

**MANAGEMENT REPORT OF FUND  
PERFORMANCE**

**December 31 2016**

**CHOU ASSOCIATES FUND**

**CHOU ASSOCIATES MANAGEMENT INC.**

## **MANAGEMENT REPORT OF FUND PERFORMANCE**

### **December 31, 2016**

This annual management report of fund performance contains financial highlights but does not contain the complete financial statements of the Fund. You can get a copy of the annual financial statements at your request, and at no cost, by calling Toll-free: 1-888-357-5070, by writing to us at 110 Sheppard Ave. East, Suite 301, Box 18, Toronto, Ontario M2N 6Y8 or by visiting our website at [www.choufunds.com](http://www.choufunds.com) and SEDAR at [www.sedar.com](http://www.sedar.com).

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

This document may contain forward-looking statements relating to anticipated future events, results, circumstances, performance, or expectations that are not historical facts but instead represent our beliefs regarding future events. By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. There is significant risk that predictions and other forward-looking statements will not prove to be accurate. We caution readers of this document not to place undue reliance on our forward-looking statements as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed or implied in the forward-looking statements.

Actual results may differ materially from management expectations as projected in such forward-looking statements for a variety of reasons including, but not limited to, market and general economic conditions, interest rates, regulatory and statutory developments, the effects of competition in the geographic and business areas in which the Fund may invest, and the risks detailed from time to time in the Fund's Simplified Prospectus. We caution that the foregoing list of factors is not exhaustive, and that when relying on forward-looking statements to make decisions with respect to investing in the Fund, investors and others should carefully consider these factors, as well as other uncertainties and potential events, and the inherent uncertainty of forward-looking statements. Due to the potential impact of these factors, the family of Chou Funds does not undertake, and specifically disclaims, any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, unless required by applicable law.

Chou Associates Management Inc. ("the Manager") manages the overall business of the Fund, including the selection of the securities in the Fund's portfolio and promoting sales of the Fund's units. For the purposes of this document, the terms Chou Associates Management Inc. and "the Manager" are interchangeable. Full contact information for the Manager is located at the end of this report.

# CHOU ASSOCIATES FUND

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## Management Discussion of Fund Performance

### Investment Objective and Strategies

Chou Associates Fund's (the "Fund") objective is to provide long-term growth of capital by investing primarily in equity securities of United States ("U.S.") and foreign businesses considered by Chou Associates Management Inc. (the "Manager") to be undervalued. The Fund may also invest in the equity securities of Canadian businesses. The Fund's investments may include common and preferred shares, convertible debentures, warrants, government and corporate bonds and short-term indebtedness.

The Fund's investment strategy follows a strong discipline with regard to the prices paid to acquire portfolio investments. The level of investments in a particular entity's securities is generally commensurate with the current price of the company's securities in relation to the Manager's assessment of such entity's intrinsic value as determined by various factors. This approach is designed to provide an extra margin of safety, which in turn, serves to reduce the Fund's overall portfolio risk.

### Risk

The risks of investing in the Fund are disclosed in the Fund's most recently filed Simplified Prospectus which can be found on the Fund's website at [www.choufunds.com](http://www.choufunds.com) and SEDAR at [www.sedar.com](http://www.sedar.com).

During the year ended December 31, 2016, there were no material changes that affected the Fund's overall level of risk.

As at December 31, 2016, Fairfax Financial Holdings held 24.0% of the units of the Fund. If Fairfax redeems its units, a significant portion of the Fund's investments may have to be liquidated in order to effect this transaction. The timing of such liquidation may not be appropriate and all investors may suffer a proportionate loss as a result of such liquidation.

### Results of Operations

For the year ended December 31, 2016, the Fund decreased by 2.8% for Series A units and 2.2% for Series F units, after fees and expenses, while the S&P 500 Total Return Index increased by 8.9% in Canadian dollars. In U.S. dollars, the Fund increased by 0.2% for Series A units and 0.7% for Series F units, while the S&P 500 Total Return Index returned 12.0%.

