

Cardinal Capital Management, L.L.C.

SMID Cap Value

Second Quarter 2018



FIRM OVERVIEW

- Focus on Small & SMID Cap Value
- Experienced, Stable Team
- 25-Year+ Track Record
- FCF-Based Valuations
- 100% Independent, Partner Owned
- \$3.6 Billion AUM

INVESTMENT TEAM

Eugene Fox, III
Managing Partner/Portfolio Manager

Robert Kirkpatrick, CFA
Managing Partner/Portfolio Manager

Rachel Matthews
Partner/Portfolio Manager

Robert Fields
Partner/Portfolio Manager

Chitra Sundaram
Senior Research Analyst

Christopher Robertson
Senior Research Analyst

Michael Cotogno, CFA
Senior Research Analyst

Market Commentary

Small, SMID and large cap indices, as represented by the Russell 2000, 2500 and 1000, rose 7.8%, 5.7% and 3.6%, respectively, in the second quarter. Within the Russell 2500, the value index rose 5.8% while the growth index rose 5.5%, primarily due to the former's higher weighting in better performing energy and real estate stocks. From an economic perspective, the relative performance of small cap stocks stemmed from the increased prospects of a trade war as small companies with their more domestic business mix are generally perceived to be less impacted by tariffs. Defensive sectors including health care, real estate and utilities performed better than most cyclical sectors such as materials, industrials and technology as investors feared that these pending trade actions would reduce global growth. Financial services stocks also lagged, particularly banks which benefit from a stronger economy and higher interest rates. There were strong fund flows into small cap stocks via ETFs, resulting in the smallest, less liquid stocks and lower quality businesses within the Russell 2000 index outperforming.

Although the current economic expansion has run for nearly nine years, recent leading indicators suggest solid growth over the near term with few signs of an impending recession. Under new leadership, the Federal Reserve has continued to methodically raise short-term interest rates despite modest signs of inflation as the impact of the tax cut has yet to be felt and there is little slack in the labor force. However, even with substantial new issuance, the U.S. yield curve is now near its flattest level in over a decade as long-term interest rates fell on worries that a trade war would reduce business activity and dampen inflation. The Trump Administration announced tariffs on steel and aluminum imported from the EU, Canada and Mexico and on \$50 billion of imported Chinese goods. Fulfilling a campaign promise, the President is attempting to open markets and eliminate tariffs put in place by our trading partners that have resulted in lost domestic jobs, persistent trade imbalances and an uneven playing field for American companies. Whether Trump's negotiating strategy proves successful is unclear. Regardless, his tactics have clouded the economic outlook, hurt business sentiment and increased equity market volatility.

Performance Commentary

The preliminary second quarter performance of Cardinal's SMID Cap Value Composite, at 3.4% net of fees, lagged the 5.8% return of the Russell 2500 Value Index. The main detractors from our relative performance were stock selection in the energy, consumer staples and financials sectors along with a lower weighting and stock selection in the real estate sector. The primary contributors were stock selection in the industrials and health care sectors. In energy, Callon Petroleum's share price fell despite higher oil prices because of widening basis differentials in the Permian Basin caused by a short-term lack of adequate pipeline capacity and management's decision to finance the acquisition of adjacent acreage with equity. In real estate, our lower weighting detracted from relative performance as interest-sensitive REITs rallied when long-term rates fell. In addition, shares of property owner and developer Howard Hughes Corporation fell after the CEO sold stock to finance the purchase of a long-term warrant on a much larger number of shares. The stock price of consumer staples company HRG Group declined sharply after its 60% owned subsidiary, Spectrum Brands, reported weak results due to short-term manufacturing and distribution issues at two new facilities. Management has acted aggressively to fix these problems, but the market remains skeptical. In financials, the share price of asset manager, Affiliated Managers Group, was lower on disappointing fund flows and the uncertainty raised by the CEO's departure due to illness.

Cardinal Capital Management, L.L.C.

SMID Cap Value

Second Quarter 2018



Performance Commentary

In Industrials, shares of short line railroad operator Genesee & Wyoming rose after the company raised guidance due to a restructuring plan for its UK operations that management said would reduce annual operating costs by \$18 million. In health care, shares of Ligand Pharmaceuticals rose after the company reported strong first quarter results driven by record milestone payments and reaffirmed their FY2018 guidance. Shares rose further late in the quarter after the company announced that an existing OnmiAb partner had prepaid \$47mm in milestone payments to restructure its license agreement but remains liable for future royalty payments if the drug candidates receive regulatory approval and are sold commercially.

The annualized net return of Cardinal's SMID Cap Value Composite since inception (April 30, 2010) is 12.7% versus 11.2% for the Russell 2500 Value Index and 12.5% for the Russell 2500 Index. Cardinal managed \$3.6 billion in small and SMID cap value assets as of June 30, 2018.

