**Portfolio Manager VIDEO**

Update from Portfolio Managers

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# Davis Select U.S. Equity ETF (DUSA)

Fall Review 2021

## Results

Since our firm's founding more than 50 years ago, we have built wealth through recessions and expansions, crashes and bubbles, fear and euphoria. Davis Select U.S. Equity ETF added to this record, increasing shareholder value by 17.42% thus far this year. ■

## Portfolio Outlook: Dispersion, Risk and Opportunity

In the five-year period culminating in June of last year (2020), the S&P 500 Index generated a compound annual return of roughly 11%. Importantly, this return masked a huge dispersion between two different investment approaches, most commonly described as growth and value. For example, over the same

***The average annual total returns for Davis Select U.S. Equity ETF periods ending June 30, 2021 are: NAV Return, 1 year, 52.28%; Inception (1/11/17), 14.62%; Market Price Return, 1 year, 52.35%; Inception, 14.67%. The performance presented represents past performance and is not a guarantee of future results.*** *Investment return and principal value will vary so that, when redeemed, an investor's shares may be worth more or less than their original cost. NAV prices are used to calculate market price performance prior to the date when the Fund was first publicly traded. Market performance is determined using the closing price at 4:00 pm Eastern time, when the NAV is typically calculated. Market performance does not represent the returns you would receive if you traded shares at other times. For the Fund's most recent month end performance, please call 800-279-0279 or visit www.davisetfs.com. The total annual operating expense ratio as of the most recent prospectus was 0.62%. The total annual operating expense ratio may vary in future years. Current performance may be lower or higher than the performance quoted. Due to market conditions the fund has experienced relatively high performance which may not be sustainable for the long term.*

This report includes candid statements and observations regarding investment strategies, individual securities, and economic and market conditions; however, there is no guarantee that these statements, opinions or forecasts will prove to be correct. Equity markets are volatile and an investor may lose money. All fund performance discussions within this piece are as of 7/31/21 unless otherwise noted. This is not a recommendation to buy, sell or hold any specific security. **Past performance is not a guarantee of future results. The Attractive Growth and Undervalued reference in this piece relates to underlying characteristics of the portfolio holdings. There is no guarantee that the Fund performance will be positive as equity markets are volatile and an investor may lose money.**

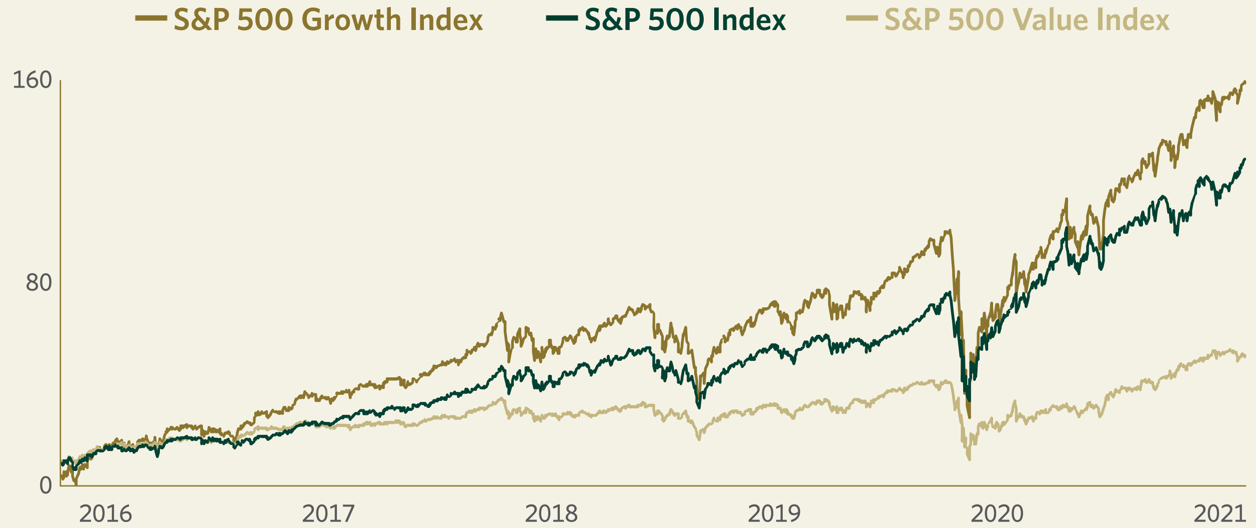
five-year period that the S&P 500 Index returned 11%, the growth component of the Index compounded at almost 15% per year, while the value component lagged growth by almost 900 basis points per year, returning only 6% per year.

