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## Market Commentary

Small and large cap equity indices rose 15.5% and 11.8%, respectively, during the fourth quarter and fell 4.2% and 1.5%, respectively, for the full year 2011. Within the Russell 2000, the value and growth indices increased 16.0% and 15.0%, respectively, for the fourth quarter and decreased 5.5% and 2.9%, respectively, for the year. The value index rose more than its growth counterpart in the fourth quarter due to its higher weighting in better performing bank stocks, and a lower weighting in Healthcare which lagged. For the year, the value index lagged as the growth index had better performing stocks in the Industrials and Technology sectors, as well as a higher weighting in better performing Utility stocks. The returns in the quarter were consistent with a more optimistic view of the economy as cyclical stocks posted the strongest returns while more defensive Utilities and Consumer Staples stocks lagged.

During the fourth quarter, U.S. economic momentum picked up, brightening prospects for 2012 despite the challenges of falling state and local government budgets, weak European economies and a slowdown in China. The improving trend was driven by increased confidence resulting from the lack of economic fallout from the Congressional super committee failure, the avoidance of a larger European sovereign debt crisis and the Federal Reserve's forecast that interest rates would remain near zero until at least mid-2013. Although the U.S. government's debt situation will not be addressed until after the 2012 election, an improving economy can only help matters. The European economies, however, are at the mercy of the capital markets until structural solutions for the European Union have been agreed to and implemented. Domestic economic challenges also persist as the unemployment rate remains high and the residential real estate market still faces several million foreclosures. Despite these headwinds, the economic environment remains favorable for U.S. equities.

## Performance Review

The fourth quarter performance of Cardinal's Small Cap Value composite, at 10.3% net of fees, was solid in absolute terms but trailed the Russell 2000 Value Index return of 16.0%. Stock selection in the Industrials, Financials and Consumer Discretionary sectors and the drag from residual cash were the main detractors from our relative performance. In the industrials sector, shares of Kaman Corp. lagged as earnings fell short due to shipment delays that are expected to be made up in the fourth quarter. Our investment in CBIZ Inc. also declined modestly on lackluster organic growth. Among Financials, our lower weighting in bank stocks, which rose sharply, and smaller gains in the overcapitalized bank stocks that we do own were the key detractors. Within Consumer Discretionary, shares of Digital Generation fell sharply on concerns of increased competition in its core business and the stock of MDC

### PORTFOLIO TEAM

- Experienced and stable team of value investors
- Same team responsible for 19-year track record
- Collaborative and dynamic process capitalizes on collective experience
- Compensation based on portfolio



GENE FOX  
MANAGING PARTNER  
16 Years With Cardinal



ROB KIRKPATRICK  
MANAGING PARTNER  
11 Years With Cardinal



AMY MINELLA  
MANAGING PARTNER  
16 Years With Cardinal



RACHEL MATTHEWS  
PORTFOLIO MANAGER  
10 Years With Cardinal

## Performance Review Cont'd

Partners lagged as the company lowered its forecast for 2011 due to higher investment spending as well as client delays and deferrals. Mitigating these performance headwinds were significant contributions from our investments in Six Flags and Nelnet whose share prices rose on better than expected results. Cardinal's avoidance of poorly performing utility stocks, which lagged in a strong equity market, was also a positive.

For the year, the -0.1% net return of Cardinal's Small Cap Value composite exceeded the Russell 2000 Value Index loss of -5.5%. The primary reason for these better relative results was stock selection in the Financials, Technology, Consumer Discretionary and Materials sectors, partially offset by our higher weighting in poorly performing Industrial stocks and the absence of better performing Utilities holdings. Among Financials, Cash America, Nelnet and CYS Investments contributed meaningfully to performance due to strong results and attractive business models. In Technology, InterDigital's stock rose sharply on the initiation of a strategic process, at which point we sold much of our investment into strength at a gain. IAC Interactive Corp., our largest Consumer Discretionary investment, performed well as its financial results were robust and management continued to buy in substantial amounts of stock. Also, our largest Materials holding, Silgan Holdings, performed much better than its commodity-based peers as its businesses are based on essentially fixed processing fees which are inherently more stable.

