



# Davis-Rea Equity Fund

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**Annual Management Report of Fund Performance**

For the year ended December 31, 2016

# Davis-Rea Equity Fund

## Annual Management Report of Fund Performance

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This Annual Management Report of Fund Performance contains financial highlights, but does not contain the audited annual financial statements of the Davis-Rea Equity Fund. You can get a copy of the audited annual financial statements of the Davis-Rea Equity Fund at your request and, at no cost, by calling Davis-Rea Ltd. at (416) 324-2200 or at (877) 391-9929, by writing to us at 79 Wellington Street West, Suite 3535, P.O. Box 239, Toronto, Ontario, M5K 1J3, or by visiting our website at [www.davisrea.com](http://www.davisrea.com) or SEDAR at [www.sedar.com](http://www.sedar.com).

Securityholders may also contact us using one of these methods to request a copy of the Davis-Rea Equity Fund's proxy voting policies and procedures, proxy voting disclosure record, and/or quarterly portfolio disclosure.

## **Management Discussion of Fund Performance**

### **Investment Objective and Strategies**

The investment objective of the Davis-Rea Equity Fund (the “**Fund**”) is to preserve and enhance capital by primarily investing in Canadian, U.S. and international equity securities for long-term gain.

Securities for the Fund will be selected by us based on our assessment of the markets and potential investment opportunities. We intend to focus the Fund on various sectors of the economy from time to time, and will typically only invest in the equity securities of large to medium capitalized companies with a market capitalization of not less than \$250 million. Any exceptions to this market capitalization will be limited to less than 10% of the value of the Fund. We may also use derivatives from time to time to hedge against changes in currency, losses from movements in the stock markets or to realize additional gains. At our discretion, the Fund may also hold cash and/or short-term money market instruments, fixed income securities and convertible debentures, and may from time to time invest up to 10% of its assets in class N units of the Davis-Rea Fixed Income Fund.

### **Risk**

The Fund is subject to a number of risks that have not changed over the last year. These risks include the Fund not being able to obtain its investment objective, general economic conditions, interest rate fluctuations and stock market risk. See the prospectus of the Fund for a full description of the risks that the Fund may be exposed to. The Fund also continues to have a risk rating of medium-to-high.

### **Results of Operations**

The Fund returned 8.90% for the full year ended December 31, 2016, compared to returns of 17.72% for the S&P/TSX 60 Index and 9.54% for the S&P 500 Index. The Fund continued to explore the main investment themes of healthcare and technology. It participated and took profits as some of our energy names recovered in the face of rising oil prices. The Fund decreased equity exposure to foreign markets as geopolitical tensions remained heightened throughout the year. We entered 2016 with a cautious stance and continued to tread carefully for much of the year, maintaining a healthy cash balance that would insulate the portfolio while allowing us to be opportunistic with any short-term weakness in the markets.

## Recent Developments

The year started with a violent sell-off caused by fears of a slowdown in global growth and concerns over negative interest rates. 2016 was ripe with uncertainty and volatility - in addition to the U.S. election, uncertainty continued to mount elsewhere in the markets as problems emerged in the European banking system, changes were made to Canada's mortgage rules, and the market sought to digest a U.S. interest rate increase in December. With so much uncertainty on the horizon, the Fund was repositioned to be slightly more defensive.

One of many political events that occurred during the year was the June, 2016 Brexit vote, which caught markets by surprise. There was a swift sell-off in a flight to quality post the vote where the Equity Fund was opportunist in adding to our healthcare and technology holdings. In the latter part of the year, the Fund participated in secondary offerings in the energy and utility sectors which offered attractive prices and yields. The Fund also exited positions providing exposure to China and India as we believed volatility and geopolitical tensions would temper returns in the near term.

Energy was a large contributor to the Fund's positive performance for the year with the market beginning to recognize a supply response to oil production beginning at the end of the first quarter of 2016. The commodity price further recovered in the last quarter of the year when a supply-side agreement was made by OPEC members to cut oil production in an attempt to raise oil prices.

