

Palos Equity Income Fund

Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)



Independent auditor's report

To the Unitholders and Trustee of Palos Equity Income Fund (the Fund)

Our opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2023 and 2022, and its financial performance and its cash flows for the years then ended in accordance with IFRS Accounting Standards as issued by the International Accounting Standards Board (IFRS Accounting Standards).

What we have audited

The Fund's financial statements comprise:

- the statements of financial position as at December 31, 2023 and 2022;
- the statements of comprehensive income (loss) for the years then ended;
- the statements of changes in net assets attributable to holders of redeemable units for the years then ended;
- the statements of cash flows for the years then ended; and
- the notes to financial statements, comprising material accounting policy information and other explanatory information.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the Fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information comprises the Management Report of Fund Performance and the information, other than the financial statements and our auditor's report thereon, included in the annual report.

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Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS Accounting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.



As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers LLP¹

Montréal, Quebec
March 28, 2024

¹ CPA auditor, public accountancy permit No. A125840

Palos Equity Income Fund

Statements of Financial Position

As at December 31, 2023 and 2022

(expressed in Canadian dollars)

	2023 \$	2022 \$
Assets		
Current assets		
Investments at fair value through profit or loss (FVTPL)	26,886,369	26,643,435
Cash	412,620	107,456
Accrued income receivable	121,536	100,952
Subscription receivable	5,225	-
Other assets	4,161	-
	<u>27,429,911</u>	<u>26,851,843</u>
Liabilities		
Current liabilities		
Distributions payable	113,638	17,069
Accrued liabilities	51,423	66,675
Management fees payable	1,472	-
	<u>166,533</u>	<u>83,744</u>
Net assets attributable to holders of redeemable units	<u>27,263,378</u>	<u>26,768,099</u>
Net assets attributable to holders of redeemable units per series		
Series A	21,010,350	20,332,452
Series F	6,253,028	6,435,647
	<u>27,263,378</u>	<u>26,768,099</u>
Net assets attributable to holders of redeemable units per series per unit		
Series A	6.74	6.51
Series F	7.34	7.05

Approved by the Manager, Palos Management Inc.

(s) Alain Lizotte

Director

(s) Philippe Marleau

Director

The accompanying notes are an integral part of these financial statements.

Palos Equity Income Fund
Statements of Comprehensive Income (Loss)
For the years ended December 31, 2023 and 2022

(expressed in Canadian dollars)

	Note	2023 \$	2022 \$
Income			
Dividend income		776,571	653,414
Interest income for distribution purposes		145,136	148,041
Net realized gain on sale of investments		1,450,626	428,539
Net change in unrealized appreciation (depreciation) of investments		414,390	(3,095,559)
		<u>2,786,723</u>	<u>(1,865,565)</u>
Expenses			
Management fees	8	413,642	419,297
Administration and other professional fees		96,404	92,965
Legal fees		39,964	64,687
Audit fees	5	58,707	49,366
Transaction cost	9	50,613	44,004
Bank charges and interest		37,977	24,782
Trustee fees		13,834	13,834
Independent review committee fees		12,001	12,001
Withholding tax expense		-	768
		<u>723,142</u>	<u>721,704</u>
Increase (decrease) in net assets attributable to holders of redeemable units		<u>2,063,581</u>	<u>(2,587,269)</u>
Increase (decrease) in net assets attributable to holders of redeemable units per series			
Series A		1,521,977	(1,963,651)
Series F		541,604	(623,618)
		<u>2,063,581</u>	<u>(2,587,269)</u>
Increase (decrease) in net assets attributable to holders of redeemable units per unit			
Series A	10	0.49	(0.63)
Series F		0.64	(0.66)

The accompanying notes are an integral part of these financial statements.

Palos Equity Income Fund

Statements of Changes in Net Assets Attributable to Holders of Redeemable Units

For the years ended December 31, 2023 and 2022

(expressed in Canadian dollars)

	Net assets attributable to holders of redeemable units, beginning of year \$	Proceeds from redeemable units issued \$	Redemption of redeemable units \$	Distributions to holders of redeemable units* \$	Reinvestment of distribution to holders of redeemable units \$	Increase (decrease) in net assets attributable to holders of redeemable units \$	Net assets attributable to holders of redeemable units, end of year \$
December 31, 2023							
Series A	20,332,452	1,119,340	(1,852,114)	(837,502)	726,197	1,521,977	21,010,350
Series F	6,435,647	230,166	(907,614)	(264,166)	217,391	541,604	6,253,028
	<u>26,768,099</u>	<u>1,349,506</u>	<u>(2,759,728)</u>	<u>(1,101,668)</u>	<u>943,588</u>	<u>2,063,581</u>	<u>27,263,378</u>
December 31, 2022							
Series A	22,004,759	1,771,394	(1,431,581)	(310,700)	262,231	(1,963,651)	20,332,452
Series F	7,723,411	450,410	(1,093,524)	(92,848)	71,816	(623,618)	6,435,647
	<u>29,728,170</u>	<u>2,221,804</u>	<u>(2,525,105)</u>	<u>(403,548)</u>	<u>334,047</u>	<u>(2,587,269)</u>	<u>26,768,099</u>

* Detailed distributions to unitholders

	From net investment income \$	From net realized gains on investments and derivatives \$	From return of capital \$	Total distributions to unitholder \$
December 31, 2023				
Series A	37,086	800,416	-	837,502
Series F	26,027	238,139	-	264,166
	<u>63,113</u>	<u>1,038,555</u>	<u>-</u>	<u>1,101,668</u>
December 31, 2022				
Series A	-	133,357	177,343	310,700
Series F	-	46,706	46,142	92,848
	<u>-</u>	<u>180,063</u>	<u>223,485</u>	<u>403,548</u>

The accompanying notes are an integral part of these financial statements.

