DAVY ASSET MANAGEMENT

FOR INVESTMENT PROFESSIONALS ONLY

DAVY DISCOVERY EQUITY STRATEGY

Q4 2018 UPDATE

PERFORMANCE	1 MONTH (%)	Q4 2018 (%)	1 YEAR (%)	3 YEARS P.A (%)	5 YEARS P.A (%)
DAVY DISCOVERY EQUITY STRATEGY* (NET OF FEES)	-9.84	-18.07	-10.71	3.89	7.85
MSCI WORLD SMALL & MID-CAP INDEX** (TOTAL RETURN)	-9.49	-15.45	-8.88	3.93	8.25

Source: Davy Asset Management (Class A Acc Eur) and Bloomberg as at 31st December 2018.

*On 19th April 2013, the previously proposed changes to the fund strategy were implemented. For more information please contact Davy Asset Management.
**The benchmark index shown above does not include fees or operating expenses and you cannot invest in it.

The Davy Discovery Equity Fund was launched on 12th December 2014. Investors should note the Davy Discovery Equity Fund (UCITS) is newly established. The past performance reflects past performance data relating to the Davy Discovery Equity Fund (non-UCITS) which merged with the Davy Discovery Equity Fund (UCITS) (the "Merger"). Prior to the Merger when the Fund was not authorised as a UCITS, the investment policy, strategy and portfolio composition were largely the same. In the circumstances, the past performance data included in this document is believed to be an appropriate reference for investors.

FUND OVERVIEW

The investment aim of the **Davy Discovery Equity Fund** (the 'Fund') is to achieve long-term capital growth by investing in shares of small and medium sized companies on a global basis. These companies demonstrate growth potential and represent attractive investment opportunities. Investing during the early stage of a company's life cycle can lead to higher than average investment returns.

FUND PERFORMANCE

The Fund declined by 18.07% versus 15.45% for its benchmark the MSCI World SMID over the quarter, as stock selection, asset allocation and currencies made negative contributions to performance. The strong rebound in Value relative to Growth in the latter months of 2018 meant the Discovery Equity Fund performed broadly in-line with its benchmark for the year. Importantly, our house style Quality helped to protect the Fund on the downside by making a positive contribution to performance in the fourth quarter and for the year overall.

The final quarter of 2018 began and ended with markets focused on sentiment not fundamentals. The third quarter earnings season was broadly positive for companies, with over 60% of stocks in the Index beating expectations. Nonetheless, the market is concerned about issues such as Brexit and President Trump's "tariff tantrum" with China. These, in combination with lower global GDP growth forecasts from the IMF and higher US interest rates, have caused stocks to deviate from their fundamental valuation.

The Information Technology sector was once again the top performing sector in the Fund for the quarter with Chinese travel software provider **Travelsky** and **Cadence Design Systems** outperforming the broader market. Despite the markets concerns over the strength of the Chinese economy and the effect of trade tariffs with the US, air traffic in and out of China is strong. Considering Travelsky's monopoly position in its domestic market, EPS growth which is faster than its global peers, and anticipated expansion in operating margins in 2019, we expect the stock to re-rate over the course of the year. Similarly, Cadence whose growth prospects are related to long term secular trends and greater economies of scale by moving part of its product portfolio to the cloud. Over the course of 2018, earnings expectations for that year and 2019 were revised upwards by c.20%. Given the positive secular outlook for the firm earnings for 2019, which are expected to grow by c. 7%, are likely to be revised upwards as the year progresses. The improved outlook is tied to better execution in the IP segment and robust demand for emulation software.

On the downside, high quality stocks such as **Cognex** have suffered from the deceleration of the growth rate of the automation sector. History suggests these downturns tend to be brief and shallow as this is a long-term secular trend. The stock is trading towards the lower end of its historic trading range having de-rated, but given the positive outlook for this sector and its oligopolistic position we have used this weakness to top-up our position. Importantly, its gross and operating margins are more like those of a software company than an industrial and it is debt free, so well positioned to benefit from any rebound in demand as the year develops.