As we wrote in our last report, "For active managers like us, (such) dispersions create opportunity for enhanced future returns (as)…this huge gap allowed us to trim positions in high fliers, while adding to durable growth businesses trading at bargain prices. By avoiding the speculative bubble of extreme valuations at one end of the market and instead owning resilient and proven growth businesses that can be purchased at bargain prices at the other end of the market, the portfolio is positioned with less risk and more relative upside than we have seen since the late 1990s."

Looking back, our analysis proved prescient, and we are pleased that the carefully selected companies that make up our portfolio appreciated more than 42% in the last 12 months, compared to 36% for the averages.[1] What's more, as can be seen in the chart below, despite the very strong performance of our portfolio, the overall dispersion between growth and value remains historically wide.

As a result, although the short-term direction of the market is unknowable, we would paraphrase Winston Churchill in characterizing our strong performance over the last 12 months as the end of the beginning, rather than the beginning of the end, of the opportunities and risks created by wide dispersion. ■

**Wide Dispersion Exists Between Growth and Value[2]**




**1.** Based on the Fund's return vs. the S&P 500 Index for 7/31/20–7/31/21. **2.** Source: Davis Selected Advisers.

## Selectivity, Growth *and* Value

Our ability to take advantage of this dispersion derives from our willingness to be highly selective. Selectivity means that we invest in fewer than one out of every 15 companies included in the S&P 500 Index. Just as with the best universities or best companies, the ability to select from a large pool of applicants creates the opportunity to choose only the most exceptional candidates and reject those that are average or worse. Our research efforts comb through hundreds of potential investments, seeking those whose business and financial characteristics can turn long-term investments into compounding machines.

In particular, we look for durable, growing businesses that can be purchased at attractive valuations and reject businesses that generate low returns, are stagnant, overvalued, overleveraged or competitively disadvantaged. While funds that passively mirror the S&P 500 Index are forced to invest in all companies, including those that we view as significantly overvalued or competitively challenged, our selective approach allows us to reject such companies. In this environment of wide dispersions, the ability to selectively reject certain companies and sectors from our portfolio may prove just as valuable as the ability to selectively invest in others.

While the growth/value categorization discussed above is helpful in illustrating both mania and opportunity, the best way to build wealth is by finding those select few businesses that combine the best characteristics of both categories. After all, categories do not build wealth. Nor do average businesses. Instead, generational wealth is built by investing in those select few businesses that combine durable and resilient growth with attractive valuations.

As can be seen in the table above, by being extremely selective, we have built a portfolio that has the best of both growth *and* value. While the earnings of our portfolio companies have grown more than 4% per year faster than average, they can currently be purchased at a 46.5% discount to the average. We consider this a value investor's dream, as companies that grow profitably over time are more valuable than companies that don't.

**Selective, Attractive Growth, Undervalued[3]**

| | Fund | Index |
|---|---|---|
| Holdings | 25 | 505 |
| EPS Growth (5 Year) | 23.8% | 19.6% |
| P/E (Forward) | 11.6x | 21.7x |

To find such an attractive combination, our research goes beyond simplistic categories to identify growth businesses with attractive valuations, as well as value businesses with attractive growth. ■

## Undervalued Growth

Within the traditional growth category, growing euphoria has led to bubble prices for many companies, most especially those with new and unproven business models. In contrast, our research focuses on a select handful of proven growth stalwarts whose shares still trade at reasonable valuations. For example, because of concerns about future litigation and regulation, several dominant internet businesses, including Amazon, Google and Facebook, trade at steep discounts to many unproven and unprofitable growth darlings that, in our view, trade at euphoric prices. While we expect a continued barrage of negative headlines around these names, as well as increased regulation in the years ahead, we do not expect a significant decline in their long-term profitability.