Palos Equity Income Fund
Statements of Cash Flows
For the years ended December 31, 2023 and 2022

(expressed in Canadian dollars)

	2023 \$	2022 \$
Cash provided by (used in)		
Operating activities		
Increase (decrease) in net assets attributable to holders of redeemable units	2,063,581	(2,587,269)
Adjustments for non-cash items		
Net realized gain on sale of investments	(1,450,626)	(428,539)
Net change in unrealized (appreciation) depreciation of investments	(414,390)	3,095,559
Foreign exchange on cash	477	(899)
Change in non-cash balances		
Increase in accrued income receivable	(20,584)	(22,135)
(Increase) decrease in other assets	(4,161)	2,164
Increase (decrease) in accrued liabilities	(15,252)	20,605
Increase (decrease) in management fees payable	1,472	(658)
Proceeds from sale of investments	21,779,689	20,489,786
Purchase of investments	(20,157,607)	(20,205,738)
Cash provided by (used in) operating activities	<u>1,782,599</u>	<u>362,876</u>
Financing activities		
Proceeds from issuance of redeemable units	1,344,281	2,227,754
Amount paid on redemption of redeemable units	(2,759,728)	(2,525,105)
Distributions paid to holders or redeemable units, net of reinvested distributions	(61,511)	(428,130)
Cash used in financing activities	<u>(1,476,958)</u>	<u>(725,481)</u>
Increase (decrease) in cash during the year	305,641	(362,605)
Foreign exchange on cash	(477)	899
Cash – Beginning of year	<u>107,456</u>	<u>469,162</u>
Cash – End of year	<u>412,620</u>	<u>107,456</u>
Supplemental information *		
Interest paid	2,562	729
Interest received	138,048	119,646
Dividends received, net of withholding taxes	755,987	644,997

* Included as a part of cash flows from operating activities

The accompanying notes are an integral part of these financial statements.

Palos Equity Income Fund

Schedule of Investment Portfolio

As at December 31, 2023

(expressed in Canadian dollars)

Description	Currency	Number of shares	Average cost \$	Fair value \$
Investments owned (98.62%)				
Equities (95.27%)				
Basic material (4.39%)				
Agnico Eagle Mines Ltd.	CAD	3,661	224,872	265,972
Franco-Nevada Corp.	CAD	2,700	435,285	396,279
K92 Mining Inc.	CAD	40,907	265,387	266,305
Wheaton Precious Metals Corp.	CAD	4,100	202,751	268,017
			1,128,295	1,196,573
Communications (4.83%)				
BCE Inc.	CAD	4,200	230,119	219,114
Cogeco Communications Inc.	CAD	2,300	122,013	136,505
Shopify Inc.	CAD	3,650	226,128	376,534
TELUS Corp.	CAD	24,840	638,067	585,727
			1,216,327	1,317,880
Consumer, cyclical (2.87%)				
ADENTRA Inc.	CAD	9,000	258,395	287,730
Canadian Tire Corp Ltd.	CAD	1,650	211,664	232,188
Pollard Banknote Ltd.	CAD	8,170	202,098	261,685
			672,157	781,603
Consumer, non-cyclical (3.75%)				
Dentalcorp Holdings Ltd.	CAD	27,500	231,468	191,400
Green Thumb Industries Inc.	CAD	12,500	150,238	185,875
Information Services Corp.	CAD	8,200	186,856	181,876
Jamieson Wellness Inc.	CAD	3,840	111,543	121,843
Park Lawn Corp.	CAD	12,550	290,348	247,737
Payfare Inc.	CAD	15,000	91,548	93,150
			1,062,001	1,021,881
Energy (19.85%)				
ARC Resources Ltd.	CAD	11,900	200,239	234,073
Canadian Natural Resources Ltd.	CAD	6,200	322,287	538,222
CES Energy Solutions Corp.	CAD	50,900	119,856	175,605
Enbridge Inc.	CAD	6,800	303,040	324,360
Enerflex Ltd.	CAD	19,800	158,528	121,374
Freehold Royalties Ltd.	CAD	19,200	212,028	262,848
Headwater Exploration Inc.	CAD	28,800	160,047	180,000
Keyera Corp.	CAD	10,220	290,775	327,347
North American Construction Group Ltd.	CAD	6,200	164,468	171,430
Parkland Corp.	CAD	6,100	178,052	260,531
Peyto Exploration & Development Corp.	CAD	6,000	74,606	72,240

The accompanying notes are an integral part of these financial statements.

