AMG Yacktman Special Opportunities Fund - Mid-Year Update - June 30, 2017

SEMI-ANNUAL INVESTOR LETTER

Class I | YASSX | Class Z | YASLX

YACKTMAN ASSET MANAGEMENT

AMG Yacktman Special Opportunities Fund – Mid-Year Update – June 30, 2017

For the six months ending 6/30/2017, the AMG Yacktman Special Opportunities Fund (the "Fund") returned 19.0%. The MSCI ACWI All Cap Index returned 11.4%, an outperformance of 7.6%.

June 30, 2017, also marks the three-year anniversary of the Fund. Since inception, the Fund has returned an annualized 6.5% versus the benchmark return of 4.9%, an outperformance of 1.6% annually. This accomplishment is satisfying given the current market environment, but we remain focused on our overarching goal—risk-adjusted returns over a full market cycle. The Fund's broad mandate to seek out the best investment ideas without constraints has led to a portfolio of quality businesses with conservative balance sheets at inexpensive absolute valuations, a resilient combination in an otherwise expensive market.

Fund Review

This year is off to a strong start, driven by healthy gains in core positions and no major detractors. This performance is on the heels of a solid 2016, leading to a trailing 12-month return of more than 40%. Even with this recent performance run, the Fund still trades at a significant discount to the market. We have responded to the upswing in the Fund by trimming winning positions while reallocating capital to other Fund portfolio companies and new investments. A critical element of our success is leveraging our flexible mandate to constantly rotate the Fund toward what we believe are better ideas. This flexibility to go anywhere will become only more important if valuations in the broader market remain elevated.

Financial Metrics[1]	YASLX / YASSX	MSCI ACWI All Cap Index	S&P 500® Index	Russell 2000® Index
P/E	11.9x	18.1x	20.73x	20.40x
P/BV	1.19x	1.94x	2.81x	2.00x
P/CF	9.55x	11.54x	13.65x	13.85x
P/Sales	0.48x	1.43x	2.08x	1.16x
EV/EBIT	6.60x	15.9x	16.6x	15.4x
Debt to Equity	58.1%	89.6%	97.0%	76.5%
ROA%	5.1%	6.2%	7.7%	3.8%

[1] *Source: AMG Funds & FactSet; Weighted average metrics; as of 6/30/17. Portfolio characteristics are subject to change*

We added a new metric to the table—enterprise value to earnings before interest and taxes (EV/EBIT). Unlike price to earnings (P/E) ratios, an EV/EBIT multiple incorporates the capital structure of the business. The Fund's average EV/EBIT multiple of 6.6x reflects the largest delta of any metric versus the market, showcasing the excess cash in many of our holdings. Cash on our companies' balance sheets dampens their return on assets (given that cash earns close to zero today) but we believe adds an important element of safety to the overall portfolio.

We added seven new positions to the Fund in the first half of 2017, demonstrating an ability to find value in an expensive market. This was an active period, although most of these new positions started out with a small weighting. At June 30, 2017, the top ten holdings in the Fund represented 45% of assets. The Fund's portfolio composition resembles a "barbell," featuring a concentrated group of top positions and a longer tail of diversified holdings for the remainder. We identified several areas of the market where we believed the risk/reward ratio was similar (such as Korean preferred shares and Japanese deep value microcaps). In those areas, we have utilized a "basket" approach to spread our investment over more companies. This structure allows us to put capital to work while waiting for truly great deals. We do not believe we are giving up much return by buying these baskets, and when diversification is free we are happy to partake.

We also exited three positions: Raven Industries Inc. (Raven), Amsterdam Commodities N.V. (Acomo) and Mocon. Raven was added to the Fund in January 2015. It has many of the characteristics we look for in an investment—strong return on capital, niche leadership positions, conservative balance sheet and successful track record. We initiated the position on a pullback in earnings due to the sharp downturn in both the agricultural and oil & gas markets. We added to the weighting as management took hard steps to right-size the business. We exited as the price recovered and the market embedded a much rosier outlook.