We have also found opportunities to buy proven growth companies at attractive prices by looking overseas, particularly at companies such as Alibaba and Naspers that serve and entertain the fast-growing and enormous Chinese middle class. While recent actions by the Chinese government significantly impaired the value of several of our education holdings, the government's long-term record of promoting economic growth and stability remains among the best in modern history. As of this writing, we believe that the government targeted the education sector for specific policy reasons and that these actions do not indicate a significant change in economic priorities.

Finally, we have found bargain-priced growth companies in less glamorous parts of the technology ecosystem. Like the manufacturers of picks and shovels during the Gold Rush, outstanding companies such as Intel

**3.** Source: Davis Selected Advisers.

and Applied Materials generate wonderful profits manufacturing the underlying hardware that enables such exciting but speculative new fields as self-driving cars, cloud computing, artificial intelligence, machine learning, software as a service and the internet of things. ■

## Growing Value

In the same way our research focuses on durable growth companies that are not overvalued, we also seek out value companies capable of long-term growth. In doing so, we seek to avoid risks inherent in companies that we would classify as value traps or speculative value. While the shares of such companies may trade at cheap prices, their businesses are often fragile, impaired, prone to disruption or highly sensitive to the timing of an economic recovery. Decades of experience have taught us the dangers of owning weak businesses unable to withstand unexpected shocks, even if they sell at cheap prices. Although such speculative gambles may hit from time to time, poor businesses do not build generational wealth. Instead, our attention within the value part of the market remains steadfastly focused on companies that combine strength and resiliency with long-term growth, profitability and competitive advantages. In today's uncertain economy, select financials represent the best combination of proven durability and low valuations.

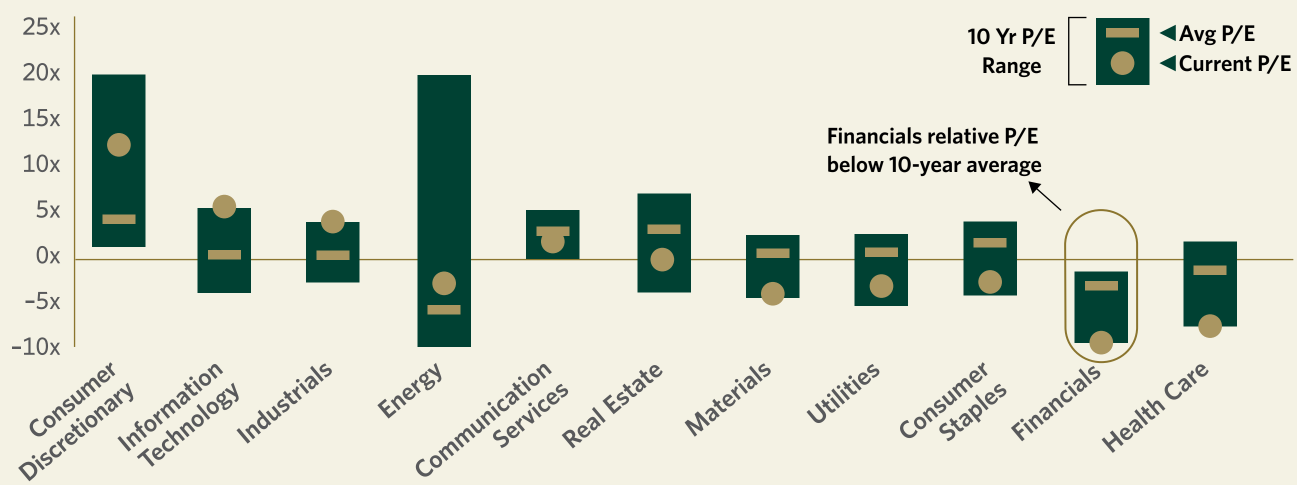
As the pandemic unfolded, panicked sellers abandoned the banking sector, making it one of the worst-performing areas of the market, despite the fact that banks entered this downturn with record high levels of capital and extremely conservative loan portfolios. As a result, we purchased or added to select well-capitalized financial leaders, such as Wells Fargo and U.S. Bancorp, all of whom were able to build enormous reserves for loan losses while still remaining profitable. With the pandemic now moving into the rearview mirror, some of the charges taken to build reserves are being reversed, further adding to profitability.

