SMID CAP CLIENT NEWSLETTER

First Quarter 2016

Cardinal Capital
MANAGEMENT, L.L.C.

IN THIS ISSUE

Market Commentary

Small, smid and large cap indices, as represented by the Russell 2000, 2500 and 1000 Indices fell by 1.5% and rose by 0.4% and 1.2%, respectively, in the first quarter of 2016. Within the Russell 2500, the value index rose by 3.3% while the growth index fell 2.7% for the quarter. The value index rose significantly more than its growth counterpart due primarily to a lower weighting in the poorly-performing healthcare sector and better performance in the utilities and financials sectors. From an economic perspective, the performance of the equity market during the quarter sent mixed signals. Broad based strength in stocks outside of the healthcare, financials and energy sectors was generally constructive but the weakness of small cap stock returns relative to large caps and the strength in utility stocks both signaled caution. Healthcare stocks were weak due to election rhetoric surrounding drug prices and a correction in biotech stocks. Within financials, bank stocks sold off as the prospects for higher interest rates faded while energy-related credit concerns grew. Despite ending the quarter relatively unchanged, the equity market was volatile, falling almost 15% in the first six weeks on interest rate concerns and recession fears before recovering later in the quarter as those abated.

Domestic economic data was mixed during the quarter, although better than most developed economies. GDP grew at a 1.4% annualized rate in the fourth quarter of 2015, employment growth moderated after a strong fourth quarter, and industrial production stabilized as the U.S. dollar weakened and commodity prices rebounded after steep declines. While the unemployment rate stayed near full employment levels, wage growth remained modest at 2.3%. The Federal Reserve left short-term interest rates unchanged during the quarter and indicated that the pace of future interest rate increases was expected to be slower than forecast in December due to the effect of uncertainty surrounding economic developments abroad. Consumer inflation was de minimis during the quarter, although ex-food and energy it rose at a 2.3% annual rate. U.S. corporate profit growth turned negative last year due to the strong U.S. dollar and falling commodity prices but should improve this year as these headwinds abate. M&A activity has slowed early in 2016, as capital became modestly more expensive with banks incrementally more cautious on lending and high yield bond spreads widening. Equity valuations, although attractive relative to bonds, are modestly above historical averages on an absolute basis. However, relative to large cap stocks, small cap valuations are now at parity and no longer at the 10% premium that they averaged over the last decade, excluding a brief period around the financial crisis.

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FIRM OVERVIEW

- Experienced Value Investors
- 23+ Year Track Record
- Research-Driven Process
- FCF-Based Valuations
- Consensus Decisions
- Owned by Current & Former PMs
- $1.9 Billion AUM

OBJECTIVES

- Superior Risk Adjusted Returns
- Preservation of Capital

HOW WE SEEK TO ADD VALUE

- Intensive fundamental research
- Detailed DCF-based valuation analysis
- Opportunistic stock selection balancing risk and return
- Aim to identify good businesses whose stocks are temporarily out-of-favor in structurally inefficient market niches
- Our annual return objective has always been 20%, making our valuations more conservative
- Our discipline is similar to that used by companies and private equity investors, resulting in more than 70 of our investments being acquired since 1995

Performance Commentary

The first quarter net performance of Cardinal's SMID Cap Value Composite, at 0.5%, trailed the 3.3% return of the Russell 2500 Value Index. The main detractors from relative performance were stock selection in information technology and materials sectors as well as an absence of investments in the utilities sectors, and an underweight to and unfavorable stock selection within the healthcare sector. In information technology, the stock price of small business services provider J2 Global fell significantly after a report questioned the viability of its eFax business and the success of its diversification strategy. J2 management has refuted the accuracy of the report. The author of the report issued a similar short recommendation several years ago and the stock has increased several-fold since. The share price of internet services provider IAC/Interactive fell after the company issued disappointing guidance for 2016. In materials, the stock price of Compass Minerals, a salt and plant nutrients company, fell as a mild winter weather reduced demand for its deicing salt. Within healthcare, shares of Akorn, which manufacturers and markets generic pharmaceuticals, switched auditors although it still expects to become current with its financial statements in early May. Since the Akorn stock would likely be delisted if the company does not meet this deadline, we sold our position. The primary contributors to relative performance were strong stock selection in the energy and industrials sectors. In energy, fuel logistics provider World Fuel Services shares rose sharply on solid earnings and the announcement that it was acquiring ExxonMobil's international airport fuel operations. In industrials, the stock price of Genesee & Wyoming, the short line railroad company, rebounded as the company's results showed solid cost controls in the face of challenging volumes.

The annualized net return of Cardinal's SMID Cap Value Composite since inception (May 1, 2010) is 11.4% versus 9.7% for the Russell 2500 Value Index and 10.6% for the Russell 2500 Index. Cardinal managed $1.9 billion in micro, small and smid cap value assets as of March 31, 2016.

