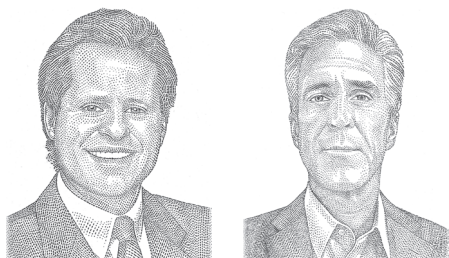




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Update from Portfolio Managers  
Andrew A. Davis and Chandler Spears

## Davis Real Estate Fund

Semi-Annual Review 2025

### Key Takeaways

- Davis Real Estate Fund (DREF) declined –1.79% in the first half of 2025 compared to a return of +1.74% for the Wilshire U.S. Real Estate Securities Index.
- Uncertainties about tariff policy and government spending cuts combined with the existing over-supply problem have undermined many sectors of the property market, not the least industrials, offices, life sciences and apartments.
- Recently we have seen the supply situation swinging back forcefully towards property owners in several sectors simultaneously, which is unique. The improvement looks durable, and, absent some policy-induced calamity, the fund is well-positioned to claw back performance.

Davis Real Estate Fund's (DREF) Class A shares provided a total return on net asset value of –1.79% for the six months ended June 30, 2025. Over the same period the Wilshire U.S. Real Estate Securities

Index returned +1.74%. During the most recent one-, five- and 10-year periods, a \$10,000 investment in Davis Real Estate Fund would have returned \$10,458, \$13,458 and \$16,744, respectively.

**The average annual total returns for Davis Real Estate Fund's Class A shares for periods ending June 30, 2025, including a maximum 4.75% sales charge, are: 1 year, –0.39%; 5 years, 5.09%; and 10 years, 4.78%. The performance presented represents past performance and is not a guarantee of future results.** Total return assumes reinvestment of dividends and capital gain distributions. 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. For most recent month-end performance, visit [davisfunds.com](https://davisfunds.com) or call 800-279-0279. Current performance may be lower or higher than the performance quoted. The total annual operating expense ratio for Class A shares as of the most recent prospectus was 1.02%. The Adviser is contractually committed to waive fees and/or reimburse the Fund's expenses to the extent necessary to cap total annual fund operating expenses of Class A shares at 1.00%. For purposes of this expense cap, operating expenses do not include foreign tax reclaim filing expenses. The expense cap expires May 1, 2026. The total annual operating expense ratio may vary in future years. Returns and expenses for other classes of shares will vary.

This material 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. All fund performance discussed within this material refers to Class A shares without a sales charge and are as of 6/30/25, 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 material 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.**

DREF has not had a good year nor even a good couple of years. Prospect theory, for those who may be interested, suggests investors facing potential losses tend to become more risk-seeking. However, instead of genuflecting to the behavioral bias of altering our risk tolerance in the face of underperformance, we are staying true to our methods. The Davis Investment Discipline has over long durations helped us generate attractive risk-adjusted returns. Even though we are in a bad stretch now, we are optimistic that better performance lies ahead. ■

## Building Conviction

This year investors have had no shortage of complexity to face when building the conviction necessary to deploy capital. Despite variables that appear to be intractable, however, often it is the simplest of economic principles that illuminates the way. As we try to digest the evolving landscape of “uncertain uncertainties” (our post-Liberation Day turn of phrase), we try to remain focused on the one thing that to us provides a basis for reliable forecasts: supply.

Long-time investors in DREF know that we often lean into this narrative, though typically to explain our positioning within a given sector. Today is rather unique in that we see the supply situation in several property sectors simultaneously swinging forcefully in the direction of property owners.

That may sound optimistic to anyone who spends any time reading press reports. For several years now it has been easy for journalists to trumpet that the country has too many offices, surplus industrial space and historical levels of new apartment deliveries, particularly in the Sunbelt markets. Generally speaking, they have been correct. The low-rate environment in the years leading up to the pandemic,

and the even lower rate environment during the pandemic, led to a boom in construction. COVID-fueled demand for delivered goods and a workforce that remained largely employed powered strong absorption in the industrial and apartment sectors. That invited even more construction, and for several years inventory additions piled up.

