SMID CAP CLIENT NEWSLETTER

Third Quarter 2017

Cardinal Capital
MANAGEMENT, L.L.C.

IN THIS ISSUE

- Market Commentary
- Performance Commentary
- Highlighted Investments:
  - *- Silicon Motion*
  - *- Kaman Corporation*
- Market and Portfolio Outlook

Market Commentary

Small, smid and large cap indices, as represented by the Russell 2000, 2500 and 1000 indices, rose 5.7%, 4.7% and 4.5% respectively in the third quarter. Within the Russell 2500, the value index rose 3.8% while the growth index increased 5.8%. For the quarter, the value index lagged its growth counterpart due to higher weightings in the poorly performing real estate and financials sectors and lower weightings in the better performing information technology and industrials sectors. Smid cap value stocks were relatively flat for the year until the President presented his tax reform plan in September. This was due to fading optimism that the administration could pass tax or regulatory reform after the President failed to build enough Republican support to repeal and replace the Affordable Care Act. After the release of the tax plan in September, the small cap value index rose sharply as investors began to discount again the potential economic benefits by gravitating toward smaller and more cyclical stocks.

Second quarter GDP rose at a 3.1% annual rate driven by strong consumer spending. During the third quarter, consumer and business sentiment improved as the unemployment rate held at a 16 year low despite industrial production dipping modestly due to Hurricane Harvey. Inflation remained below the Federal Reserve's 2% target level. As expected, the Federal Reserve left short-term interest rates unchanged at their September meeting but did decide to start slowly unwinding its quantitative easing program. Ten year government bond yields ended the quarter basically unchanged after falling sharply intra quarter once Yellen reiterated the Fed's plan to raise rates again in 2017. U.S. corporate profits rose 7.4% in the second quarter slightly below the 7.7% first quarter growth rate but solid nonetheless. The U.S. dollar weakened over the quarter as prospects for economic growth in Europe and other large international economies were better than domestic ones but began to recover following the Fed's upbeat economic and interest rate outlook in September. Even with political turmoil at home and abroad, U.S. equity market volatility has been remarkably low despite valuations that remain high on a historical basis.

Performance Commentary

The preliminary third quarter net of fee return for Cardinal's Smid Cap Value Composite, at 5.8%, outpaced the 3.8% return of the Russell 2500 Value Index. The main contributors to our relative performance were a higher weighting and stock selection in industrials as well as stock selection in financials, consumer discretionary, healthcare, and information technology. The primary detractors were stock selection in real estate, energy and consumer staples. In industrials, shares of measurement

FIRM OVERVIEW

- Experienced Value Investors
- 25+ Year Track Record
- Research-Driven Process
- FCF-Based Valuations
- Consensus Decisions
- Owned by Current & Former PMs
- $2.6 Billion Discretionary 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 Cont'd

provider Teledyne Technologies rose on better than expected quarterly results. Management also raised annual guidance to reflect the acquisition of e2v which expanded its digital imaging business and was accretive. In financials, the stock price of financial and real estate broker, BGC Partners, climbed on the announcement of the acquisition of Berkley Point, a multifamily loan originator and servicer, which should boost the growth of their commercial real estate segment and offer material cross-selling opportunities. In consumer discretionary, the stock price of auto dealer Lithia Motors lifted on better than expected results for the quarter and continued accretive acquisitions. In healthcare, the share price of Ligand Pharmaceuticals rose nicely on a beat and raise quarter, driven by strong royalty revenue and materials sales. In information technology, the stock prices of Match Group and IAC/Interactive, owner of 83% of Match, were up strongly on the successful launch of Tinder Gold which adds user features at an additional cost. In real estate, the stock price of New York REIT fell on a disappointing auction of its interest in One Worldwide Plaza, its largest asset, which will result in them retaining a 51% interest in the building that will likely be transferred into a nontraded liquidating trust. We sold the holding. In energy, the share price of oil and gas producer Parsley Energy fell despite a production beat and raise due to concerns about the higher gas and lower oil mix of its production. In consumer staples, the stock price of HRG Group, which owns approximately 60% of Spectrum Brands shares, fell as Spectrum's quarterly financial results were negatively impacted by weather, inventory destocking and product recalls.

The annualized net return of Cardinal's Smid Cap Value Composite since inception (July 1, 1992) is 12.7% versus 11.4% for the Russell 2500 Value Index and 12.3% for the Russell 2500 Index. Cardinal managed $2.6 billion in micro, small and smid cap value discretionary assets as of September 30, 2017.