Highlighted Investments

At Cardinal, we focus on finding companies with solid fundamentals at opportunistic valuations. Air Methods is the largest provider of air medical transportation services in the U.S, with operations in 42 states. The air medical transportation business is unusual as demand is price inelastic with services used essentially for patients who require immediate transport to a medical facility, regardless of the patient's ability or willingness to pay. With fairly stable demand, the company has been successful in raising its commercial rates to more than offset

Highlighted Investments Cont'd

an adverse mix shift toward Medicaid and Medicare patients who pay much lower prices for the same services. The company has also benefited from healthcare reform as the number of uninsured patients declines. Demand for air medical services increases with miles driven, accident rates, consolidation of trauma centers in hospital groups and rural hospital closures. Air Methods has recently been more aggressive in expanding geographies and services through acquisitions. Adverse trends in the company's collection rates and DSO's have recently depressed the stock price resulting in a discounted valuation relative to its peers. As insurance companies have looked to cut expenses, out-of-network costs such as emergency air support have been targeted and Air Methods has seen an increase in the denial of valid claims, delays in payments and a shift of emergency transport expenses to the patient. Nonetheless, management has been able to keep its net dollar collections flat to growing by raising prices. In addition, the company is trying to increase its in-network commercial accounts where it makes sense. However, until Medicare and Medicaid rates better reflect the cost of delivering air medical transportation services, demographics will make the availability of those services increasingly problematic in rural areas. Despite insurer related challenges on reimbursement, Air Method's operating cash flow has been strong allowing it to upgrade its helicopter fleet, making it one of the youngest in the industry. Given its industry leading position, strong growth outlook and solid balance sheet, the company's stock should trade in-line with its peers once its collections and DSO's normalize.

Starwood Properties Trust originates, invests in, finances and manages commercial real estate related investments globally. The company is headed by Barry Sternlicht who along with the Starwood Capital Group team own $150 million of stock. Starwood Properties was formed after the financial crisis to provide commercial real estate financing to fill a void left by traditional commercial banks who were exiting the market for economic and regulatory reasons. The portfolio that it has built is diversified by asset type and geography as it operates in three segments: lending, servicing, and property ownership. The lending business makes primarily floating rate first mortgage and mezzanine loans. It benefits from Starwood Capital's deal flow and their strong credit culture which has resulted in no realized losses since inception. The servicing business was acquired via the 2013 acquisition of LNR, making the Trust the largest manager of distressed commercial mortgages in the U.S. LNR not only provides a wealth of proprietary historical data which benefits Starwood's loan underwriting but also serves as a hedge as the business is countercyclical. Ownership of stabilized high-quality real estate properties is the newest business line. This addition provides the Trust with the flexibility to be either borrower or lender on attractive real estate depending upon each's relative

PORTFOLIO TEAM

- Experienced and stable team of value investors
- Collaborative and dynamic process capitalizes on collective experience
- Consistency in team responsible for 23+ year track record
- Compensation based on portfolio

GENE FOX
MANAGING PARTNER
At Cardinal Since 1995

ROB KIRKPATRICK
MANAGING PARTNER
At Cardinal Since 2000

RACHEL MATTHEWS
PARTNER
At Cardinal Since 2001

BOB FIELDS
PARTNER
At Cardinal Since 2013

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merits. In 2014, Starwood spun off its single family home rental operations, now known as Colony Starwood Homes as a separate public company. With its positive economic exposure to rising interest rates, strong credit culture and market position, we believe that this strong management team will over time be able to the reduce the discount to its net asset value that the stock is trading at while we are paid an 11% current dividend yield in the interim.

Market and Portfolio Outlook

Looking to the rest of 2016, we expect U.S. economic growth to remain moderate and inflation benign. Short-term U.S. interest rates are expected to rise at a measured pace given the negative interest rate policies of Europe and Japan and the desire to keep the U.S. dollar from appreciating further. Although off its lows, the price of oil is unlikely to move meaningfully higher this year unless oil producing countries agree to cut output. Global economic uncertainty remains elevated outside the U.S. While the short-term economic environment in Europe has improved faster than expected, growth rates in China are not likely to see significant improvement over last year. Given the scarcity of growth and the value that can be created through consolidation, the M&A market should improve as long as capital remains available at reasonable rates. Despite low oil prices and weak global economies, U.S. corporate earnings should grow modestly as the U.S. dollar shifts from a headwind to a tailwind. Our portfolio company managements continue to actively deploy their free cash flow through share repurchases, dividends and opportunistic acquisitions which should bode well for future value creation.

Disclosures

Net performance reflects the deduction of advisory fees and expenses which reduce an investor's total return on investment. Returns presume investment for the entire period indicated and reinvestment of all interest income, capital gains, dividends and other distributions. Performance returns for 2015 are unverified estimates and have been computed by Cardinal. Depending on the timing of an investor's investment in the strategy, net performance for such investor may vary from the net performance stated herein. Past performance is not indicative of future results.

The Russell 2500™ Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "smid" cap. The Russell 2500 Index is a subset of the Russell 3000® Index. It includes approximately 2500 of the smallest securities based on a combination of their market cap and current index membership. The Russell 2500 Value Index measures the performance of small to mid-cap value segment of the U.S. equity universe and includes those Russell 2500 Index companies with lower price-to-book ratios and lower forecasted growth values. These indices are included merely to show the general trend in the small to mid-cap equity markets in the periods indicated and is not intended to imply that Cardinal's investments were comparable to the indices either in composition or element of risk. There is no guarantee that the performance of the strategy will meet or exceed any index. An investor cannot invest directly in an index.

The discussion of specific discrete investments in this newsletter (i) is included merely to illustrate certain investment processes and strategies utilized by Cardinal, (ii) is not intended to indicate overall performance that may be expected to be achieved by the Strategy, and (iii) should not be considered a recommendation to purchase or sell any particular security. The investments discussed herein are not a comprehensive list of securities or positions held by the Strategy. There is no assurance that any securities discussed herein will be or remain in the portfolio or, if sold, have not been or will not be repurchased.

Any projections, market outlooks or estimates in this newsletter are forward looking statements and are based upon certain assumptions. Other events which were not taken into account may occur and may significantly affect the returns or performance of the Strategy. Any projections, outlooks or assumptions should not be construed to be indicative of actual events which will occur.