The annualized net return of Cardinal's Small Cap Value composite since inception (July 1, 1992) is 12.3% versus 10.4% for the Russell 2000 Value Index and 8.7% for the Russell 2000 Index.

## Highlighted Investments

At Cardinal, we focus on finding companies with solid fundamentals at opportunistic valuations. For example, Teleflex develops, manufactures and markets medical devices designed to improve clinical outcomes, reduce infection, and improve patient and provider safety in an array of therapeutic and diagnostic settings. The vast majority of Teleflex's sales are single use disposable products. Having just completed its transition to a pure-play medical technology company, management is in the early stages of implementing its strategy, which entails accelerating revenue growth, expanding gross margins, reinvesting in R&D, and driving operating margins to 25%. Revenue growth will come from pricing initiatives, greater focus on GPO contracts, new product introductions and future "bolt-on" acquisitions. With margins that are below peer group averages, there is ample room for margin expansion through improved pricing and product mix.

### FIRM OVERVIEW

- Experienced Value Investors
- 19-Year Track Record
- Research Driven Process
- FCF-Based Valuations
- Consensus Decisions
- 100% Employee-Owned
- \$1.2 billion AUM

### OBJECTIVES

- Superior Risk Adjusted Returns
- Preservation of Capital

### HOW WE ADD VALUE

- Intensive fundamental research
- Detailed DCF-based valuation analysis
- Opportunistic stock selection balancing risk and return.
- Identify good businesses whose stocks are temporarily out-of-favor in structurally inefficient market niches where.
- Our annual return objective has always been 20%, making our valuations more conservative.
- Our discipline is identical to that used by companies and private equity investors, resulting in 60 of our investments being acquired since 1995.

## Highlighted Investments Cont'd

Although Teleflex's valuation is now more comparable to its medical device peers following the sale of non-core assets, the company retained substantial capital with which to make acquisitions to leverage its core healthcare franchise. With significant growth opportunities ahead, Teleflex should perform well regardless of the regulatory uncertainty plaguing the healthcare industry.

Global Payments is a processor of electronic transactions for merchants around the world. The company provides merchants with the capability to accept credit and debit cards from VISA, Amex, MasterCard and others. Even though the business is price competitive, Global offers a high level of service, critical to the middle market, and has important strategic relationships with banks such as HSBC. More importantly, electronic transactions are still growing steadily, particularly in emerging markets where governments are trying to increase tax collections. With 30% of its revenues in higher margin international markets, Global Payments should continue its solid organic revenue growth and profit margin expansion. With modest capital needs, the company generates significant free cash flow, which it will continue to redeploy through international acquisitions which leverage its scalable platform and accretive share repurchases. Ultimately, Global Payments is likely to be acquired as the processing industry continues to consolidate.

## Market and Portfolio Outlook

Entering 2012, we believe that economic growth will be moderate, short-term interest rates will remain low and inflation will remain benign. Our equity market outlook is cautiously optimistic as corporate earnings should continue to grow, albeit unevenly, and valuations of small cap stocks are generally reasonable. Merger and acquisition activity should increase from the depressed second half levels due to an improved high yield bond market and easier bank lending conditions. The cyclical high beta rally in small cap stocks that we witnessed in the fourth quarter is apt to continue if economic data remain strong. The wild card is Europe and as long as equity market valuations remain attractive and interest rates low, our portfolio companies are likely to continue to use their free cash flow for share repurchases and opportunistic acquisitions.

Cardinal's approach of opportunistically buying sound free cash flow producing businesses at inexpensive valuations has generated attractive long-term returns and we are confident that it will continue to do so. Recently, our portfolio company managements have become much more active in redeploying their cash flow in accretive ways including acquisitions and share repurchases. These actions will benefit 2012 results and also bode well for the future.