The main event of the fourth quarter was the U.S. Presidential election where the result caught most market participants and pundits off guard. With Donald Trump as President-elect, the markets rallied behind the optimism of wide sweeping reform by Trump, such as reducing regulatory restrictions for banks, repatriation of cash held overseas at favourable rates and fiscal stimulus to increase infrastructure spending and bring back jobs to the U.S. The Fund's healthcare holdings were a drag on performance throughout the year as the entire sector underperformed as concerns regarding drug pricing and business models weighed on the entire sector. The sector did however rebound slightly post-election as Trump's policies for healthcare and pricing were viewed as more lenient and favorable to those of Hillary Clinton. The Fund's technology holdings did not produce positive returns as many sector constituents sold off over concerns that Trump would impose new regulations detrimental to their businesses and products.

In the fourth quarter of 2016, the Equity Fund initiated a new position in the consumer sector when a company sold off after a solid earnings report earlier in the quarter. We had been following the company for some time and took advantage of this sell-off to initiate a position. Our energy holdings continue to possess strong balance sheets and are poised to take advantage of the improving price environment. Markets continue to move higher on the optimistic view of Trump's policy changes, but we remain cautious. We believe that while

Trump's policies and proposals may sound good on paper, they might be challenging to implement. We also believe that some of the suggested policies may actually be a hindrance to trade and global growth, such a border adjustment tax. In the long run, we remain confident in our holdings, but nonetheless continue to maintain a healthy cash balance.

## Related Party Transactions

Davis-Rea Ltd. (the “**Manager**”) is the manager and portfolio adviser for the Fund. The Manager is responsible for managing the day-to-day activities of the Fund and providing or arranging for all required administrative services of the Fund. In consideration for such services, certain classes of units of the Fund pay the Manager a monthly management fee based on the net asset value (“**NAV**”) of the applicable classes of units of the Fund, calculated daily. Each holder of class O units of the Fund pays their management fee directly to us pursuant to their class O investment management agreement. The class N units of the Fund do not pay a management fee and may only be bought by another Davis-Rea Mutual Fund.

The Manager has also created an independent review committee (“**IRC**”) to review and provide impartial judgment on conflict of interest matters. The IRC reviews potential conflicts of interest referred to it by the Manager and makes recommendations on whether a course of action is fair and reasonable for the Fund. The IRC prepares an annual report of its activities for interested parties. A copy of the IRC’s report for 2016 will be available at [www.davisrea.com](http://www.davisrea.com) at the end of March, 2017.

## Management Fees

The table below outlines the Fund’s annual management fees and the trailer fees, if any, that the Manager pays to dealers who distribute units of the applicable class of the Fund (i.e., a percentage of the daily NAV of such class). The Manager is paid an annual management fee by each unitholder who invests in class O units of the Fund pursuant to a class O investment management agreement, which will not exceed the management fee that we receive from class A units of the Fund. The class N units of the Fund do not pay a management fee and may only be bought by another Davis-Rea Mutual Fund.

	Class A	Class B	Class F	Class O	Class N
Management Fee	1.75%	2.00%	1.50%	Negotiated	N/A
Trailer Fee (maximum rate as a percentage of management fees)	N/A	0.50%	N/A	N/A	N/A

## Class O Units\*

### Financial Highlights

The following tables show selected key financial information about the class O units of the Fund\* and are intended to help you understand the Fund's financial performance for the past five years ended December 31.