Notwithstanding the political uncertainties, the U.S. stock market had a very good year in 2016. The market started soft in January and February with concerns of China's economic slowdown and prolonged declines in oil prices, but has quickly rebounded since then. The first political shocks came from the unexpected decision by British voters to leave the European Union in late June. News of Brexit sent the S&P 500 down 3.6% in just one day, as investors turned to safe haven assets like gold, which jumped over 4%. However, U.S. stocks quickly stabilized and coasted toward the November election. Despite the initial shock, the stock market reacted positively to Donald Trump winning the U.S. presidency as the Dow soared 257 points on election night. The rally was likely fuelled by expectations of lower taxes, reduced regulations, pro-business initiatives and stimulus fiscal spending on infrastructure. Industrial and financial stocks particularly benefited since the election with Trump calling for a reduction in former president Obama's expanded regulations on oil production and to scale back or even reverse financial regulations.

With employment and inflation rates steadily increasing in 2016, the Federal Reserve announced the second rate hike in a decade in December, increasing its benchmark rate a quarter percentage point. Expectations of further rate increases will potentially lead to higher borrowing costs for consumers and companies while incentivising more to save.

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The biggest positive contributors to the Fund's performance in 2016 included JPMorgan Chase warrants expiring on October 2018, the equity securities of MBIA Inc., Overstock.com, Goldman Sachs Group, and the 2<sup>nd</sup> lien term loan of Exco Resources Inc.

Equities of Valeant Pharmaceuticals, Sears Holdings Corporation, Resolute Forest Products, and Nokia Corporation were the main negative contributors to the Fund's performance during the same period. The Canadian currency strengthened against the US dollar, which also negatively affected the Fund.

The Fund decreased its holdings of Berkshire Hathaway by 50%, and exited all shares of International Automotive Components Group.

New additions during the year include an equity stake in Valeant Pharmaceuticals, debt securities of Exco Resources unsecured 8.5% due April 2022, Westmoreland Coal Company 8.75% due January 2022, and preferred shares of Overstock.com. The Fund also increased its position in Sears Holdings Corporation and the 2<sup>nd</sup> lien term loan of Exco Resources.

In 2016, the Fund received \$3,195,369 in income from its securities lending program.

The Fund had no covered call options in its portfolio as at December 31, 2016.

The Fund did not enter into any foreign currency contracts during the year ended December 31, 2016.

The Fund's net redemptions for the year ended December 31, 2016 were approximately \$45,297,156 for Series A units and there were net purchases of \$736,318 for Series F units. The Fund's average month-end cash position for the year was 13.1% of the Fund's net assets.

### **Recent Developments**

There have been no recent market developments of particular note, aside from the normal fluctuations of the markets that are expected to have an undue influence on the portfolio of the Fund when compared to its benchmark.

### **Related Party Transactions**

The Manager manages the overall business of the Fund, including selection of the securities in the Fund's portfolio and promoting the sale of the Fund's units.

The Manager is also the trustee of the Fund. Investors receive units of a trust when they invest in the Fund. The Manager, as trustee, holds actual title to the property in the Fund, the cash and portfolio securities, on behalf of the Fund's investors.

The Manager, its officers and directors invest in units of the Fund from time to time in the normal course of business. All transactions with the Manager are measured at the exchange amounts.

During the year ended December 31, 2016, there were no transactions with related parties except in the capacities and instances set out above.

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## Financial Highlights

The following tables show selected key financial information about the Fund and are intended to help you understand the Fund's financial performance for the year ended December 31, 2016, and for each of the past five years ended December 31, as applicable.