The combination of growing profitability and lagging prices was not just a 2020 phenomenon. In fact, over the last decade, during which the earnings of financials grew from 15% to more than 20% of the S&P 500 Index, their prices have fallen from roughly 18% to a record low 12% of the Index. This disconnect between price and value creates the significant opportunity that we have positioned for today.

Although bank stocks have enjoyed a sharp recovery from last year's panic-induced lows, investors need not worry that they missed an opportunity. As can be seen in the chart below, financials remain the cheapest sector in the market. What's more, the current valuation of the financial sector is low, not just relative to the market, but even relative to its own historic discount.

**Financials Are Attractively Priced[4]**

Relative P/E for S&P 500 Sectors




**4.** Source: Credit Suisse as of 4/22/21.

Given the strength that the sector demonstrated in remaining profitable through such a challenging year, we believe that investors' attitudes towards the sector are poised for change, leading to an increase in their relative valuation and a sharp closing of this enormous discount.

Beyond financials, our selectivity and willingness to look beyond simplistic definitions and categories has led to a portfolio that includes growth companies at value prices and value companies with long-term growth. As a result, the portfolio is both growing and undervalued. This rare combination positions us to build on DUSA's recent outperformance in the years and decades ahead. ■

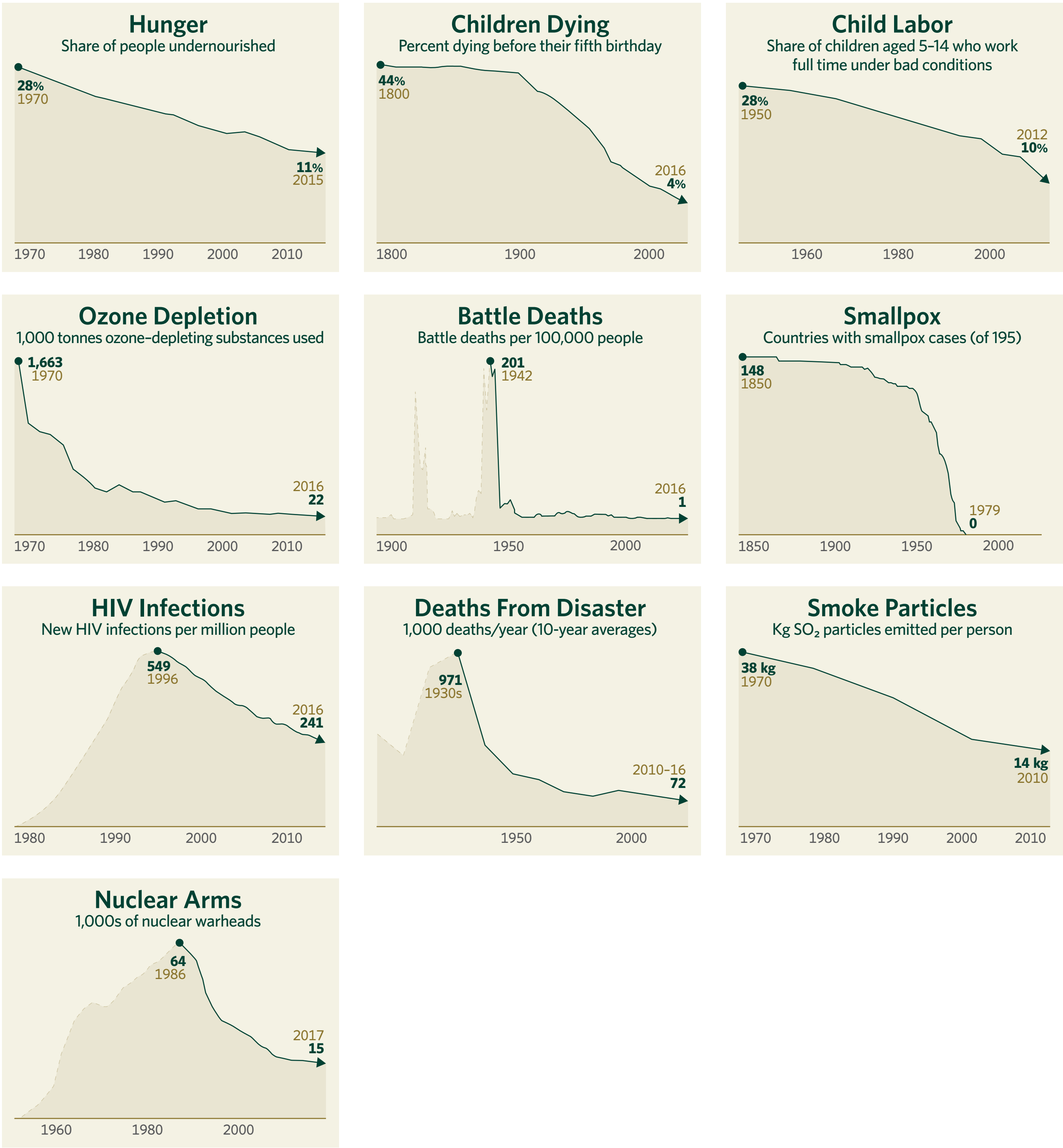
## Conclusion

While the pandemic of 2020 extracted an awful toll on so many families, it also highlighted the inventiveness, creativity and ingenuity of our society. From e-commerce to biotechnology, 2020 was a year of explosive innovation, adaptability and resiliency and a powerful reminder of two seemingly contradictory investment truths.

First, unexpected bad things can and will happen. Over our firm's history, we have navigated countless awful and unexpected crises including the energy crisis, the hostage crisis, the inflation crisis, 9/11, the financial crisis, the COVID crisis and the ongoing climate crisis. As fiduciaries, we must incorporate both expected and unexpected challenges and crises into every aspect of our investment process.

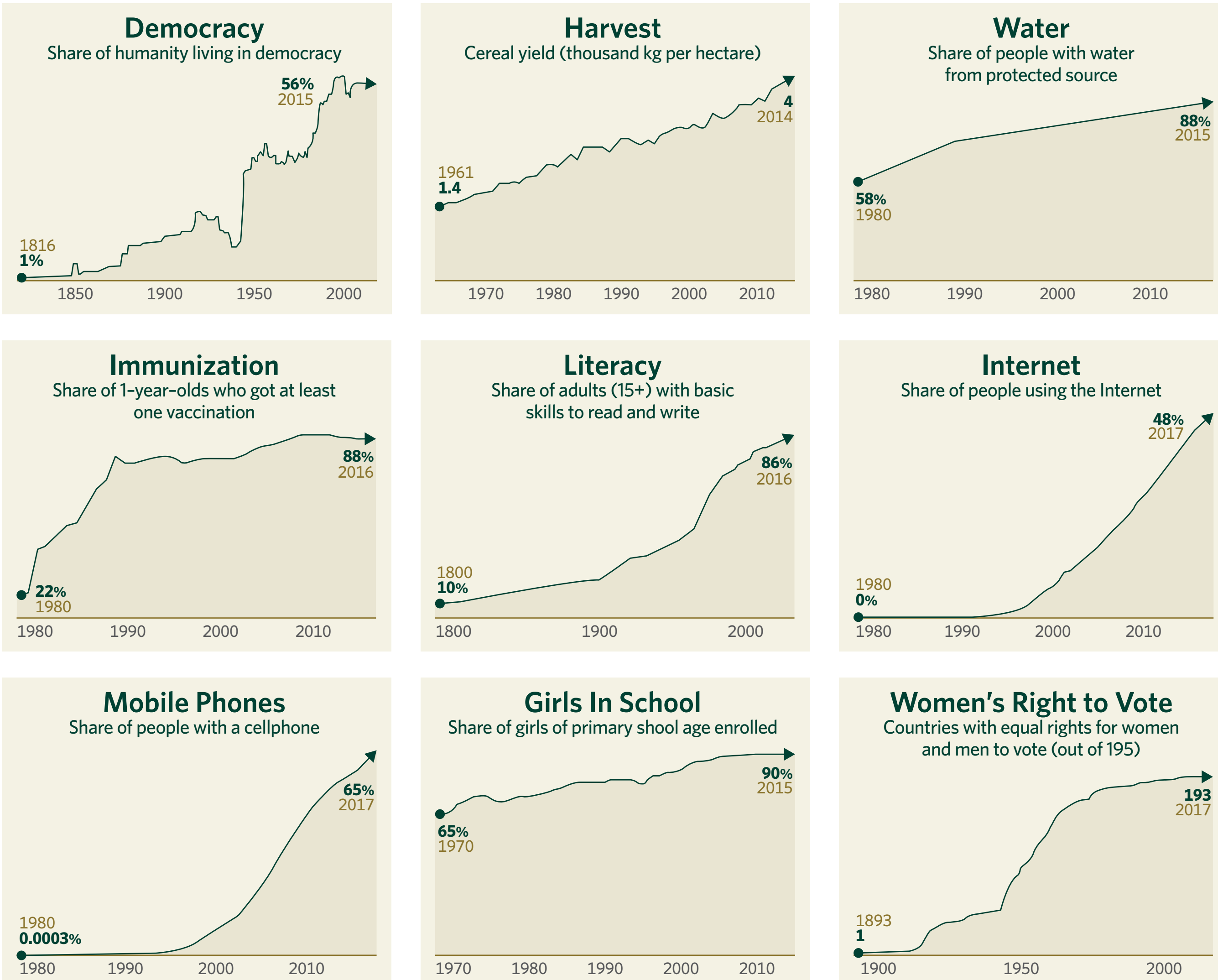
Second, we must also recognize the incredible power of innovation and invention. In the early stages of the pandemic, the most optimistic forecasts called for a vaccine in three-to-five years. And yet, scientists developed one in a matter of months. Similarly, over the longer term, human ingenuity has led to stunning progress in addressing a vast range of horrific global challenges. The graphs on the following pages offer a compelling if incomplete quantitative picture of this progress.