Highlighted Investments

At Cardinal, we focus on finding companies with solid fundamentals at opportunistic valuations. Silicon Motion Technology Corporation is the leading merchant developer and supplier of NAND controller chips used in solid-state storage for smartphones, tablets, and personal computers. The company's customers include most of the NAND flash memory makers, leading tech OEMs, and manufacturers of storage device modules. Cardinal became interested in Silicon Motion because its business is perceived to be similar to that of its customers who are undifferentiated cyclical components suppliers. In contrast, Silicon Motion's business is differentiated and less cyclical because it has significant

PORTFOLIO TEAM

- Experienced and stable team of value investors
- Collaborative and dynamic process capitalizes on collective experience
- Consistency in team responsible for 25+ 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

Highlighted Investments Cont'd

software content that would take years and hundreds of millions of dollars to replicate. The software allows vendors to get new products to market much faster than the competition. The smaller size of Silicon Motion's controllers allows their customer more flexibility in product design. In addition, the company has the scale efficiencies which make them the low cost provider. As result, most of the technology OEM's have outsourced to Silicon Motion and Silicon Motions' pricing has remained stable which is unusual for a technology company. The other factor which attracted us was the accelerating demand for their customer's solid state disk drives which have rapidly taken market share from hard disk drives. The proprietary nature of the company's business model has been reflected in its financial performance over the last five years with strong growth in revenue, cash operating margins and free cash flow. Recent results have been hurt by supply shortages as vendors have had difficulty ramping 3D NAND capacity and we have used the price decline to add to our position. Nonetheless, Silicon Motion has remained very profitable and in fact announced a major share repurchase program. With a pristine balance sheet and an improving NAND supply situation entering 2018, Silicon Motion's revenue and cash flow growth should resume. We believe that with improving fundamentals and new products targeted to the enterprise market, the stock price will rise to better reflect its solid prospects.

Kaman Corporation is an industrial distributor and aerospace manufacturer with products ranging from programmable bomb fuzes to frictionless ball bearings. Founded in 1945 as a helicopter manufacturer, the firm diversified into the manufacture and distribution of musical instruments and the distribution of motion control products. In 2005, the board negotiated an end to the Kaman family's voting control of the company by eliminating its dual class voting structure. Cardinal then invested in Kaman as its legacy governance and unrelated portfolio of businesses had resulted in a compelling valuation. Two years later, its music operations were sold and the proceeds reinvested in acquisitions within the remaining businesses. As the company's stock price declined significantly during the credit crisis, we opportunistically increased our investment. Strategically, Kaman has expanded its industrial distribution business via acquisition to broaden its product offerings with higher margins lines such as fluid power and automation control. This business has faced sluggish demand and price competition from larger lower cost suppliers for several years. The crown jewels of the aerospace business are the bearings and the fuzing businesses which are high margin and benefit from strong intellectual property positions and long-term demand growth. The small and lower margin aerostructures business is being restructured and may be divested. Most recently, the company's largest shareholder has called for a vote

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Highlighted Investments Cont'd

at the May 2018 annual meeting to separate the industrial distribution business, a step which we believe should eliminate Kaman's conglomerate discount.

Market and Portfolio Outlook

Our near-term outlook for equities remains cautious as equity market valuations are full although most economic indicators point to steady growth for the balance of the year. With continued low inflation, the market is only anticipating one interest rate hike through 2018 and long-term interest rates remain lower than expected, particularly with the Federal Reserve starting to unwind its quantitative easing program. This environment has been supportive of higher equity prices but negative for the U.S. dollar, especially with economic fundamentals improving across much of the developed world. The M&A market remains active and this should continue as long as capital is available and inexpensive and high levels of shareholder activism continue to lead to corporate break-ups and sales of non-core assets.

Consistent with our investment discipline, our focus remains on the stocks of companies where business performance is generally less dependent on the growth rate of the U.S. economy. By attempting to limit macroeconomic risks and taking them only when we feel that we are being adequately compensated, we believe that we are reducing overall portfolio risk because tools under management's control are generally more dependable. Looking ahead, our portfolio companies continue to redeploy 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 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. The Russell 2000 Index consists of the 2000 smallest stocks in the Russell 3000 Index that represent approximately 10% of the total market capitalization of that Index. The Russell 1000 Index consists of the 1000 largest stocks in the Russell 3000 Index that represent approximately 90% of the total market capitalization of that Index. The Russell 2000 Value Index measures the performance of the small-cap value segment of the U.S. equity universe and includes those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. The Russell 2000 Growth Index measures the performance of the small-cap growth segment of the U.S. equity universe. It includes those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values. These indices are included merely to show the general trend in the small-cap equity markets in the periods indicated and is not intended to imply that Cardinal's investments were comparable to the index either in comparison 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.

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