Office, on the other hand, has been in a multi-year funk. First, we saw demand fall away under work-from-home stubbornness. Then, when demand finally returned, employers made a concerted effort to use lease renewal opportunities to reposition their workforces into smaller spaces in the most premier buildings. That is, the oversupply situation in office had less to do with new construction, though there has been some, than with a downdraft in demand. The end result is the same, however.

The evolution of supply over the past several years provides a convenient backdrop to discuss recent performance given that it is integral to understanding what went wrong. The nascent recovery in the supply outlook, meaning less of it, allows us to frame why many of the stocks that have hurt performance recently are some of our favorites looking forward. ■

## What's Worked, and What Hasn't

The year got off to a good start for DREF but it was derailed by unexpected policy actions coming out of Washington, D.C. Liberation Day, as it's come to be known, ushered in tariff regimes that were far beyond what most expected. The fund could not have been more ill-suited for this outcome, given its overweight position in industrial. In a nutshell, policy actions colluded with heavy supply to hobble the fund's investments in apartments and life science.

Let's begin with the tariffs. The consensus seems to be that tariffs will curtail demand for industrial space as imports decline. It is further believed that tariffs will prove inflationary, compounding the decline in space demand as consumers buckle under higher prices. We agree with both those assessments. What we did not envision as a likely outcome was the extent to which the Trump administration would pursue tariff policy. To our mind, weighted average tariff rates would end up in the mid-teens. (We still believe that, though it will likely take a while to get there.) The "supermax" regime that ended up being floated was 10-fold our expectation and, consequently, industrial REITs became the obvious sell.

For DREF's largest overweight, Rexford Industrial, tariff machinations have proven particularly painful. That's because its only market, southern California, is the most frequently used port for goods inbound from China. It is also a market where supply has become a sticking point, though a keen eye will note most of the pain is in the eastern submarkets where Rexford has a *de minimis* position. Most frustrating of all is that, but for the tariffs, we might have been reporting how industrial REITs buoyed performance this year. Prior to Liberation Day, industrial fundamentals were inflecting with much improved pricing and absorption. Now tenants are content to sit on their hands. Apart from EastGroup Properties, whose ownership of shallow-bay industrial in Sunbelt markets has proven relatively resilient, all DREF's industrial holdings have been a drag on performance.

No commercial property sector has suffered more inventory additions (as a percentage of existing stock) than the apartment sector. The situation has been most acute in many Sunbelt markets where impediments to new construction are far less onerous than in most coastal markets. Inventory

growth in a few metro areas reached historic growth rates over the past couple of years. If not for the surprisingly strong employment market that has helped absorption remain steady, the fund's considerable holdings in apartment REITs might have dampened performance far more than they did.

*"Davis Real Estate Fund has had notable success with its investments in tower infrastructure. We've long held that the cash flow stability of this business is underappreciated, and that it is myopic to fixate on towers as a simple inverse interest rate play."*

Alexandria Real Estate has also been bruised by new policy actions. The Trump administration seems intent on eliminating wasteful spending and in so doing has fouled the gears of life science funding. This is proving problematic for Alexandria, the leading landlord for life science companies in the U.S. It's not its current tenants that are being materially compromised. Most of those are many funding rounds beyond needing U.S. government support. Rather, it's the incremental demand that arises when incumbent tenants expand their reach by *de novo* product development or by acquiring newly formed companies. Almost 90% of Alexandria's incremental leasing comes from its existing tenancy.

The unfavorable supply backdrop worsens matters for Alexandria. Its life science properties, while nominally office in appearance, are really lab buildings. That proved highly desirable during the pandemic when massive amounts of capital were channeled into drug development. It was a virtuous environment. However, liberal construction lending practices and an influx of competition

saw new construction sprout in Alexandria's most important markets. Incremental leasing among life science tenants has all but stopped, with only the cadence of renewals providing any leasing velocity. Consequently, Alexandria has been DREF's single worst performer this year.

Conversely the fund has had notable success with its investments in tower infrastructure. We've long held that this business' cash flow stability is underappreciated, and that it is overly myopic to regard towers as a simple inverse interest rate play. In fairness, declining interest rates have helped sentiment, but the capital expenditure plans that wireless carriers announced earlier this year suggest an improving demand environment for cell towers. That's the real story.