## Bad Things Have Been Declining[5]




**5.** Source: https://www.gapminder.org/factfulness-book/32-improvements/

## Good Things Have Been Increasing[5]




Betting against progress has been a losing proposition.

Thus, we believe that our portfolio companies have the durability and strength to withstand unexpected shocks and crises, we also select those that also have the ability to innovate, adapt and build wealth in an ever-changing and unpredictable world.

With more than $2 billion of our own money invested alongside clients, our interests are aligned, and our conviction is more than just words.[6] This alignment is an uncommon advantage, given that 88% of all funds are overseen by managers who have less than $1 million invested alongside their clients.

Although our investment discipline may not be rewarded by the market over shorter periods, our proven active management approach has built wealth for our shareholders over many decades.

We value the trust you have placed in us and look forward to continuing our investment journey together. ■

**6.** As of 6/30/21 Davis Advisors, the Davis family and Foundation, its employees, and Fund directors have more than $2 billion invested alongside clients in similarly managed accounts and strategies.

*This report is authorized for use by existing shareholders. A current Davis Select U.S. Equity ETF prospectus must accompany or precede this material if it is distributed to prospective shareholders. You should carefully consider the Fund's investment objective, risks, fees, and expenses before investing. Read the prospectus carefully before you invest or send money.*

Shares of DUSA are bought and sold at market price (not NAV) and are not individually redeemed from the ETF. There can be no guarantee that an active trading market for ETF shares will develop or be maintained, or that their listing will continue or remain unchanged. Buying or selling ETF shares on an exchange may require the payment of brokerage commissions and frequent trading may incur brokerage costs that detract significantly from investment returns.

This report includes candid statements and observations regarding investment strategies, individual securities, and economic and market conditions; however, there is no guarantee that these statements, opinions or forecasts will prove to be correct. These comments may also include the expression of opinions that are speculative in nature and should not be relied on as statements of fact.

Davis Advisors is committed to communicating with our investment partners as candidly as possible because we believe our investors benefit from understanding our investment philosophy and approach. Our views and opinions include "forward-looking statements" which may or may not be accurate over the long term. Forward-looking statements can be identified by words like "believe," "expect," "anticipate," or similar expressions. You should not place undue reliance on forward-looking statements, which are current as of the date of this report. We disclaim any obligation to update or alter any forward-looking statements, whether as a result of new information, future events, or otherwise. While we believe we have a reasonable basis for our appraisals and we have confidence in our opinions, actual results may differ materially from those we anticipate.