The Fund's Net Assets per Unit	Dec. 31, 2016**	Dec. 31, 2015**	Dec. 31, 2014**	Dec. 31, 2013**	Dec. 31, 2012
<b>Net assets - beginning of period<sup>(1)</sup></b>	\$144,616,649	\$137,855,612	\$80,747,475	\$24,038,130	\$3,598,576
<b><i>Increase (decrease) from operations:</i></b>					
Total revenue	\$1,068,856	\$2,053,719	\$1,487,656	\$779,613	\$375,235
Total expenses	\$344,888	\$513,430	\$795,839	\$104,234	\$55,359
Realized gains (losses) for the period	(\$6,563,517)	\$10,268,593	\$9,863,411	\$3,637,691	\$496,812
Unrealized gains (losses) for the period	\$16,635,083	(\$4,749,224)	(\$8,902,433)	\$3,832,368	\$957,478
<b>Total increase (decrease) from operations<sup>(2)</sup></b>	\$10,795,534	\$7,059,658	\$1,652,795	\$8,145,438	\$1,774,167
<b><i>Distributions:</i></b>					
From net realized gain on investments	\$1,676,466	\$8,856,661	\$9,695,919	\$3,655,121	\$522,189
From net investment income	\$537,095	\$1,668,646	\$1,166,745	\$674,769	\$285,790
<b>Total Annual Distributions</b>	\$2,213,561	\$10,525,308	\$10,862,664	\$4,329,890	\$807,979
<b>Net assets - end of period</b>	\$126,089,070	\$144,616,649	\$137,855,612	\$80,747,475	\$23,990,965
<b><i>Ratios and Supplemental Data</i></b>					
Total net asset value <sup>(1)</sup>	\$126,089,070	\$144,616,649	\$137,855,612	\$80,747,475	\$23,990,965
Number of units outstanding <sup>(1)</sup>	10,446,208	12,832,001	11,977,029	6,913,311	2,217,049
Management expense ratio	0.13%	0.15%	0.16%	0.22%	0.37%
Management expense ratio ^ before waivers or absorption (%) <sup>(2)</sup>	0.13%	0.15%	0.16%	0.22%	0.37%
Trading expense ratio (%) <sup>(3)</sup>	0.07%	0.06%	0.35%	0.41%	0.53%
Portfolio turnover rate (%) <sup>(4)</sup>	46.46%	41.53%	70.30%	59.50%	200.80%
<b>Net asset value per unit</b>	\$12.07	\$11.27	\$11.51	\$11.68	\$10.82

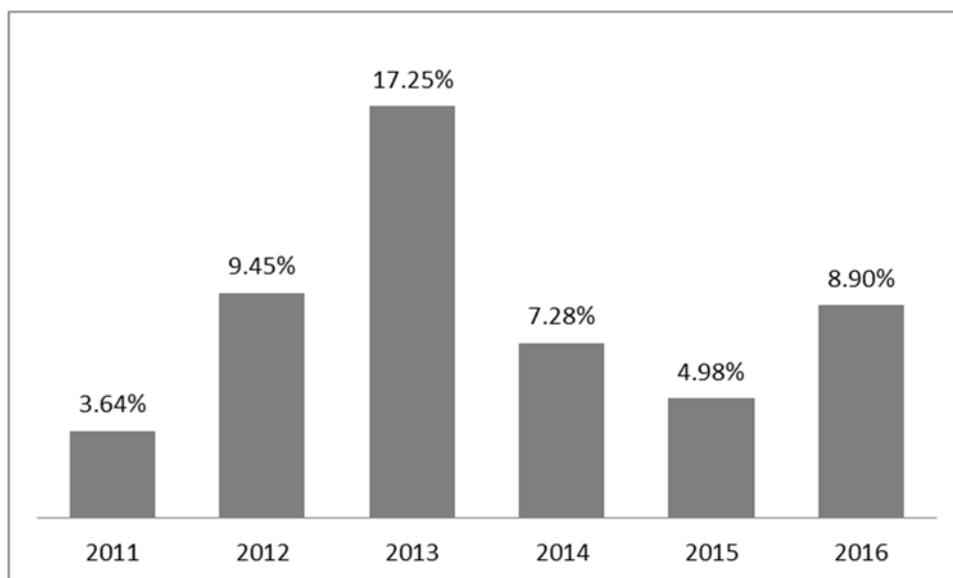
- \* Class O units of the Fund were first offered by prospectus on March 18, 2013 and were offered on an exempt basis since June 19, 2011. For explanatory notes, please refer to “Explanatory Notes to Financial Highlights” at the end of the section.
- \*\* Financial Highlights for the years 2016, 2015, 2014 and 2013 have been prepared under IFRS standards. Prior years were prepared under Canadian GAAP standards. Previously under Canadian GAAP, the Fund measured the values of its investments in accordance with Section 3855, Financial Instruments – Recognition and Measurement. As a result of the adoption of IFRS on January 1, 2014, an adjustment was recognized to increase the carrying value of the Fund’s investments by \$47,165 as at January 1, 2013.
- ^ Each investor enters into a class O investment management agreement with the Manager and pays a management fee to the Manager directly.