### The Fund's Net Assets per Unit<sup>1</sup> - Class A Units

	2016		2015		2014		2013		2012	
<b>Net Assets, beginning of period</b>	\$	<b>115.50</b>	\$	<b>124.04</b>	\$	<b>111.35</b>	\$	<b>81.21</b>	\$	<b>65.86</b>
<b>Increase (decrease) from operations:</b>										
Total revenue	\$	2.11	\$	0.01	\$	1.94	\$	1.91	\$	3.37
Total expenses	\$	(2.06)	\$	(2.38)	\$	(2.18)	\$	(2.00)	\$	(1.52)
Realized gains (losses) for the period	\$	12.19	\$	7.31	\$	4.36	\$	11.72	\$	0.70
Unrealized gains (losses) for the period	\$	(17.19)	\$	(13.35)	\$	9.19	\$	21.42	\$	15.59
<b>Total increase (decrease) from operations<sup>2</sup></b>	\$	<b>(4.95)</b>	\$	<b>(8.41)</b>	\$	<b>13.31</b>	\$	<b>33.05</b>	\$	<b>18.14</b>
<b>Distributions:</b>										
From income (excluding dividends)	\$	1.54	\$	-	\$	0.71	\$	0.10	\$	2.52
From dividends	\$	-	\$	-	\$	-	\$	0.05	\$	-
From capital gains	\$	0.04	\$	0.07	\$	-	\$	3.14	\$	-
Return of capital	\$	0.06	\$	-	\$	-	\$	-	\$	-
<b>Total Distributions<sup>3</sup></b>	\$	<b>1.64</b>	\$	<b>0.07</b>	\$	<b>0.71</b>	\$	<b>3.29</b>	\$	<b>2.52</b>
<b>Net Assets, end of period</b>	\$	<b>110.60</b>	\$	<b>115.50</b>	\$	<b>124.04</b>	\$	<b>111.35</b>	\$	<b>81.21</b>
<b>Net Assets, end of period (USD)</b>	\$	<b>82.37</b>	\$	<b>83.47</b>	\$	<b>106.88</b>	\$	<b>104.72</b>	\$	<b>81.64</b>

### Ratios and Supplemental Data - Class A Units

	2016		2015		2014		2013		2012	
<b>Total Net Asset Value (000s)<sup>4</sup></b>	\$	<b>403,678</b>	\$	<b>468,191</b>	\$	<b>514,449</b>	\$	<b>469,149</b>	\$	<b>402,050</b>
Number of Units Outstanding		3,650,048		4,053,774		4,142,334		4,208,995		4,951,551
Management Expense Ratio <sup>5</sup>		1.87%		1.82%		1.81%		1.82%		1.86%
Management Expense Ratio before waivers or absorptions <sup>6</sup>		1.87%		1.82%		1.81%		1.82%		1.86%
Trading Expense Ratio <sup>7</sup>		0.05%		0.02%		0.03%		0.06%		0.12%
Portfolio Turnover Rate <sup>8</sup>		16.55%		4.06%		7.73%		9.14%		16.58%
<b>Net Asset Value per Unit</b>	\$	<b>110.60</b>	\$	<b>115.50</b>	\$	<b>124.04</b>	\$	<b>111.35</b>	\$	<b>81.20</b>

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## The Fund's Net Assets per Unit<sup>1</sup> - Class F Units

	2016	2015	2014	2013	2012
<b>Net Assets, beginning of period</b>	<b>\$ 114.76</b>	<b>\$ 123.33</b>	<b>\$ 110.76</b>	<b>\$ 81.01</b>	<b>\$ 65.66</b>
<b>Increase (decrease) from operations:</b>					
Total revenue	\$ 2.11	\$ 0.01	\$ 1.95	\$ 1.88	\$ 3.37
Total expenses	\$ (1.50)	\$ (1.69)	\$ (1.52)	\$ (1.44)	\$ (1.08)
Realized gains (losses) for the period	\$ 12.15	\$ 7.27	\$ 4.35	\$ 11.54	\$ 0.81
Unrealized gains (losses) for the period	\$ (15.42)	\$ (13.89)	\$ 8.99	\$ 21.94	\$ 15.41
<b>Total increase (decrease) from operations<sup>2</sup></b>	<b>\$ (2.66)</b>	<b>\$ (8.30)</b>	<b>\$ 13.77</b>	<b>\$ 33.92</b>	<b>\$ 18.51</b>
<b>Distributions:</b>					
From income (excluding dividends)	\$ 2.03	\$ -	\$ 1.40	\$ 0.68	\$ 2.91
From dividends	\$ -	\$ -	\$ -	\$ 0.33	\$ -
From capital gains	\$ 0.03	\$ 0.84	\$ -	\$ 3.14	\$ -
Return of capital	\$ 0.06	\$ -	\$ -	\$ -	\$ -
<b>Total Distributions<sup>3</sup></b>	<b>\$ 2.12</b>	<b>\$ 0.84</b>	<b>\$ 1.40</b>	<b>\$ 4.15</b>	<b>\$ 2.91</b>
<b>Net Assets, end of period</b>	<b>\$ 110.03</b>	<b>\$ 114.76</b>	<b>\$ 123.33</b>	<b>\$ 110.76</b>	<b>\$ 81.00</b>
<b>Net Assets, end of period (USD)</b>	<b>\$ 81.95</b>	<b>\$ 83.47</b>	<b>\$ 106.27</b>	<b>\$ 104.16</b>	<b>\$ 81.43</b>