Acomo has been in the Fund from the start. It is primarily a spice trading company with a long history (several subsidiaries were founded back in the 1800s) and few comparable peers. Acomo offered stability—we never expected the stock to double or triple, but rather to steadily compound business value. Management delivered on this premise and our return was boosted as the earnings multiple expanded (showcasing the benefits of buying cheaply). These are some of our favorite types of investments, as the market often overlooks the boring or unique.

Finally, Mocon was acquired by Ametek for $30 per share in June. Mocon was also in the Fund since inception, when we purchased our initial position around $16. The company's permeation segment is by far the dominant leader with ~80% share in a niche market (equipment to measure the amount of gases that penetrate materials such as food packaging). It wasn't an exciting growth business, but we liked the combination of stable returns and a defensible position. This was the second acquisition of a company in the Fund, following Martha Stewart in 2015.

More than half of current holdings have been part of the Fund since inception. We hope to hold many of these companies for a long time. However, we are constantly adjusting portfolio weightings as price movements impact our estimates of future returns. Most of our trading in the first half of the year was trimming existing positions as prices moved higher, raising our cash position to 12%. Our cash holding is a reflection of our bottom-up investment approach. While we search for new areas to deploy these proceeds, cash serves as a useful option if the inevitable downturn appears.

Contributors / Detractors

Among the three largest contributors to the Fund in the first half were Samsung Electronics Preferred (Samsung), Emeco Holdings 9.875% 2019 Notes (Emeco) and Hargreaves Services plc (Hargreaves). Samsung moved past the Galaxy Note 7 setback to post strong earnings, driven by its components businesses. The company should benefit from a tight memory market and a shift in smartphones to OLED displays, both areas where Samsung has a technology lead and low cost position. An improved shareholder return policy featuring share repurchases was also well received by the market. Samsung is one of the largest companies in the world, yet the share price of the preferred shares has more than doubled in the last 18 months.

We have discussed Hargreaves in previous letters, often in the detractors section. However, it is pleasing to note the recent recovery in the share price as management reoriented the business in the face of a shifting U.K. coal and power market. Despite a deterioration in the core business, our investment was cushioned by Hargreaves' business model. As a distributor, Hargreaves' shrinking sales base turned working capital into cash and allowed the company to rapidly reduce debt. The biggest problem area, Hargreaves' surface mining operations, are now confined to a single mine. Despite being the main culprit of the earnings decline, the mining operation generated a hidden asset—vast land holdings that offer a number of real estate projects with potential returns far higher than Hargreaves' modest cost basis. The recent approval of the Blindwells development, a large residential housing project outside of Edinburgh, caused a sharp spike in the shares. We continue to be impressed by the management team and their navigation of such a challenging environment.

A special mention is also warranted for our investment in the Emeco bonds, which has been a strong contributor to returns. While we are an equity-focused fund, we took advantage of a unique situation in the high yield market, an option unavailable to many of our competitors. After our initial purchase, we suffered through a markdown on the bonds during the commodity bear market in 2016, as Emeco's equipment rental model was at the center of the maelstrom. But we felt secure in our senior position in the capital structure, with our bonds covered by Emeco's assets on the balance sheet. Fast forward to today—activist investors have installed new management, operations have improved and the company moved forward with an ambitious three-way merger with two rental peers. We received both new debt and equity in the combined company, with the new debt covering our cost basis in the old bonds. This means we received the equity upside for free and continue to hold a security paying 9.25% interest until 2022, not bad in an ultra-low rate world. The new bonds trading above par signal much improved prospects ahead.

Our largest detractors were Texhong Textile Group Ltd, America's Car-Mart Inc. and Reading International, Inc. All three had a negligible impact, due mostly to the normal variation in stock prices. In fact, we only had six positions decrease even a small amount during the first six months of 2017. We are doubtful that feat can be repeated for the rest of the year, but will work hard to match it.

Three Years In

Past letters have reminded shareholders that random fluctuations influence short-term results. A few quarters or years are not always representative of our investment analysis or execution, as prices can diverge from underlying value for extended periods. For a time, we felt the Fund was responding well below its potential due to headwinds from foreign currency movements and temporary price declines in some of our top holdings.