Market and Portfolio Outlook

Our near-term outlook for equities remains cautious as valuations are full, the economic cycle is extended, monetary policy is tightening and the possible imposition of tariffs could both slow the economy and accelerate inflation. Nonetheless, the U.S. economy is currently growing at a solid pace and the beneficial impact of the U.S. corporate tax cut is only beginning to be felt. The prospects for domestic small cap stocks appear better than for large caps as the stronger U.S. dollar is less of a headwind and the impact of tariffs is less consequential. However, if the trade issues are favorably resolved or if the U.S. economy starts to slow, small cap stocks would likely underperform. The Federal Reserve still expects to gradually raise interest rates and is unlikely to deviate from that path unless the trade situation escalates or inflation increases meaningfully. With heightened uncertainty, we continue to prefer stocks where the success of the investment is based upon company-specific prospects and less dependent on the general economic outlook. Our high return requirements and long-term focus often make risk averse environments challenging for our relative performance because investors shorten their time horizons.

The strong M&A market, increased corporate share repurchases from repatriated cash and the lower U.S. corporate tax rate are all supporting equity valuations. Private equity and activist hedge funds continue to unlock value by improving operational performance, divesting non-core assets and selling companies. These activities have been and will remain a source of alpha in our portfolio over time. We remain optimistic that our portfolio companies will continue to redeploy their free cash flow through share repurchases, dividends and opportunistic acquisitions which should bode well for future value creation.

Cardinal Capital Management, L.L.C.

SMID Cap Value

Second Quarter 2018



Highlighted Investments



At Cardinal, we focus on finding companies with solid fundamentals at opportunistic valuations. FMC Corporation is a global chemical company which operates in two secularly-driven and high return segments. The agricultural chemical business provides crop protection and pest control through a portfolio of insecticides, fungicides and herbicides. The lithium business supplies carbonate as well as value added products such as hydroxide to battery manufacturers and metal to health care suppliers. The agricultural chemical division shifted its focus from basic R&D to reformulation and application while outsourcing its manufacturing to reduce the capital intensity of the business. The result was a doubling of sales and profits from 2009 to 2014. To expand the scale of its European operations, FMC acquired Cheminova in 2015. Two years later, FMC took advantage of divestitures required by antitrust authorities to complete the Dow-DuPont merger and purchased select agricultural chemical assets for cash and its health and nutrition business. This transformative deal should add over 50% growth to their EPS in 2018 and more in future years as additional synergies are realized. Just as important, the acquisition enhanced FMC's franchise value as it added significant R&D capabilities and made them a top five industry player. FMC's lithium business is in the midst of a multi-year growth phase as they add capacity to support the rapidly growing electric vehicle industry. With three-year customer contracts, the business has both volume and pricing visibility. Despite generalized lithium pricing concerns that have weighed on FMC's stock price this year, management is set to IPO the business later this year and spin it off to shareholders early in 2019. Although there is no publicly-traded pure-play domestic competitor, the valuation of SQM, a world-class Chilean producer would suggest an IPO valuation closer to 15 times cash flow. Applying that multiple to its lithium business would imply a valuation of about 10 times cash flow for FMC's agricultural chemical business which is inconsistent with its position as the only pure play major agricultural chemical producer, which should garner it a premium valuation given its market leading growth, modest leverage and strong free cash flow generation.



Gaming & Leisure Properties (GLPI) is a real estate investment trust which owns 38 gaming facilities across 14 states. Created by successful gaming entrepreneur and current CEO, Peter Carlino, the company was spun-off from Penn National Gaming in late 2013 to take advantage of the valuation disparity between REITs and regional gaming companies which made the sale-leaseback of real estate assets attractive to both parties. The leases are triple net in structure, where the gaming company tenants pay a primarily fixed rent with inflationary-based escalators plus all facility operating and maintenance costs under multi-decade terms that are cross-collateralized by the lease holder. In addition, the tenants' gaming licenses can only be used at GLPI's properties per the terms of the master lease agreements. GLPI's claim on the casino's cash flows is even senior to the debt service obligations of the tenants. With little in the way of operating costs, the company's free cash flow is largely paid out to shareholders as a dividend. Founded primarily with Penn National's gaming properties and the goal of diversifying operators and geographies, GLPI acquired the real estate of Pinnacle Entertainment in 2016. GLPI was able to add Boyd Gaming as a customer and extract higher rent and additional properties when Penn Gaming and Pinnacle announced their plans to merge their casino operations earlier this year. In addition, the company will acquire the real estate assets of the Tropicana properties when ownership shifts to El Dorado Resorts around year-end. With a significant acquisition pipeline, GLPI intends to diversify its customer base and grow its dividend which should reduce its valuation discount to other triple net lease REITs.

Cardinal Capital Management, L.L.C.

SMID Cap Value

Second Quarter 2018



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. 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.

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.