Palos Equity Income Fund
Schedule of Investment Portfolio ...continued
As at December 31, 2023

(expressed in Canadian dollars)

Description	Currency	Number of shares	Average cost \$	Fair value \$
Precision Drilling Corp.	CAD	3,100	219,991	223,076
Secure Energy Services Inc.	CAD	39,600	251,276	373,428
Surge Energy Inc.	CAD	28,600	239,114	185,328
Tamarack Valley Energy Ltd.	CAD	85,900	325,641	263,713
TC Energy Corp.	CAD	6,200	305,000	320,912
Teck Resources Ltd.	CAD	7,530	345,732	421,755
Topaz Energy Corp.	CAD	17,400	317,986	337,212
Tourmaline Oil Corp.	CAD	6,820	305,637	406,404
Trican Well Service Ltd.	CAD	51,300	161,333	211,356
			4,655,636	5,411,214
Financial (30.85%)				
Alaris Equity Partners Income	CAD	14,400	206,298	234,576
Bank of Montreal	CAD	9,070	960,946	1,189,168
Boardwalk Real Estate Investment Trust	CAD	3,967	155,532	283,006
Brookfield Asset Management Ltd.	CAD	4,800	198,308	255,456
Brookfield Corp.	CAD	7,100	285,583	377,365
BSR Real Estate Investment Trust	USD	15,300	241,461	239,808
Canadian Imperial Bank of Commerce	CAD	16,563	859,431	1,056,719
Crombie Real Estate Investment Trust	CAD	20,460	318,189	282,348
Dream Industrial Real Estate Investment Trust	CAD	22,505	286,374	314,170
EQB Inc.	CAD	3,250	158,228	283,498
Flagship Communities REIT	USD	10,600	194,412	223,248
InterRent Real Estate Investment Trust	CAD	23,700	295,141	313,551
National Bank of Canada	CAD	6,410	417,271	647,410
Royal Bank of Canada	CAD	8,430	724,849	1,129,620
StorageVault Canada Inc.	CAD	49,820	168,354	260,559
The Toronto-Dominion Bank	CAD	12,929	698,589	1,106,981
Trisura Group Ltd.	CAD	6,300	205,241	214,200
			6,374,207	8,411,683
Funds (6.81%)				
BMO Short Corporate Bond Index ETF	CAD	60,927	783,816	817,640
BMO Short Federal Bond Index ETF	CAD	64,930	853,002	876,555
Purpose High Interest Savings ETF	CAD	3,250	163,005	162,533
			1,799,823	1,856,728
Industrial (10.95%)				
Ag Growth International Inc.	CAD	4,600	240,640	232,392
ATS Corp.	CAD	4,100	186,572	234,151
Canadian National Railway Co.	CAD	2,420	285,686	403,051
Canadian Pacific Kansas City Ltd.	CAD	3,895	202,876	408,352
Cargojet Inc.	CAD	2,740	326,253	326,526
CCL Industries Inc.	CAD	4,410	221,935	262,792
GFL Environmental Inc.	CAD	7,100	246,012	324,541

Palos Equity Income Fund
Schedule of Investment Portfolio ...continued
As at December 31, 2023

(expressed in Canadian dollars)

Description	Currency	Number of shares	Average cost \$	Fair value \$
Mullen Group Ltd.	CAD	19,300	232,077	270,972
TFI International Inc.	CAD	1,495	157,263	269,459
WSP Global Inc.	CAD	1,370	156,005	254,464
			<u>2,255,319</u>	<u>2,986,700</u>
Technology (3.83%)				
CGI Inc.	CAD	1,870	178,780	265,447
Constellation Software Inc.	CAD	85	163,383	279,248
Kinaxis Inc.	CAD	1,690	240,108	251,320
Open Text Corp.	CAD	4,441	207,469	247,319
			<u>789,740</u>	<u>1,043,334</u>
Utilities (7.14%)				
AltaGas Ltd.	CAD	7,500	171,385	208,650
Boralex Inc.	CAD	6,500	204,862	218,920
Brookfield Infrastructure Corp.	CAD	5,475	240,174	255,902
Capital Power Corp.	CAD	13,120	476,714	488,720
Innergex Renewable Energy Inc.	CAD	25,900	377,394	238,021
Northland Power Inc.	CAD	22,318	667,411	537,194
			<u>2,137,940</u>	<u>1,947,407</u>
Total Equities			<u>22,091,445</u>	<u>25,975,003</u>

Palos Equity Income Fund
Schedule of Investment Portfolio ...*continued*
As at December 31, 2023

(expressed in Canadian dollars)