### **Past Performance**

The following information does not take into account any class O management fees, which are paid to the Manager pursuant to a class O investment management agreement. The past performance indicated below assumes that all distributions made by the Fund in the periods shown were re-invested in additional units of the applicable class of the Fund. In addition, the past performance results shown below does not take into account sales, redemption, distribution or other optional charges that would have reduced returns or performance. Finally, past performance does not necessarily indicate how the Fund will perform in the future.

## Year-by-Year Returns

The bar chart below shows the Fund's performance for class O units in each of the years shown. It illustrates how the Fund's performance has changed from year to year. In percentage terms, the bar chart shows how much an investment made at the beginning of the period has increased or decreased by the end of the period.



## Annual Compound Returns

The following table shows the annual compound total returns for the class O units of the Fund for the last year, three years, and since inception (i.e., June 19, 2011). The annual returns are compared to the returns of a Blended Equity Benchmark. This benchmark return is generated using a 50% weighting in the S&P/TSX 60 Index and a 50% weighting in the S&P 500 Index.

	Since Inception (June, 2011)	1 Year	3 Year	5 Year
Davis-Rea Equity Fund	9.25%	8.90%	7.04%	9.54%
Blended Equity Benchmark	6.55%	13.63%	5.66%	8.98%

The above comparison demonstrates how the Fund has generally achieved its investment objective of preserving and enhancing capital since inception. For example, since June 19, 2011, the performance of the Class O units was 2.7% above the return of a Blended Equity benchmark.

## Class B Units\*

### Financial Highlights

The following tables show selected key financial information about the class B units of the Fund\* and are intended to help you understand the Fund's financial performance for the three years ended December 31.

The Fund's Net Assets per Unit	Dec. 31, 2016	Dec. 31, 2015	Dec. 31, 2014
<b>Net assets - beginning of period<sup>(1)</sup></b>	\$28,922	\$28,180	\$0
<b><i>Increase (decrease) from operations:</i></b>			
Total revenue	\$235	\$414	\$96
Total expenses	\$722	\$793	\$37
Realized gains (losses) for the period	(\$1,610)	\$2,035	\$308
Unrealized gains (losses) for the period	\$3,966	(\$897)	(\$4,129)
<b>Total increase (decrease) from operations<sup>(2)</sup></b>	\$1,868	\$759	(\$3,762)
<b><i>Distributions:</i></b>			
From net realized gain on investments	\$344	\$0	\$434
From net investment income	\$0	\$1,793	\$109
<b>Total Annual Distributions</b>	\$344	\$1,793	\$543
Net assets - end of period	\$30,790	\$28,922	\$28,180
<b><i>Ratios and Supplemental Data</i></b>			
Total net asset value <sup>(1)</sup>	\$30,790	\$28,922	\$28,180
Number of units outstanding <sup>(1)</sup>	3,492	3,449	3,250
Management expense ratio	2.39%	2.40%	2.12%
Management expense ratio ^ before waivers or absorption (%) <sup>(2)</sup>	2.39%	2.40%	2.12%
Trading expense ratio (%) <sup>(3)</sup>	0.07%	0.06%	0.35%
Portfolio turnover rate (%) <sup>(4)</sup>	46.46%	41.53%	70.30%
<b>Net asset value per unit</b>	\$8.82	\$8.39	\$8.67