Two office REITs located in the United Kingdom also provided a boost to performance. Great Portland Estates and Derwent London each specialize in premier office accommodation in the city of London. Their conditions are not just similar to the Grand Central submarket in New York City, the U.S.'s best office market, but are actually better. In many respects the supply-demand balance in prime U.K. office space is ahead of the best markets in the U.S. Investors are clearly warming to the U.K. office market and performance has been very good this year. Even so, valuations remain depressed, not only relative to their history but, pronouncedly so, relative to the valuation of U.S. office REITs.

Investments in seniors housing also aided performance in the first half. It is important to recognize we have been underweight this sector for a while due to extreme valuation. So even though our two holdings in this sector helped absolute performance, their considerable size in the benchmark versus the fund's underweight position

cost us relative performance. It's not that we don't appreciate the ongoing recovery in seniors housing post-pandemic. Rather, the extreme multiples at which these businesses trade is inconsistent with any reasonable growth trajectory over the next several years. It is our belief that the market's indifference to valuation in this sector is driven in part by a fear of other sectors facing greater headline risk. We simply aren't willing to chase richly priced seniors housing stocks simply for the appearance of being safe. ■

## **Outlook:** **Improving Supply Backdrop**

As we consider how Davis Real Estate Fund is positioned, we accept that the road from here to eventual outperformance will be a rocky one. There are simply too many unknowns. Over the long term, however, the improving supply backdrop we mentioned earlier is likely to prove durable, and at least more long-lived than the current administration. Absent some policy-induced calamity, the fund is very well-positioned to claw back performance and, hopefully, exceed even that.

We continue to believe the office sector is being unfairly maligned and deserves to trade at much higher multiples. The "return to office" narrative is essentially dead, as it should be for anyone with even a modicum of understanding of the deeper texture of office demand. Office REITs are beginning to report meaningful leasing traction and rents are inflecting higher. Factor in a rapidly improving supply picture for the sort of office space most in demand and it's easy to feel sanguine about our overweight in this sector. This line of thinking also extends to the fund's U.K. office holdings, by the way.

The deflating supermax tariff regime that hobbled performance of our industrial holdings does not alter our long-term stance on the sector. Valuations discount some rather extreme outcomes that we don't view as highly probable, though our underwriting remains very conservative to account for those wide outcomes. We hold several industrial REITs in the fund, ranging from unique shallow-bay industrial in fast-growing Sunbelt markets to massive intermodal facilities. However, our largest overweight investment in the sector continues to be Rexford Industrial. Supply remains an overhang on sentiment (although it's not as severe as headlines may suggest), but in time we expect pricing power will swing back in favor of Rexford's "last-touch" properties. We may be early to the recovery, but we are being paid to wait with an above-average dividend yield backed by a fortress balance sheet and a management team up to the challenge.

*"Sunstone has an under-levered balance sheet, owns a small portfolio of highly desirable hotels and lacks impediments common among companies with entrenched management. Despite all this, we hold it as a going concern."*

Apartments remain a favorite, too. Demand has proven far more resilient than we expected, buffering a potentially damaging blow to market rents during a period when inventory additions were at peak levels. Absent a serious recession we expect even muted employment gains to be sufficient to drive solid rent increases if, as expected, new deliveries drop significantly through the middle of 2026. Starts have been in a steady decline for a couple of years now so we see no realistic scenario where supply could reaccelerate in time

to jeopardize what should be a favorable leasing environment for apartment owners over the next couple of years. To us, the sector is "spring-loaded."

Ric Campo, CEO of Camden Properties, the fund's largest Sunbelt apartment holding, shares this view. During a recent earnings call he said, "... when they turn, they're going to turn hard, hard up and high to the right." He was characterizing potential future operating conditions in the Nashville and Austin apartment markets, two markets with the greatest inventory growth over the past couple of years. We believe his comments can apply to many apartment markets in the U.S., and we continue to like our positioning in Sunbelt apartment REITs.

Lastly, there are two other notable positions that deserve discussion. The first is Alexandria Real Estate, which has been in the fund at some level for the current management's entire career. It has suffered under the pressure of excess supply for several years now. Then, early this year, it received a haymaker from the Trump administration's near cessation of life science funding. Our position on Alexandria in early 2024 was that supply would reach equilibrium sooner rather than later. With recent policy actions it is likely to take longer for fundamentals to stabilize, two to three years by the company's own admission. We strongly believe in Alexandria's franchise and are willing to wait for the tide to turn in its favor. In the meantime, the better than 7.5% dividend yield compensates us for being patient with this deeply discounted stock.