Description	Currency	Number of shares/ Nominal value	Average cost \$	Fair value \$
Fixed income (3.28%)				
Basic material (2.25%)				
Chemtrade Logistics Income Fund, 6.5% / Oct. 31, 2026 / CONV \$15.80	CAD	250,000	250,000	244,280
North American Construction Group Ltd., 5.5% / June 30, 2028 / CONV \$24.75	CAD	300,000	300,000	367,836
			<u>550,000</u>	<u>612,116</u>
Consumer cyclical (1.03%)				
Exchange Income Corp. 5.25% / Jan. 15, 2029 / CONV \$59.99	CAD	300,000	300,000	281,229
			<u>850,000</u>	<u>893,345</u>
Warrants (0.07%)				
Constellation Software Inc. / March 31, 2040	CAD	90	-	-
Flow Beverage Corp. \$10 / June 29, 2023	CAD	3,400	3,060	4,250
Star Royalties Ltd. \$1 / Feb. 19, 2024	CAD	85,000	7,565	425
The Lion Electric Co. \$2.80 / Dec. 13, 2027	USD	25,000	-	12,896
Tidewater Midstream and Infrastructure Ltd. \$1.44 / Aug. 16, 2024	CAD	15,000	1,500	450
			<u>12,125</u>	<u>18,021</u>
Total investments owned			22,953,570	26,886,369
Commissions and other portfolio transaction costs			<u>(26,958)</u>	
Net investments owned (98.62%)			<u>22,926,612</u>	<u>26,886,369</u>
Other assets, net (1.38%)				<u>377,009</u>
Net assets attribute to holders of redeemable units (100%)				<u><u>27,263,378</u></u>

Palos Equity Income Fund

Notes to Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)

1 General information

Palos Equity Income Fund (the Fund) was formed on January 3, 2008 under the laws of the Province of Quebec pursuant to a trust agreement, as amended for the last time on August 26, 2013, between Computershare Trust Company of Canada (the trustee) and Charles Marleau (the settlor). The address of the Fund's registered office is 1 Place Ville-Marie, Suite 1670, Montréal, Quebec, H3B 2B6 Canada. The Fund is an open-ended mutual fund, is qualified as a mutual fund trust and is a registered investment fund under Section 204.4 of the Income Tax Act (Canada).

Series A opened on January 3, 2008, and Series F opened on February 24, 2012.

The Fund acts as an investment holding unit trust for the benefit of unitholders by acquiring, investing in, holding, transferring, disposing of, or otherwise dealing with such investments as the trustee and the investment fund manager determine, at their discretion, in accordance with the investment objectives of the Fund, which are to preserve capital, to provide an attractive and steady stream of income and to deliver trading-enhanced returns.

The investment fund manager and portfolio advisor is Palos Management Inc. (the Manager).

These financial statements have been authorized for issue by the Board of Directors of the Manager on March 28, 2024.

2 Basis of presentation

These financial statements are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS Accounting Standards).

3 Summary of material accounting policy information

Financial instruments

Classification

IFRS 9, Financial Instruments, sets out a classification and measurement model for financial assets to determine whether a financial asset should be classified at amortized cost, at fair value through profit or loss (FVTPL) or fair value through other comprehensive income (FVOCI). This model is based on the contractual cash flow characteristics of the financial asset and the business model under which the financial asset is held. The Fund manages its investments in financial assets with the objective of realizing cash flows through both the sale of the assets and income generated from those assets. The Manager makes decisions based on the assets' fair values and manages the assets to realize those fair values.

Palos Equity Income Fund

Notes to Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)

IFRS 9 requires that an entity recognize a loss allowance for expected credit losses on financial assets that are measured at amortized cost or FVOCI. Financial assets held by the Fund that are measured at FVTPL will not be subject to the recent impairment requirements.

With respect to receivables, the Fund considers both historical analysis and forward-looking information in determining any expected credit loss. As at the statement of financial position dates, all receivables are due to be settled within the short-term. The Fund considered the probability of default to be close to zero as these instruments have a low risk of default and the counterparties have a strong capacity to meet their contractual obligation in the near term. Given the limited exposure of the Fund to credit risk from financial assets recorded at amortized cost, no loss allowance has been recognized as any such impairment will not have a significant impact on the financial statements.

Recognition

Regular-way purchases and sales of financial assets are recognized at their trade date. Transaction costs are expensed as incurred in the statements of comprehensive income (loss). The Fund's investment assets and liabilities are measured at FVTPL, including certain investments in debt securities, which have been designated at FVTPL. The Fund's derivative and non-derivative investments are classified as FVTPL upon initial recognition. The Fund's obligation for net assets attributable to holders of redeemable units is classified as a financial liability at the redemption amount, which approximates fair value. The redemption amount is determined as the net difference between total assets and all other liabilities for which accounting policies are described herein. Under this method, financial assets and financial liabilities reflect the amount required to be received or paid, discounted, when appropriate, at the contract's effective interest rate. The Fund's accounting policies for measuring the fair value of its investments and derivatives are identical to those used in measuring its net asset value (NAV) for transactions with unitholders.

Income recognition

The interest income for distribution purposes shown on the statements of comprehensive income (loss) represents the contractual interest accounted for on an accrual basis. The Fund does not amortize premiums paid or discounts received on the purchase of fixed income securities except for zero coupon bonds and loans, which would be amortized on a straight-line basis. Dividend income is recorded on the ex-dividend date.