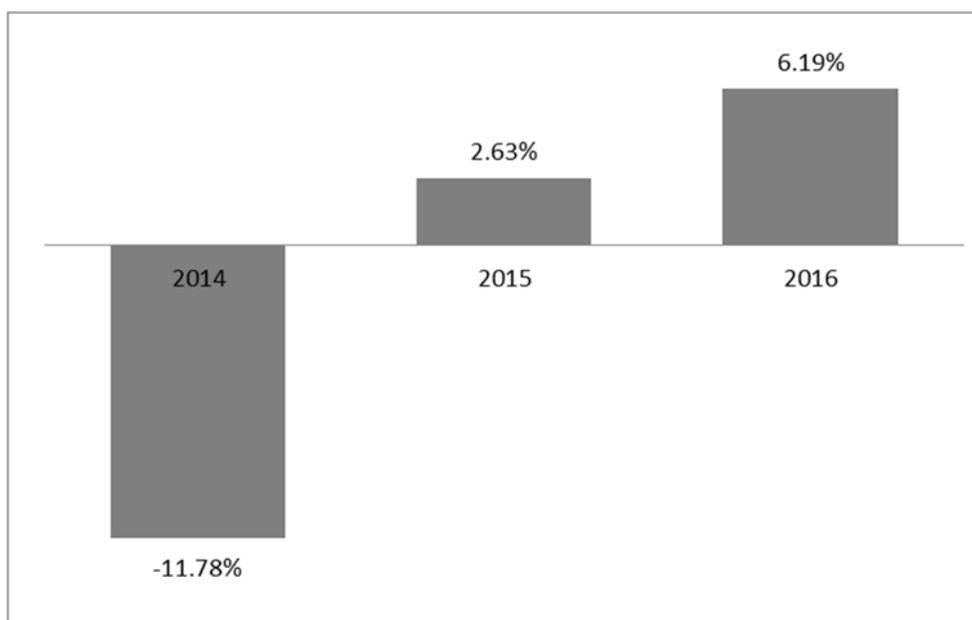
- \* Class B units of the Fund were first offered by prospectus on March 18, 2013. Class B units were first issued on September 17, 2014. For explanatory notes, please refer to “Explanatory Notes to Financial Highlights” at the end of the section.
- \*\* Class F units of the Fund are offered by prospectus, but as at December 31, 2016, no units of either class had yet been issued to the public.

## Past Performance

The following information takes into account all class B management fees. The past performance indicated below assumes that all distributions made by the Fund in the periods shown were re-invested in additional units of the applicable class of the Fund. In addition, the past performance results shown below does not take into account sales, redemption, distribution or other optional charges that would have reduced returns or performance. Finally, past performance does not necessarily indicate how the Fund will perform in the future.

## Year-by-Year Returns

The bar chart below shows the Fund’s performance for class B units in each of the years shown. It illustrates how the Fund’s performance has changed from year to year. In percentage terms, the bar chart shows how much an investment made at the beginning of the period has increased or decreased by the end of the period. The return shown for 2014 is for the period since inception on September 17, 2014.



## Annual Compound Returns

The following table shows the annual compound total returns for the class B units of the Fund for the period ended December 31, 2016 and since inception (i.e., September 17, 2014). The annual returns are compared to the returns of a Blended Equity Benchmark. This benchmark return is generated using a 50% weighting in the S&P/TSX 60 Index and a 50% weighting in the S&P 500 Index.