Currency movements were a drag on performance in the first 18 months. Although many of our holdings employ natural currency hedges, this dynamic was not always immediately recognized by the market. Currency volatility has moderated and we continue to believe that these swings will wash out in the long run.

Also, a confluence of events in a short period caused price declines in some of our top holdings. For example, litigation financer IMF Bentham Ltd. (Bentham) has been a large holding since inception. The company had built up a stellar track record of cases through 2015, losing only 6 cases out of 159 (a 96% success rate). Who could have predicted the company would then lose three major cases in a few short months? Even the best lawyers (or investment managers) get a few wrong, but the market often forecasts such losing streaks to continue indefinitely.

Bentham's string of case losses remind us of an advanced statistic in baseball called batting average on balls in play (BAPIP), which measures how many hits result when a ball is batted but stays on the field (ignoring strikeouts, walks, homeruns, etc.). Anyone who has played sports recognizes the role luck can play and how luck can seem to concentrate in a few critical plays. Sometimes the batter hits a hard line drive with tremendous velocity but directly to the shortstop for an easy out. The same hit two feet to the left leads to the baseball rolling in the gap for a double. Is this difference of a few feet luck or skill? Over short periods of time, unpredictable bounces can overwhelm skill and make an all-star player look like a minor leaguer. Yet over the long term, BAPIP tends to normalize and reveal a player's true abilities. The Fund experienced some tough bounces in a short period of time, but we stuck to our investment discipline. We purchased more of Bentham in response, and watched as Bentham's win percentage subsequently normalized, helping to drive a rapid recovery in Fund performance on both an absolute and relative basis. We finally hit a few line drives in the gap.

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Amongst our top contributors over the first three years were Emeco Holdings 9.875% Bonds, Samsung Electronics, Texhong Textile Group, America's Car-Mart and Retail Holdings. It is an eclectic list—from a subprime auto dealer to a Hong Kong yarn company, and from one of the largest technology companies in the world to a sub-$100m market cap special situation. Such a varied list of contributors validates our wide-ranging approach. While many funds are restricted to investing within narrow bands, we retain flexibility to go anywhere and be different. We feel having such differentiated insight across a range of investment opportunities is key to long-term success. This has proven true in our first three years and we believe it can continue in the future as well.

Amongst the Fund's top three detractors since inception include Hargreaves, Aggreko Plc, and Nac Co. All share a common element of being exposed to macro forces largely outside of the company's control which impacted business results. We still hold both Hargreaves and Aggreko, believing there is further room for recovery in both shares. We have taken a permanent loss of capital in only a few positions over the first three years, and most holdings have positive returns versus our cost basis. Avoiding major losses is just as critical as our top contributors. Our record in this area highlights our value discipline and focus on risk-adjusted returns.

The drawdown and subsequent recovery was a good testing ground of our core principles. The true mettle of the Fund's investment strategy will only show itself on the other side of a market downturn, but we believe our strategy of holding quality businesses at inexpensive prices is sound. Any market pullback would be an opportunity to deploy more capital at better prices. Having gone through our own mini-bear market and recovery in the Fund in only three years, we are confident that sticking to our core philosophy will yield strong long-term results.

Conclusion

The current bull market began in March 2009, more than eight years ago. Valuations are expensive across the majority of asset classes, generally a dangerous time for investors. We make no attempt to predict the timing of the next major downturn, but instead emphasize our bottom-up investment process. If the bull market carries on, we will lean on our go-anywhere approach, as we believe it gives us the best possible chance of uncovering the remaining pockets of value. If a downturn occurs, we are well prepared with a collection of high quality businesses and ample cash to take advantage of cheaper prices.

At the three-year mark, we have generated both positive absolute returns and outperformed our benchmark while holding excess cash in the Fund. We believe there remains significant value embedded in the Fund's portfolio which is only beginning to shine through. Our objective remains to produce attractive risk-adjusted returns over a full market cycle, and we appreciate our shareholders who entrust us with capital in pursuit of this long-term goal.