## Ratios and Supplemental Data - Class F Units

	2016	2015	2014	2013	2012
<b>Total Net Asset Value (000s)<sup>4</sup></b>	<b>\$ 45,074</b>	<b>\$ 45,520</b>	<b>\$ 43,059</b>	<b>\$ 33,864</b>	<b>\$ 24,814</b>
Number of Units Outstanding	409,648	396,647	348,701	305,457	306,407
Management Expense Ratio <sup>5</sup>	1.32%	1.26%	1.24%	1.26%	1.30%
Management Expense Ratio before waivers or absorptions <sup>6</sup>	1.32%	1.26%	1.24%	1.26%	1.30%
Trading Expense Ratio <sup>7</sup>	0.05%	0.02%	0.03%	0.06%	0.12%
Portfolio Turnover Rate <sup>8</sup>	16.55%	4.06%	7.73%	9.14%	16.58%
<b>Net Asset Value per Unit</b>	<b>\$ 110.03</b>	<b>\$ 114.76</b>	<b>\$ 123.33</b>	<b>\$ 110.76</b>	<b>\$ 80.98</b>

(1) This information is derived from the Fund's audited annual unaudited semi-annual financial statements. For financial reporting purposes, prior to January 1, 2013, under Canadian GAAP, the net assets per security presented in the financial statements differ from the net asset value calculated for fund pricing purposes.

(2) Net assets and distributions are based on the actual number of units outstanding at the relevant time. The increase/decrease from operations is based on the weighted average number of units outstanding over the financial period.

(3) Distributions were reinvested in additional units of the Fund or paid in cash upon request.

(4) This information is provided as at period end shown and is rounded to the nearest thousand.

(5) Management expense ratio ("MER") is based on total expenses (excluding commissions and other portfolio transaction costs) for the stated period and is expressed as an annualized percentage of weekly average net asset value during the period. The Manager may, at its discretion, waive or absorb certain operating expenses. MER includes the waiver or absorption by the Manager of certain operating expenses, while the MER before absorption shows the MER prior to operating expenses being waived or absorbed by the Manager.

(6) The trading expense ratio represents total commissions and other portfolio transaction costs expressed as an annualized percentage of weekly average net asset value during the period.

(7) The Fund's portfolio turnover rate indicates how actively the Fund's portfolio adviser manages its portfolio investments. A portfolio turnover rate of 100% is equivalent to the Fund buying and selling all of the securities in its portfolio once in the course of the year. The higher a fund's portfolio turnover rate in a year, the greater the trading costs payable by the fund in the year, and the greater the chance of an investor receiving taxable capital gains in the year. There is not necessarily a relationship between a high turnover rate and the performance of a fund.

(8) Information from 2013 and thereafter is in accordance with IFRS. Information for years prior to 2013 is reported under Canadian GAAP.

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## Management Fees

The Manager manages the Fund. The Manager is entitled to an investment management fee calculated daily as a percentage of the market value of the net assets equal to 1.5% per annum for Series A units and 1.0% per annum for Series F units, payable monthly. The Manager pays 50 basis points per year trailer fees to dealers out of management fees for Series A units. There is no trailer fee paid out for Series F units.