	<b>Since Inception (September, 2014)</b>	<b>1 Year</b>
Davis-Rea Equity Fund	-1.67%	6.19%
Blended Equity Benchmark	3.40%	13.63%

## Class A Units\*

### Financial Highlights

The following tables show selected key financial information about the class A units of the Fund\* and are intended to help you understand the Fund's financial performance for the two years ended December 31.

The Fund's Net Assets per Unit	Dec. 31, 2016	Dec. 31, 2015
<b>Net assets - beginning of period<sup>(1)</sup></b>	\$922,373	\$14
<b><i>Increase (decrease) from operations:</i></b>		
Total revenue	\$7,504	\$15,899
Total expenses	\$20,471	\$22,523
Realized gains (losses) for the period	(\$51,493)	\$75,519
Unrealized gains (losses) for the period	\$126,851	(\$187,473)
<b>Total increase (decrease) from operations<sup>(2)</sup></b>	\$62,390	(\$118,579)
<b><i>Distributions:</i></b>		
From net realized gain on investments	\$10,966	\$45,047
From net investment income	\$0	\$662
<b>Total Annual Distributions</b>	\$10,966	\$45,709
<b>Net assets - end of period</b>	\$984,765	\$922,373
<b><i>Ratios and Supplemental Data</i></b>		
Total net asset value <sup>(1)</sup>	\$984,765	\$922,373
Number of units outstanding <sup>(1)</sup>	67,067	66,245
Management expense ratio	2.10%	2.14%
Management expense ratio ^ before waivers or absorption (%) <sup>(2)</sup>	2.10%	2.14%
Trading expense ratio (%) <sup>(3)</sup>	0.07%	0.06%
Portfolio turnover rate (%) <sup>(4)</sup>	46.46%	41.53%
<b>Net asset value per unit</b>	\$14.68	\$13.92

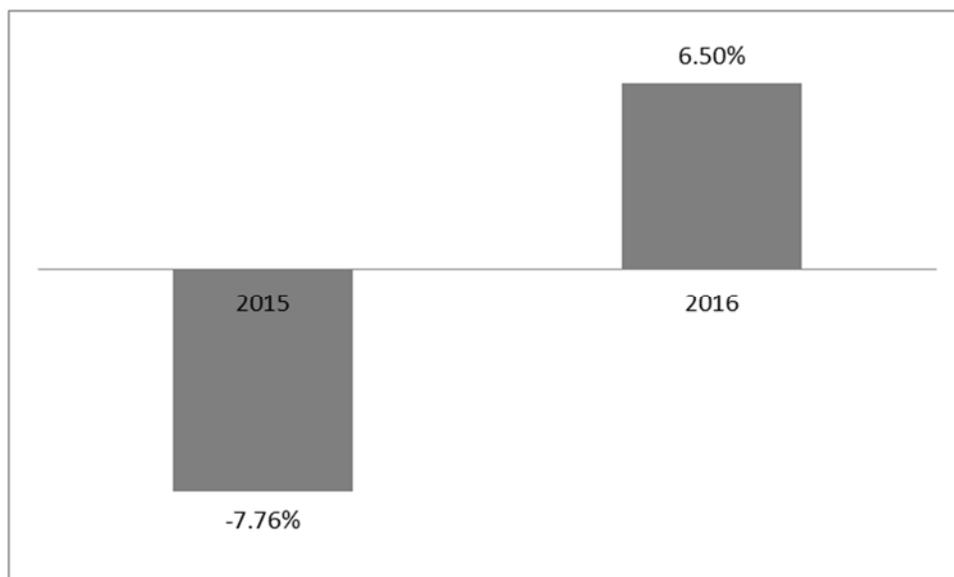
- \* Class A units of the Fund were first offered by prospectus on March 18, 2013. Class A units were first issued on April 30, 2015. For explanatory notes, please refer to “Explanatory Notes to Financial Highlights” at the end of the section.