Disclosure

Investors should carefully consider the Fund's investment objectives, risks, charges and expenses before investing. For this and other information, please call 800.835.3879 or visit amgfunds.com to download a free prospectus. Read it carefully before investing or sending money.

Past performance is no guarantee of future results.

Investments in international securities are subject to certain risks of overseas investing including currency fluctuations and changes in political and economic conditions, which could result in significant market fluctuations. These risks are magnified in emerging markets.

The Fund may suffer significant losses on assets that it sells short. Unlike the possible loss on a security that is purchased, there is no limit on the amount of loss on an appreciating security that is sold short.

The Fund can invest in securities of different market capitalizations (small-, mid- and large-capitalizations) and styles (growth vs. value), each of which will react differently to various market movements.

The Fund is subject to currency risk resulting from fluctuations in exchange rates that may affect the total loss or gain on a non-U.S. Dollar investment when converted back to U.S. Dollars.

The Fund is subject to the special risks associated with investments in micro-cap companies, such as relatively short earnings history, competitive conditions, less publicly available corporate information, and reliance on a limited number of products.

The Fund is subject to risks associated with investments in small- and mid-capitalization companies such as greater price volatility, lower trading volume, and less liquidity than the stocks of larger, more established companies.

Companies that are in similar businesses may be similarly affected by particular economic or market events; to the extent the Fund has substantial holdings within a particular sector, the risks associated with that sector increase.

A greater percentage of the Fund's holdings may be focused in a smaller number of securities which may place the Fund at greater risk than a more diversified fund.

The Funds are subject to the risks associated with investments in debt securities, such as default risk and fluctuations in the perception of the debtor's ability to pay its creditors.
Changing interest rates may adversely affect the value of an investment. An increase in interest rates typically causes the value of bonds and other fixed income securities to fall.

Price/earnings (or P/E) ratio is a comparison of the company's closing stock price and its trailing 12-month earnings per share.

Price/book (or P/B) ratio is calculated by dividing the market price of a company's outstanding stock by its book value (total assets of a company less liabilities) and then adjusting for the number of shares outstanding. Stocks with negative book values are usually excluded from this calculation.

The price-to-cash-flow (or P/CF) ratio is a stock valuation indicator that measures the value of a stock's price to its cash flow per share. The ratio takes into consideration a stock's operating cash flow (OCF), which adds non-cash earnings such as depreciation and amortization to net income.

The price-to-sales (or P/Sales) ratio is a valuation ratio that compares a company's stock price to its revenues. The price-to-sales ratio is an indicator of the value placed on each dollar of a company's sales or revenues.

EV/EBIT equals a company's enterprise value (market capitalization plus debt, minority interest and preferred shares, minus total cash and cash equivalents) divided by earnings before interest and tax.

Debt/Equity (D/E) Ratio, calculated by dividing a company's total liabilities by its stockholders' equity, is a debt ratio used to measure a company's financial leverage.

ROA is the percentage a company earns on its assets in a given year. The calculation is net income divided by average total assets. The better the company, the more profit it generates as a percentage of its assets.

High-yield bonds (also known as "junk bonds") are subject to additional risks such as the risk of default.

A short-term redemption fee of 2% will be charged on redemptions of Funds shares within 60 days of purchase.

The Fund may use derivatives, such as options and futures, which can be illiquid, may disproportionately increase losses, and have a potentially large impact on performance.

The MSCI All Country World Index (ACWI) All Cap covers approximately 14,000 securities and includes large, mid, small and micro cap size segments for all Developed Markets countries in the index together with large, mid and small cap size segments for the Emerging Markets countries. Unlike the Fund, the MSCI ACWI All Cap is unmanaged, is not available for investment and does not incur expenses.

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The S&P 500 Index is a capitalization-weighted index of 500 stocks. The S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Russell 2500 ® Index

The Russell 2000® Index is composed of the 2000 smallest stocks in the Russell 3000® Index and is widely regarded in the industry as the premier measure of small-cap stock performance.

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