## Past Performance

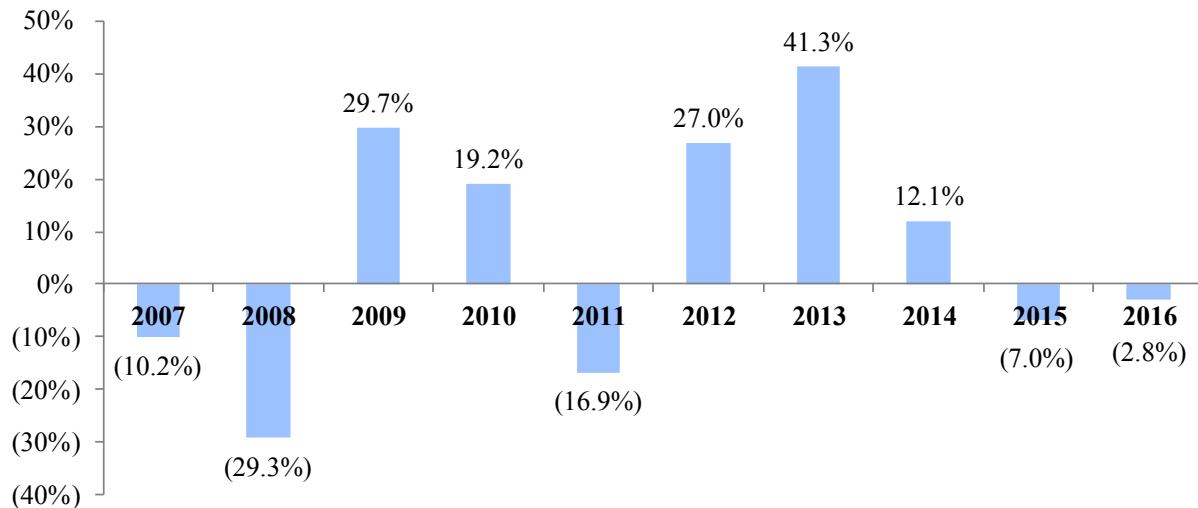
### General

The following charts and tables show the Fund's past performance. Rates of return are historical total returns that include changes in unit prices and assume the reinvestment of all distributions. These returns do not take into account any sales charges, redemption fees, other optional expenses or income taxes that the Fund's investors have to pay and which could reduce these returns. The Fund's past performance does not necessarily indicate its future performance.

### Year-by-Year Returns

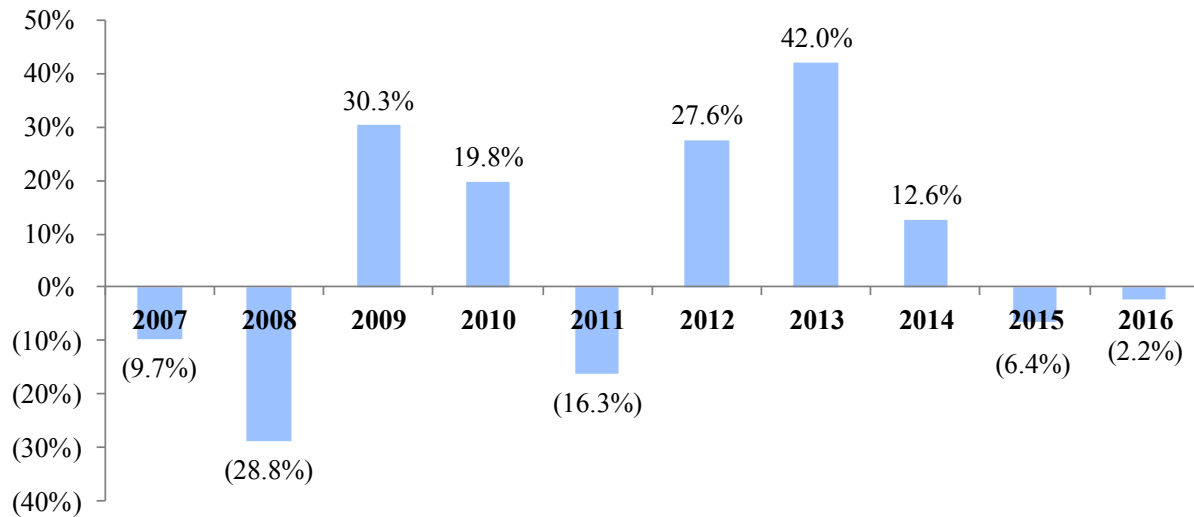
The following bar charts show the annual performance for each of the Series A and Series F units of the Fund for each of the years shown. Each chart shows, in percentage terms, how an investment on January 1 would have increased or decreased by December 31 for each of the years, and how the performance of the Fund varied from year to year.