Realized gain on sale of investments and unrealized appreciation (depreciation) of investments are determined on an average cost basis. Average cost does not include amortization of premiums or discounts on fixed income securities with the exception of zero coupon bonds.

Palos Equity Income Fund

Notes to Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of financial assets and financial liabilities traded in active markets (such as publicly traded derivatives and marketable securities) are based on quoted market prices at the close of trading on the reporting date. The Fund uses the last traded market price for both financial assets and financial liabilities where the last traded price falls within that day's bid-ask spread. In circumstances where the last traded price is not within the bid-ask spread, the Manager determines the point within the bid-ask spread that is most representative of fair value based on the specific facts and circumstances.

The fair value of financial assets and financial liabilities that are not traded in an active market, including over-the-counter derivatives, is determined using valuation techniques. The Fund uses a variety of methods and makes assumptions that are based on market conditions existing at each reporting date. Valuation techniques include the use of comparable recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, option-pricing models and others commonly used by market participants and which make the maximum use of observable inputs.

Investment entities

The Fund meets the definition in IFRS 10, Consolidated Financial Statements, for investment entities and accounts for its investments in underlying at FVTPL.

Structured entities

The Fund may invest in other investment funds (underlying funds) by holding redeemable shares of the underlying funds, which entitle the holder to an appropriate share of the underlying funds' net assets. The Fund does not invest in underlying funds for the purpose of exercising management control. Such investments expose the Fund to the risk that underlying funds may not perform as expected and indirectly to all of the risks applicable to investments in underlying funds.

The carrying value of investments in underlying funds is included in Investment at FVTPL in the statements of financial position and also represents the maximum exposure to losses. Changes in fair value of investments in underlying funds are included within net change in unrealized appreciation (depreciation) of investments in the statements of comprehensive income (loss).

Classification of redeemable units

The Fund's outstanding redeemable units are in different series that do not have identical features. Consequently, the Fund's outstanding redeemable units are classified as financial liabilities and recorded as net assets attributable to holders of redeemable units, in accordance with the requirements of International Accounting Standard (IAS) 32, Financial Instruments: Presentation.

Palos Equity Income Fund

Notes to Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)

Foreign currency translation

The Fund's subscriptions and redemptions are denominated in Canadian dollars, which is also its functional and presentation currency. Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates that transactions occur. Foreign currency assets and liabilities denominated in a foreign currency are translated into the functional currency using the exchange rate prevailing at the measurement date. Foreign exchange gains and losses relating to cash and to other financial assets and financial liabilities are presented as net realized gain on sale of investments and net change in unrealized appreciation (depreciation) of investments in the statements of comprehensive income (loss).

Offsetting financial assets and financial liabilities

Financial assets and financial liabilities are offset in the Fund's statements of financial position when and only when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. The Fund has a legally enforceable right to offset a financial asset and financial liability when such right is enforceable in the normal course of business and in the event of default, insolvency or bankruptcy.

Over-the-counter derivatives, securities lending, repurchase agreements and receivable for investments sold and payable for investments purchased are subject to master netting or similar agreements that do not meet the criteria for offsetting in the statements of financial position as they give a right to set-off that is enforceable only in the event of default, insolvency or bankruptcy.

Cash

Cash comprises deposits with financial institutions and bank overdraft.

Increase (decrease) in net assets attributable to holders of redeemable units per unit per series

The increase (decrease) in net assets attributable to holders of redeemable units per unit of each series is calculated by dividing the increase (decrease) in net assets attributable to holders of redeemable units of each series by the weighted average number of units outstanding during the year.

Taxation

The Fund qualifies as a mutual fund trust under the Income Tax Act (Canada). All of the Fund's net income for tax purposes and sufficient net capital gains realized in any period are required to be distributed to unitholders such that no income tax is payable by the Fund. As a result, the Fund does not record income taxes. Since the Fund does not record income taxes, the tax benefit of capital and non-capital losses has not been reflected in the statements of financial position as a deferred income tax asset.

The Fund currently incurs withholding taxes imposed by certain countries on investment income and capital gains. Such income and gains are recorded on a gross basis and the related withholding taxes are shown as a separate expense in the statements of comprehensive income (loss).

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Notes to Financial Statements

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New standards, interpretations and amendments not yet adopted

There are no new standards, interpretations or amendments that have not yet been adopted, that would affect the Fund's financial statements.

New standards, interpretations and amendments adopted during the year

Effective January 1, 2023, the Fund adopted the amendment to IAS 1, Presentation of Financial Statements, with regard to disclosure of material accounting policy information. This amendment did not have a material impact on these financial statements. There are no other standards, amendments to standards or interpretations that are effective for annual periods beginning on January 1, 2023 that have a material effect on the financial statements of the Fund.

4 Critical accounting estimates and judgments

The preparation of financial statements requires management to use judgment in applying its accounting policies and to make estimates and assumptions about the future. The following discusses the most significant accounting judgments and estimates that the Manager has made in preparing the financial statements:

a) Classification and measurement of investment and application of the fair value option

In classifying and measuring financial instruments held by the Fund, the Manager is required to make significant judgments about whether or not the business of the Fund is to manage its portfolio of investments and evaluate performance on a fair value basis and that the portfolio of investments is neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets. The most significant judgments made include assessing and determining the appropriate business model that enables the decision that the Fund's investments are classified as FVTPL.