SAMPLE PORTFOLIO TRANSACTIONS

The Fund made three disposals and one purchase over the quarter. **Idexx, LKQ** and **Azimut** were sold while **Medidata Solutions** was bought. We invested in Medidata as it's a cloud based electronic data capture and data management platform used in clinical trials. This system is being used to replace traditional paper-based clinical data management as increased regulation and complexity is driving the need for more efficient paperless framework. This means its revenues model has a high degree of visibility as 85% of revenues are subscription based with the remainder coming from professional services. It estimates there are c.150,000+ registered clinical trials underway globally and only 10% of these use dedicated software.

We took the opportunity to exit Idexx Laboratories Inc having made a c.70% return over the 18 months the Fund held the stock. It's a market leader for animal healthcare innovation, developing diagnostic, detection and information systems used in the veterinary (60% market share), livestock, water testing and dairy markets. Over 86% of revenues are from companion animals with livestock contributing 8% and water testing the remainder. This results in a very stable and visible revenue stream. Over the last 12 months we have been gradually exiting our position in LKQ. This company specialises in distributing reclaimed vehicle parts which cost 20-40% less than comparable new OEM parts. Although LKQ is high-cash generative, it is highly levered as it grows by acquisition and a rising interest rate environment is likely to be more challenging for its business model.

Markets for most of 2018 were surprisingly robust despite the rapidly evolving political environment, which caused them to fluctuate. The sell-off in the final quarter highlights once again the importance of investing in high quality businesses. Corporate earnings are expected to be positive for 4Q18 due to the positive effects of lower corporate taxes. Importantly for investors, equities are the cheapest they've been since 2013 and many of these negative headlines are likely to soften in 2019.

CALENDAR YEAR PERFORMANCE	2018 (%)	2017 (%)	2016 (%)	2015 (%)	2014 (%)
Davy Discovery Equity Strategy (Net of fees)	-10.7	14.2	10.0	13.5	14.7
MSCI World Small and Mid-Cap Index** (Total Return)	-13.2	23.5	10.4	0.4	4.1
TRAVELSKY TECHNOLOGY	-13.4	45.4	29.4	54.3	12.3
CADENCE DESIGN SYSTEMS	4.0	65.8	21.2	9.7	35.3
COGNEX CORP	-36.5	92.9	89.6	-17.9	8.3
LKQ CORP	-41.7	32.7	3.4	5.4	-14.5
IDEXX LABORATORIES	19.0	33.4	60.8	-1.6	39.4
AZIMUT HOLDING SPA	-32.9	6.2	-24.6	31.4	-5.7

Source: Davy Asset Management (Class A Acc Eur) and Bloomberg as at 31st December 2018. Performance is quoted in local currency unless otherwise stated.

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Warning: Past performance is not a reliable guide to future performance.

Warning: Neither past experience nor the current situation are necessarily accurate guides to the future growth in value or rate of return of the Fund. The value of the investment can reduce as well as increase and, therefore, the return on the investment will also be variable. Changes in exchange rates may have an adverse effect on the value price or income of the product.

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The Davy Discovery Equity Fund is a sub-fund of Davy Funds plc, an open-ended umbrella investment company with variable capital and segregated liability between sub-funds incorporated with limited liability under the Companies Acts 2014, authorised by the Central Bank of Ireland as a UCITS pursuant to the Regulations. Davy Funds plc is authorised by the Central Bank of Ireland as an Undertaking for Collective Investment in Transferrable Securities (UCITS). The Prospectus, Supplement and Key Investor Document for the fund are available in English from Davy, Davy House, 49 Dawson Street, Dublin 2, Ireland or http://www.davyassetmanagement.com/funds/davy-ucits/important-information.html. Investors should be aware that some of the Directors of the Company (Davy Funds plc) are also employed by the Investment Manager, Promoter and Distributor. Further information in relation to the management of potential conflicts of interest is available upon request.

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