Secondly, we've never invested based solely on the likelihood of M&A, but Sunstone, the fund's only hotel holding, is most definitely a candidate for takeout. In late 2024 there was a rumor of a potential bid for the company that never came to pass. Its attractiveness to others is understandable.

Sunstone has an underleveraged balance sheet, owns a small portfolio of highly desirable hotels and lacks impediments common among companies with entrenched management. Despite all this, we hold it as a going concern. The stock has performed poorly due to a drop in leisure travel and the delayed delivery of a repositioned hotel in south Florida. However, we believe it is poised to meaningfully accelerate earnings this year and next. Additionally, in a show of commitment to the company's inherent value proposition, management has been jettisoning the lowest quality assets to purchase Sunstone's own stock, and doing so at a valuation arbitrage. That means it is selling assets at valuations higher than the valuation at which the

company's repurchased stock is trading. At some point Sunstone's depressed valuation is going to become too great for investors to ignore or else the acquisition vultures will likely begin circling again.

For more than 50 years at Davis Advisors we have navigated a constantly changing investment landscape guided by one North Star: to grow the value of the funds entrusted to us. We are pleased to have achieved strong results thus far and look forward to the decades ahead. With more than \$2 billion of our own money invested in our portfolios, we stand shoulder to shoulder with our clients on this long journey.<sup>1</sup> We are grateful for your trust and are well-positioned for the future. ■

<sup>1</sup>. As of 6/30/25, Davis Advisors, the Davis family and Foundation, our employees, and Fund directors have more than \$2 billion invested alongside clients in similarly managed accounts and strategies.

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**Objective and Risks.** The investment objective of Davis Real Estate Fund is total return through a combination of growth and income. There can be no assurance that the Fund will achieve its objective. Some important risks of an investment in the Fund are: **stock market risk:** stock markets have periods of rising prices and periods of falling prices, including sharp declines; **common stock risk:** an adverse event may have a negative impact on a company and could result in a decline in the price of its common stock; **real estate risk:** real estate securities are susceptible to the many risks associated with the direct ownership of real estate, such as declines in property values and increases in property taxes; **headline risk:** the Fund may invest in a company when the company becomes the center of controversy. The company's stock may never recover or may become worthless; **large-capitalization companies risk:** companies with \$10 billion or more in market capitalization generally experience slower rates of growth in earnings per share than do mid- and small-capitalization companies; **manager risk:** poor security selection may cause the Fund to underperform relevant benchmarks; **fees and expenses risk:** the Fund may not earn enough through income and capital appreciation to offset the

operating expenses of the Fund; **mid- and small-capitalization companies risk:** companies with less than \$10 billion in market capitalization typically have more limited product lines, markets and financial resources than larger companies, and may trade less frequently and in more limited volume; and **variable current income risk:** the income which the Fund pays to investors is not stable. 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 6/30/25, the top ten holdings of Davis Real Estate Fund were: American Tower, 6.26%; BXP, 4.35%; Prologis, 4.33%; Cousins Properties, 4.31%; Ventas, 4.22%; Brixmor Property Group, 4.18%; Rexford Industrial Realty, 4.01%; Equinix, 4.01%; Digital Realty Trust, 3.71%; and AvalonBay Communities, 3.57%.

Davis Funds has adopted a Portfolio Holdings Disclosure policy that governs the release of non-public portfolio holding information. This policy is described in the Statement of Additional Information. Holding percentages are subject to change. Visit [davisfunds.com](http://davisfunds.com) or call 800-279-0279 for the most current public portfolio holdings information.

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The **Wilshire U.S. Real Estate Securities Index** is a broad measure of the performance of publicly traded real estate securities, such as Real Estate Investment Trusts (REITs) and Real Estate Operating Companies (REOCs). The index is capitalization-weighted. The beginning date was 1/1/78, and the index is rebalanced monthly and returns are calculated on a buy and hold basis. Investments cannot be made directly in an index.

After 10/31/25, this material must be accompanied by a supplement containing performance data for the most recent quarter end.