**Objective and Risks.** Davis Select U.S. Equity ETF's investment objective is long-term capital growth and capital preservation. There can be no assurance that the Fund will achieve its objective. The Fund invests primarily in equity securities issued by large companies with market capitalizations of at least $10 billion. Some important risks of an investment in the Fund are: stock market risk; **common stock risk; market trading risk:** includes the possibility of an inactive market for Fund shares, losses from trading in secondary markets, periods of high volatility, and disruptions in the creation/redemption process. **ONE OR MORE OF THESE FACTORS, AMONG OTHERS, COULD LEAD TO THE FUND'S SHARES TRADING AT A PREMIUM OR DISCOUNT TO NAV; exchange-traded fund risk:** the Fund is subject to the risks of owning the underlying securities as well as the risks of owning an exchange-traded fund generally; **focused portfolio risk:** investing in a limited number of companies causes changes in the value of a single security to have a more significant effect on the value of the Fund's total portfolio; **financial services risk; foreign country risk; headline risk; large-capitalization companies risk; manager risk; authorized participant concentration risk:** to the extent that Authorized Participants exit the business or are unable or unwilling to proceed with creation and/or redemption orders with respect to the Fund and no other Authorized Participant is able to step forward to create or redeem Creation Units, Fund shares may trade at a discount to NAV and could face delisting; **cybersecurity risk:** a cybersecurity breach may disrupt the business operations of the Fund or its service providers; **depositary receipts risk:** depositary receipts involve higher expenses and may trade at a discount (or premium) to the underlying security; **fees and expenses risk; foreign currency risk; intraday indicative value risk:** the Fund's INAV agent intends to disseminate the approximate per share value of the Fund's published basket of portfolio securities every 15 seconds. The IIV should not be viewed as a ''real-time'' update of the NAV per share of the Fund because the IIV may not be calculated in the same manner as the NAV, the calculation of NAV may be subject to fair valuation at different prices, the IIV does not take into account Fund expenses, and the IIV calculations are based on local market prices and may not reflect events that occur subsequent to the local market's close; and **mid- and small-capitalization companies risk.** See the prospectus for a complete description of the principal risks.

The information provided in this material should not be considered a recommendation to buy, sell or hold any particular security. As of 6/30/21, the top ten holdings of Davis Select U.S. Equity ETF were: Capital One Financial, 12.17%; Alphabet, 10.50%; Berkshire Hathaway, 7.70%; Amazon.com, 7.56%; Wells Fargo, 5.97%; Facebook, 4.89%; DBS Group, 4.47%; Alibaba Group, 4.43%; American Express, 4.15%; U.S. Bancorp, 3.83%

Davis Fundamental ETF Trust has adopted a Portfolio Holdings Disclosure policy that governs the release of non-public portfolio holding information. This policy is described in the prospectus. Holding percentages are subject to change. Visit davisetfs.com or call 800-279-0279 for the most current public portfolio holdings information.

**Forward Price/Earnings (Forward P/E) Ratio** is a stock's current price divided by the company's forecasted earnings for the following 12 months. The values for the portfolio and index are the weighted average of the p/e ratios of the stocks in the portfolio or index.

**Five-Year EPS Growth Rate** is the average annualized earning per share growth for a company over the past five years. The values for the portfolio and index are the weighted average of the five-year EPS Growth Rates of the stocks in the portfolio or index.

**Bps** stands for Basis Points. One basis point = 0.01%.

We gather our index data from a combination of reputable sources, including, but not limited to, Lipper, Wilshire, and index websites.

The **S&P 500 Index** is an unmanaged index of 500 selected common stocks, most of which are listed on the New York Stock Exchange. The index is adjusted for dividends, weighted towards stocks with large market capitalizations and represents approximately two-thirds of the total market value of all domestic common stocks. The **S&P 500 Value Index** represents the value companies of the S&P 500 Index. The **S&P 500 Growth Index** represents the growth companies of the S&P 500 Index. Investments cannot be made directly in an index.

After 10/31/21, this material must be accompanied by a supplement containing performance data for the most recent quarter end.

**Shares of the Davis Fundamental ETF Trust are not deposits or obligations of any bank, are not guaranteed by any bank, are not insured by the FDIC or any other agency, and involve investment risks, including possible loss of the principal amount invested.**

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