### Series A



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## Series F



### Annual Compound Returns

The following tables<sup>(1)</sup> show the annual compound total return for each of the Series A and Series F units of the Fund. The tables outline the Fund's past performance for the one-, three-, five-, ten-, fifteen- and twenty-year periods ended on December 31, 2016 for Series A units and since inception and for the one-, three-, five- and ten-year periods ended on December 31, 2016 for Series F units. Also shown for the same periods are the respective historical annual compound total returns or changes of the S&P 500 (the "Index"). The Index is based on the market capitalizations of 500 leading companies publicly traded in the U.S. stock market representing all major industries, as determined by Standard & Poor's. The Index is one of the most commonly followed equity indices and has been widely regarded as the best single gauge of the large cap U.S. equities market since the Index was first published in 1957. The benchmark Index is calculated without the deduction of management fees and fund expenses, whereas the performance of the Fund is calculated after deducting such fees and expenses.

### Series A

December 31, 2016	Past Year	Past 3 Years	Past 5 Years	Past 10 Years	Past 15 Years
Chou Associates Fund	-2.79%	0.45%	12.71%	4.02%	7.45%
S&P 500 (\$CAN)	8.89%	17.75%	21.23%	8.48%	5.49%

### Series F

December 31, 2016	Past Year	Past 3 Years	Past 5 Years	Past 10 Years	Since Inception
Chou Associates Fund	-2.25%	1.02%	13.32%	4.60%	6.22%
S&P 500 (\$CAN)	8.89%	17.75%	21.23%	8.48%	9.14%

<sup>(1)</sup> Tables assume the reinvestment of all dividend



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## Summary of Investment Portfolio

The following tables provide a summary of the Fund's portfolio as at December 31, 2016.

<u>Sector Mix</u>	<u>% of Fund's Net Assets</u>
Financials	48.4%
Energy	12.1%
Health Care	11.7%
Consumer Discretionary	9.3%
Information Technology	6.0%
Materials	5.4%
Industrials	0.7%
Net Cash & Equivalents	6.4%

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<b>Total Portfolio</b>	<b>100.0%</b>
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<u>Total Issuers</u>	<u>% of Fund's Net Assets</u>
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*(excluding cash equivalents)*

### Equities

Berkshire Hathaway Inc., Class 'A'	11.0%
Citigroup Inc.	7.3%
Valeant Pharmaceuticals International Inc.	7.0%
Nokia OYJ, ADR	5.4%
The Goldman Sachs Group Inc.	5.4%
Resolute Forest Products Inc.	5.4%
Sanofi, ADR	4.7%
MBIA Inc.	3.5%
Sears Holdings Corporation	3.2%
Overstock.com Inc.	2.3%
Sears Hometown and Outlet Stores Inc.	1.9%
Ascent Capital Group Inc., Series 'A'	1.5%
Chicago Bridge & Iron Co.	0.6%
Sears Canada	0.3%
Overstock.com Inc. Preferred	0.2%

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<b>Total Equities</b>	<b>59.5%</b>
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### Warrants

JPMorgan Chase & Company, warrants, October 28, 2018	15.0%
Wells Fargo & Company, warrants, October 28, 2018	6.4%
General Motors Company, warrants, October 07, 2019	0.1%

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<b>Total Warrants</b>	<b>21.4%</b>
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### Bonds

Exco Resources Inc., term loans, October 20, 2020	11.3%
Westmoreland Coal Company, 8.75%, January 1, 2022, Callable	0.7%
Dex Media West Inc., term loans, December 31, 2017	0.6%
Exco Resources Inc., 8.500%, April 15, 2022, Callable	0.2%

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<b>Total Bonds</b>	<b>12.7%</b>
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<b>Total Holdings</b>	<b>93.6%</b>
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The summary of the Fund's investment portfolio may change due to ongoing portfolio transactions of the Fund. The next quarterly update as at March 31, 2017 will be in the Quarterly Portfolio Disclosure and will be posted on our website [www.choufunds.com](http://www.choufunds.com) on or before May 31, 2017.

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