### Past Performance

The following information takes into account all class A management fees. The past performance indicated below assumes that all distributions made by the Fund in the periods shown were re-invested in additional units of the applicable class of the Fund. In addition, the past performance results shown below does not take into account sales, redemption, distribution or other optional charges that would have reduced returns or performance, Finally, past performance does not necessarily indicate how the Fund will perform in the future.

### Year-by-Year Returns

The bar chart below shows the Fund’s performance for class A units in each of the years shown. It illustrates how the Fund’s performance has changed from year to year. In percentage terms, the bar chart shows how much an investment made at the beginning of the period has increased or decreased by the end of the period. The return shown for 2015 is for the period since inception on April 30, 2015.



## Annual Compound Returns

The following table shows the annual compound total returns for the class A units of the Fund since inception (i.e., April 30, 2015). The annual returns are compared to the returns of a Blended Equity Benchmark. This benchmark return is generated using a 50% weighting in the S&P/TSX 60 Index and a 50% weighting in the S&P 500 Index.

	<b>Since Inception (April, 2015)</b>	<b>1 Year</b>
Davis-Rea Equity Fund	-1.07%	6.50%
Blended Equity Benchmark	3.17%	13.63%

## Class N Units\*

### Financial Highlights

The following tables show selected key financial information about the class N units of the Fund\* and are intended to help you understand the Fund's financial performance for the past five years ended December 31.

The Fund's Net Assets per Unit	Dec. 31, 2016**	Dec. 31, 2015**	Dec. 31, 2014**	Dec. 31, 2013**	Dec. 31, 2012
<b>Net assets - beginning of period<sup>(1)</sup></b>	\$15,583,328	\$12,533,126	\$12,698,296	\$6,136,068	\$1,301,022
<b><i>Increase (decrease) from operations:</i></b>					
Total revenue	\$118,447	\$218,467	\$181,426	\$154,852	\$105,611
Total expenses	\$40,404	\$54,617	\$98,819	\$20,704	\$15,581
Realized gains (losses) for the period	(\$927,510)	\$1,133,299	\$1,240,523	\$722,543	\$139,830
Unrealized gains (losses) for the period	\$2,103,679	(\$778,289)	(\$95,209)	\$619,298	\$164,141
<b>Total increase (decrease) from operations<sup>(2)</sup></b>	\$1,254,212	\$518,860	\$1,227,922	\$1,475,989	\$394,000
<b><i>Distributions:</i></b>					
From net realized gain on investments	\$172,704	\$955,794	\$944,011	\$735,994	\$133,296
From net investment income	\$57,632	\$177,505	\$129,012	\$148,653	\$69,831
<b>Total Annual Distributions</b>	\$230,336	\$1,133,299	\$1,073,023	\$884,647	\$203,127
<b>Net assets - end of period</b>	\$16,562,540	\$15,583,328	\$12,533,126	\$12,698,296	\$6,124,041
<b><i>Ratios and Supplemental Data</i></b>					
Total net asset value <sup>(1)</sup>	\$16,562,540	\$15,583,328	\$12,533,126	\$12,698,296	\$6,124,041
Number of units outstanding <sup>(1)</sup>	1,354,595	1,365,420	1,074,882	1,086,252	565,378
Management expense ratio	0.13%	0.15%	0.19%	0.22%	0.37%
Management expense ratio before waivers or absorption (%) <sup>(2)</sup>	0.13%	0.15%	0.19%	0.22%	0.37%
Trading expense ratio (%) <sup>(3)</sup>	0.07%	0.06%	0.35%	0.41%	0.53%
Portfolio turnover rate (%) <sup>(4)</sup>	46.46%	41.53%	70.30%	59.50%	200.80%
<b>Net asset value per unit</b>	\$12.23	\$11.41	\$11.66	\$11.69	\$10.83

- \* Class N units of the Fund may only be purchased by another Davis-Rea Mutual Fund. For explanatory notes, please refer to “Explanatory Notes to Financial Highlights” at the end of the section.
- \*\* Financial Highlights for the years 2016, 2015, 2014 and 2013 have been prepared under IFRS standards. Prior years were prepared under Canadian GAAP standards. Previously under Canadian GAAP, the Fund measured the values of its investments in accordance with Section 3855, Financial Instruments – Recognition and Measurement. As a result of the adoption of IFRS on January 1, 2014, an adjustment was recognized to increase the carrying value of the Fund’s investments by \$12,027 as at January 1, 2013.