5 Audit fees

For the year ended December 31, 2023, fees paid or payable to PricewaterhouseCoopers LLP and its network firms for the audit of the financial statements of Canadian Reporting Issuer were \$46,897 (2022 – \$37,514). Fees for other services were \$11,810 (2022 – \$11,853).

Palos Equity Income Fund

Notes to Financial Statements

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(expressed in Canadian dollars)

6 Risks associated with financial instruments

Risk factors

The Fund's activities expose it to a variety of risks associated with financial instruments, as follows: credit risk, liquidity risk, market risk (including currency risk, interest rate risk and price risk) and concentration risk. The Fund's overall risk management program seeks to maximize the returns derived for the level of risk to which the Fund is exposed and seeks to minimize potential adverse effects on the Fund's financial performance. All investments result in a risk of loss of capital. These risks are moderated through careful selection of securities and other financial instruments within the Fund's investment guidelines. The risks are measured using a method that reflects the expected impact on the results and net assets attributable to unitholders of the Fund from reasonably possible changes in the relevant risk variables.

Credit risk

The Fund is exposed to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The majority of the credit risk to which the Fund is exposed arises from its investments in debt securities. In selecting fixed income securities for the Fund, the Manager considers factors such as the debt security's yield, risk of interest rate fluctuation, credit risk, the issuer's capital structure, credit spread and duration. As at December 31, 2023, all investments in fixed income were non-rated (2022 – non-rated).

All portfolio transactions in securities are settled or paid for upon delivery using approved brokers. The risk of default is considered minimal as delivery of securities sold is only made once the broker has received payment. Payment is made on a purchase once the securities are received by the broker. The trade will not settle if either party fails to meet its obligation. In addition, the Fund lodges its cash with quality institutions. Credit risk with respect to accrued income receivable is limited as the receivables are derived from a portfolio of diversified investments.

The Fund's maximum exposure to credit risk is equal to the carrying value of the assets presented on the statements of financial position. The Fund does not anticipate any significant losses from the non-performance of counterparties.

Liquidity risk

Liquidity risk is the risk that the Fund will encounter difficulty in meeting obligations associated with financial liabilities. The Fund is exposed to daily cash redemptions. Financial liabilities that potentially subject the Fund to liquidity risk consist of payable for investments purchased, redemptions payable, distributions payable, accrued liabilities and management fees payable. The Fund's investment approach focuses on investing in highly liquid securities and moderately liquid securities, which are therefore readily saleable to meet liquidity needs.

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(expressed in Canadian dollars)

The Fund may invest in debt securities and unlisted equity investments that are not traded in an active market. As a result, the Fund may not be able to quickly liquidate its investments in these instruments at amounts that approximate their fair values, or be able to respond to specific events such as deterioration in the creditworthiness of any particular issuer. In accordance with the Fund's policy, the Manager monitors the Fund's liquidity position on a daily basis. The tables below analyze the Fund's financial liabilities into relevant maturity groupings based on the remaining period to the contractual maturity date. The amounts in the tables are the contractual undiscounted cash flows.

	2023		
Financial liabilities	On demand	< 3 months	Total
	\$	\$	\$
Distributions payable	-	113,638	113,638
Accrued liabilities	-	51,423	51,423
Management fees payable	-	1,472	1,472
Redeemable units	27,263,378	-	27,263,378

	2022		
Financial liabilities	On demand	< 3 months	Total
	\$	\$	\$
Distributions payable	-	17,069	17,069
Accrued liabilities	-	66,675	66,675
Redeemable units	26,768,099	-	26,768,099

Redeemable units are redeemable on demand at the holder's option. However, the Manager does not expect that the contractual maturity disclosed above will be representative of the actual cash outflows, as holders of these instruments typically retain them for a longer period.

Market risk

The Fund's investments are subject to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. To monitor the risk, the Fund's Manager uses stress testing to examine the impact that abnormally large swings in market factors and periods of prolonged inactivity might have on trading portfolios. The stress testing is designed to identify key risks and ensure that the losses from abnormal events are not above the Fund's risk tolerance.

The following tables include sensitivity analyses that show how the net assets attributable to holders of redeemable units would have been affected by a reasonably possible change in the relevant risk variable at each reporting date. In practice, the actual results may differ and the difference could be material.

Palos Equity Income Fund

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(expressed in Canadian dollars)

a) Currency risk

The Fund invests in monetary assets denominated in currencies other than Canadian dollar. These investments result in currency risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The table below indicates the foreign currencies to which the Fund had significant exposure as at December 31, 2023 and 2022, in Canadian dollars. The table also illustrates the potential impact on the net assets attributable to holders of redeemable units if the Canadian dollar had strengthened or weakened by 5% in relation to each of the other currencies, with all other variables held constant. The monetary exposure presents the impact on cash and the non-monetary exposure presents the impact on investments. Non-monetary items are investments in equity securities and are classified based on the currency in which they were purchased.

