high-yield bonds should be competitive with the returns on other fixed-income maturities. A long and deep recession would produce a V-shape performance with further sharp declines followed later by a much stronger rally.

High-yield spreads are now over 600 basis points. This is very attractive if the economy holds together. In a more serious recession, we would expect the spread to approach the 1120 basis points that was seen in October 2002 after the Enron and Worldcom debacles. Historically, spreads over 900 basis points have provided excellent buying opportunities from a longer-term perspective. At the moment, the market seems to be heading in that direction.

We have not yet seen truly exceptional bargains in the market, but expect the opportunities to increase in coming quarters. We will be closely tracking the trend in the level of defaults. As we mentioned, it is more likely that a good bottom for high-yield bond prices, and a peak in defaults, will be seen in 2009. This year will be a time to put together a potential shopping list of issues and to pay particular attention to the sectors of the market that show a high level of distress.

The market will quickly improve when there are signs that defaults are no longer rising, and we hope to gradually move into a good position to take advantage of the next upswing. The high-yield category provided outstanding returns in 2003 and 2004 after the last peak in defaults, and we expect a similar terrific rally after this market downturn. That is probably still a number of months away, but we will be adopting a much more aggressive attitude as we see better opportunities.

Conclusion

This continues to be a difficult period for the bond market and for the Fund. We have frequently discussed the cyclical nature of the high-yield bond market, and we are moving through the most challenging part of the cycle. If we can navigate the coming year in a satisfactory fashion, we believe that the long-term outlook is outstanding.

We again want to mention to you that we are substantial investors with you in the Fund. The Fund portfolio manager and fellow employees of the Advisor have invested well over $1 million in the Fund, and therefore will be personally sharing in a significant way in the Fund's future performance. We are continuing to focus on achieving superior returns for your investment in the Fund.

Thank you once again for your confidence in the Fund and we look forward to sharing a prosperous future with you.

Aegis Financial Corporation
William S. Berno, CFA
Managing Director, Portfolio Manager

– Aegis High Yield fund's one-year, three-year and since inception (1/1/2004) average annual returns for the period ending December 31, 2007 are 0.74%, 7.21% and 6.37% respectively. Returns include reinvestment of dividends and capital gains. 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 of principal value will fluctuate so that upon redemption, an investor's shares may be worth more or less than their original cost. The Fund has an annualized expense ratio of 1.20%. Investors may call 1-800-528-3780 or go to the Fund's website www.aegisfunds.com to obtain performance data current to the most recent month end.

Investors should consider the Fund's investment objectives, risks, charges and expenses. The prospectus contains this and other information about the Fund. Investors can obtain a copy of the Fund's prospectus by downloading it from the Fund's website www.aegisfunds.com or by calling 1-800-528-3780. Investors should read the prospectus carefully before investing or sending money.

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