## **Explanatory Notes to Financial Highlights**

### **Net assets per unit:**

- (1) This information is derived from the Fund’s audited annual financial statements. In the period the Fund or a class of units of the Fund is established, the financial information is provided from the date of inception to the end of the period.
- (2) Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase (decrease) in net assets from operations is based on the weighted average number of units outstanding over the fiscal period. This table is not intended to be a reconciliation of opening and closing net assets per unit.

### **Ratios and Supplemental Data:**

- (1) This information is provided at the end of the period shown.
- (2) Management expense ratio is based on total expenses for the stated period and is expressed as an annualized percentage of daily average net asset value during the period.
- (3) The trading expense ratio represents the total commissions and other portfolio transaction costs expressed as an annualized percentage of net asset value during the period.
- (4) The Fund’s portfolio turnover rate indicates how actively the Fund’s investments are traded. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all its investments once in the course of the relevant period. There is

not necessarily a relationship between a high turnover rate and the performance of the Fund.

## Summary of Investment Portfolio

### Davis-Rea Equity Fund – as at December 31, 2016

	<b>% of NAV</b>
<b>Canadian Equities</b>	
<b>Consumer Discretionary</b>	
Aritzia Inc.	0.73%
	<b>0.73%</b>
<b>Energy</b>	
Gear Energy Ltd.	8.71%
Kelt Exploration Ltd.	8.25%
Keyera Corp.	6.96%
Spartan Energy Corp.	9.05%
Tourmaline Oil Corp.	9.83%
	<b>42.80%</b>
<b>Financials</b>	
Automotive Properties REIT	3.04%
	<b>3.04%</b>
<b>Utilities</b>	
Brookfield Infrastructure Partners L.P.	4.64%
	<b>4.64%</b>
<b>Total Canadian Equities</b>	<b>51.22%</b>
<b>Canadian Bonds</b>	
Air Canada, Callable, 4.750%, 2023/10/06	4.14%
Kelt Exploration Ltd., Convertible, 5.000%, 2021/05/31	3.41%
<b>Total Canadian Bonds</b>	<b>7.54%</b>
<b>Foreign Equities</b>	
<b>Consumer Discretionary</b>	
Amazon.com Inc.	1.57%
McDonald's Corp.	1.31%
Walt Disney Co. (The)	2.51%
	<b>5.39%</b>
<b>Health Care</b>	
Celgene Corp.	5.29%
Cerner Corp.	1.02%
Stryker Corp.	3.58%
	<b>9.89%</b>
<b>Industrials</b>	
Stanley Black & Decker Inc.	2.68%
	<b>2.68%</b>
<b>Information Technology</b>	
Alphabet Inc., Class 'A'	7.03%
Apple Inc.	1.05%
Facebook Inc., Class 'A'	3.76%
	<b>11.83%</b>
<b>Total Foreign Equities</b>	<b>29.79%</b>
<b>Total Cost and Fair Value of Investments</b>	<b>88.56%</b>
<b>Transaction Cost Included in Average Cost</b>	<b>0.00%</b>
<b>Total Investments</b>	<b>88.56%</b>
<b>Other Assets and Liabilities, Net</b>	<b>11.44%</b>
<b>Net Assets Attributable to Holders of Redeemable Units</b>	<b>100.00%</b>

The Fund's summary of investment portfolio set out above will change due to ongoing portfolio transactions. A quarterly update is available on request.

# DAVIS-REA EQUITY FUND

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