Currency	Exposure			Impact if CAD strengthened or weakened by 5% in relation to other currencies		
	Monetary \$	Non-monetary \$	Total \$	Monetary \$	Non-monetary \$	Total \$
December 31, 2023						
US dollar	3,019	475,952	478,971	151	23,798	23,949
% of Net assets attributable to holders of redeemable units	0.0	1.7	1.7	0.0	0.1	0.1

Currency	Exposure			Impact if CAD strengthened or weakened by 5% in relation to other currencies		
	Monetary \$	Non-monetary \$	Total \$	Monetary \$	Non-monetary \$	Total \$
December 31, 2022						
US dollar	(113,120)	518,416	405,296	(5,656)	25,921	20,265
% of Net assets attributable to holders of redeemable units	(0.4)	1.9	1.5	0.0	0.1	0.1

b) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Fund holds securities with fixed interest rates that expose the Fund to fair value interest rate risk. The Fund also holds cash that is subject to variable interest rates that exposes the Fund to cash flow interest rate risk.

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(expressed in Canadian dollars)

The Fund mitigates interest rate risk by monitoring interest rates and the maturities of its portfolio of interest-bearing financial instruments. The following table summarizes the Fund's exposure to interest rate risk. It includes the Fund's interest-bearing financial assets at fair value, categorized by the earlier of contractual interest rate reset dates or maturity dates. The table also illustrates the potential impact on the net assets attributable to holders of redeemable units if the prevailing levels of market interest rates changed by 1%, assuming a parallel shift in the yield curve with all other variables held constant.

Terms to maturity	2023 \$	2022* \$
1–3 years	244,280	-
3–5 years	367,836	245,818
Over 5 years	281,229	608,700
Total	893,345	854,518
Impact on net assets attributable to holders of redeemable units	26,646	26,750
Impact on net assets attributable to holders of redeemable units (%)	0.1%	0.1%

* The comparative figures previously reported as at December 31, 2022 have been adjusted in the table above. The table was previously showing only one category for 1 to 5 years.

c) Price risk

Price risk is the risk that the value of an investment will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual investment or its issuer, or by factors affecting all securities traded in the market. The Fund is exposed to price risk through its equity investment portfolio, which includes a variety of common shares in a wide range of industries. Other assets and liabilities are monetary items that are short-term in nature, and as such are not subject to price risk.

As at December 31, 2023, the expected increase or decrease in net assets attributable to holders of redeemable units of the Fund if the S&P/TSX composite index had increased or decreased by 5%, with all other variables held constant, would amount to \$1,317,432 and would represent 4.8% of the net assets attributable to holders of redeemable units of the Fund (2022 – \$1,318,850 representing 4.9%).

Palos Equity Income Fund

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(expressed in Canadian dollars)

Concentration risk

Concentration risk arises as a result of the concentration of exposure within the same category, whether it is geographical location, product type, industry sector or counterparty type. The following is a summary of the Fund's concentration risk by market segment over the total investments market value:

Market segment	% of portfolio	
	2023	2022
Basic materials	4.6	7.5
Communications	4.9	3.4
Consumer, cyclical	2.9	4.1
Consumer, non-cyclical	3.7	4.4
Energy	20.1	18.1
Financial	31.3	29.5
Funds	6.9	6.6
Industrial	11.1	11.1
Technology	3.9	5.9
Utilities	7.2	6.1
Bonds	3.3	3.2
Warrants	0.1	0.1
	<hr/> 100.0	<hr/> 100.0

Market segment	% of portfolio	
	2023	2022
Bonds	3.3	3.2
Common stock	95.2	96.2
Warrants	0.1	0.1
Other net assets	1.4	0.5

Palos Equity Income Fund

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(expressed in Canadian dollars)

Fair value measurement

The carrying amounts of accrued income receivable, subscription receivable, other assets, distributions payable, accrued liabilities and management fees payable approximate their fair values due to the short-term nature of these financial instruments.

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

				2023
	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
Assets				
Equity	25,975,003	-	-	25,975,003
Fixed income	-	893,345	-	893,345
Warrants	18,021	-	-	18,021
	<u>25,993,024</u>	<u>893,345</u>	<u>-</u>	<u>26,886,369</u>
				2022
	Level 1* \$	Level 2 \$	Level 3 \$	Total \$
Assets				
Equity	25,761,288	-	-	25,761,288
Fixed income	-	854,518	-	854,518
Warrants	27,629	-	-	27,629
	<u>25,788,917</u>	<u>854,518</u>	<u>-</u>	<u>26,643,435</u>

All fair value measurements above are recurring. Fair values are classified as Level 1 when the related security or derivative is actively traded and a quoted price is available. If an instrument classified as Level 1 subsequently ceases to be actively traded, it is transferred out of Level 1. In such cases, the instruments are reclassified into Level 2, unless the measurement of its fair value requires the use of significant unobservable inputs, in which case it is classified as Level 3.

There was no change in levels during the years ended December 31, 2023 and 2022.

Palos Equity Income Fund

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(expressed in Canadian dollars)

Equities and convertible bonds

The Fund's equity and convertible bond positions are classified as Level 1 when the security is actively traded and a reliable price is observable. All equities and convertible bonds are classified as Level 1 investments.

Bonds and short-term investments

Corporate bonds are valued using models with inputs including interest rate curves, credit spreads and volatilities. The inputs that are significant to valuation are generally observable, and therefore the Fund's bonds and short-term investments have been classified as Level 2.

7 Redeemable units

During the years ended December 31, 2023 and 2022, the number of units issued, redeemed and outstanding were as follows:

	Redeemable units – Beginning of year	Redeemable units issued	Redemption of redeemable units	Reinvestments of units	Redeemable units – End of year
December 31, 2023					
Series A	3,123,732	165,774	(278,950)	108,132	3,118,688
Series F	912,859	31,829	(122,653)	29,698	851,733
December 31, 2022					
Series A	3,038,038	255,512	(209,866)	40,048	3,123,732
Series F	994,079	58,525	(149,901)	10,156	912,859

Capital structure

Units issued and outstanding are considered to be the capital of the Fund. The Fund does not have any specific capital requirements.

The Fund is authorized to issue an unlimited number of redeemable unit series, as well as an unlimited number of redeemable units within each series. Each series unit enables its bearer to participate equally in the allocations the Fund completes for the given series. Unit fractions may also be issued.

The Fund is composed of more than one redeemable unit series; each redeemable unit series may feature different structures regarding management fees, performance fees and brokerage. As a result, each redeemable unit entitles its holder to one vote and to participate equally in the allocations the Fund completes and, in the case of Fund liquidation, in the allocation of the redeemable unit series' net assets attributable to holders of redeemable units after all current liabilities have been paid.

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(expressed in Canadian dollars)

8 Related party transactions

Management fees and performance fees

The Manager provides management and advisory services to the Fund in accordance with the agreement. In return for these services, the Manager is paid a management fee and a performance fee. The Series A units of the Fund are subject to a monthly management fee equal to 1/12 of 1.5% of the NAV of the Series A units. The Manager will pay a trailer fee of 0.75% out of the management fees collected from the Fund with respect to Series A units.

Series F is similar to Series A, but no trailer fee is included in the management fee. Series F charges a monthly management fee of 1/12 of 0.75% of the NAV of Series F.

Based on the agreement amended and restated on August 26, 2013, the performance fee is 20% of the amount by which the Fund outperforms its benchmark, the S&P/TSX Composite Index. Performance fees are paid annually.

The total management fees and performance fees for the year ended December 31, 2023 amounted to \$413,642 and \$nil, respectively (2022 – \$419,297 and \$nil, respectively), with \$1,472 in outstanding fees due to the Manager as at December 31, 2023 (2022 – \$nil).

The Manager may waive or absorb the operation of management fees of the Fund. The decision to do so is reviewed regularly and is determined at the sole discretion of the Manager. During the year, the Manager did not waive any fees (2022 – did not waive any fees).

Independent Review Committee fees

The total remuneration paid to members of the Independent Review Committee during the year ended December 31, 2023 amounted to \$12,001 (2022 – \$12,001) and consisted only of fixed fees.

Palos Equity Income Fund

Notes to Financial Statements

December 31, 2023 and 2022

(expressed in Canadian dollars)

9 Brokerage commissions and soft dollars

The total commissions paid by the Fund to brokers in connection with portfolio transactions for the years ended December 31, 2023 and 2022, together with other transaction charges, are disclosed in the statements of comprehensive income (loss) of the Fund. Brokerage business is allocated to brokers based on the best net result for the Fund. Subject to these criteria, preference may be given to brokerage firms that provide (or pay for) certain services (arrangements referred to as “soft dollar”), which may include investment research, analysis and reports, and databases or software in support of these services. The ascertainable soft dollar value received as a percentage of total brokerage commissions paid during the years ended December 31, 2023 and 2022 is disclosed below:

	2023	2022
Soft dollars	\$5,461	\$5,234
Percentage of total transaction costs (%)	11%	12%

10 Increase (decrease) in net assets attributable to holders of redeemable units per series per unit

The increase (decrease) in net assets attributable to holders of redeemable units per series per unit for the years ended December 31, 2023 and 2022 is calculated as follows:

	Increase (decrease) in net assets attributable to holders of redeemable units per series \$	Weighted average of redeemable units outstanding during the year	Increase (decrease) in net assets attributable to holders of redeemable units per unit \$
December 31, 2023			
Series A	1,521,977	3,114,887	0.49
Series F	541,604	852,408	0.64
December 31, 2022			
Series A	(1,963,651)	3,096,748	(0.63)
Series F	(623,618)	944,443	(0.66)

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11 Taxes

The Fund qualifies as a mutual fund trust under the Income Tax Act (Canada).

All or substantially all of the net income for tax purposes and net taxable capital gains realized in any period, after use of loss carry-forwards, are distributed to unitholders such that no income taxes are payable by the Fund.

Capital and non-capital losses determined for tax purposes as at December 31, 2023 were \$nil (2022 – \$nil).

