Cardinal Capital Management, L.L.C.

Small Cap Value

Third Quarter 2022

FIRM OVERVIEW

- Focus on Small & SMID Cap Value
- Experienced, Stable Team
- 30-Year Track Record
- FCF-Based Valuations
- 100% Independent, Partner Owned
- $3.5 Billion AUM

INVESTMENT TEAM

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Market Commentary

Small and large cap stock indices, as represented by the Russell 2000 and 1000, fell 2.2% and 4.6%, respectively, in the third quarter. Within the Russell 2000, the Value Index fell 4.6%, while the Growth Index rose 0.2%. The Value Index underperformed its growth counterpart due primarily to its lower weighting in the better-performing health care sector (particularly biotechnology stocks), poorly performing constituents in the industrials sector, and a higher weighting in the poorly performing real estate sector. The equity market rebounded early in the quarter on good corporate earnings, better than expected inflation data, and a rally in the bond market driven by recession fears and the hope that monetary tightening was nearly complete. However, a disappointing inflation report, stronger economic data, and a more hawkish Federal Reserve led to sharply rising interest rates, a two-decade high in the U.S. dollar, and a sell-off in the equity market as the likelihood of a recession rose. Investors, fearing higher interest rates and an economic downturn, became more risk-averse. Counterintuitively, low-quality and higher beta stocks led the market rebound and significantly outperformed defensive stocks during the quarter. With earnings confidence fading and interest rates rising, investors shunned profitability and valuation factors in favor of better balance sheets and less economically sensitive businesses. Although unusual, this behavior has happened before during periods of elevated fear and uncertainty, such as during the 2008 Great Financial Crisis.

U.S. economic growth is estimated to be barely positive in the third quarter, after a slight decline in the second quarter, mainly due to decreasing inventories and lower construction spending. Consumer and business confidence improved during the quarter despite higher interest rates and persistent core inflation as gasoline prices fell sharply from their peak following the Russian invasion of Ukraine. The labor market also remained strong, with the unemployment rate at 3.7% and job openings double the number of unemployed. Despite emerging evidence of economic weakness, the Federal Reserve raised the interest rate target it believes is necessary to bring inflation under control. With its roots in COVID-stimulus and supply chain issues, this bout of inflation will take time to dissipate. Wages are rising due to a lack of available and qualified job candidates, and housing rents are rising as starts are well below household formations. These inflationary forces will pressure corporate earnings as companies absorb higher labor, input, and interest costs amidst moderating demand offset by pricing power and cost-cutting efforts. However, consumers and businesses have been slow to pull back spending because their balance sheets remain in excellent shape from substantial excess savings and record profits. In addition, mergers and acquisitions activity has slowed materially as business valuations adjust to higher interest rates and lower equity prices. Unfortunately, monetary policy acts with a lag, so the Federal Reserve is unlikely to change course until there is a clear trend of falling inflation. This approach has increased the odds of a recession and means that equity market volatility will likely remain elevated.

Third Quarter Performance Commentary

The preliminary third quarter return of Cardinal's Small Cap Value Composite, at -7.7% net of fees, trailed the -4.6% return of the Russell 2000 Value Index. The primary detractors from relative performance were stock selection in the information technology and consumer staples sectors, a lower weighting in the better-performing health care sector, and a higher weighting in the poorly-performing communication services sector. In information technology, the share price of Taiwan-based Silicon Motion lagged after the likelihood of Chinese regulatory approval of its purchase by U.S.-based MaxLinear decreased due to worsening bilateral relations. The stock price of ACI Worldwide trailed its payments peers after the software provider reiterated its annual financial forecast but guided to a weaker third quarter. In consumer staples, the share price of Spectrum Brands fell after the Department of Justice filed suit to block the consumer products company's sale of its Hardware and Home Improvement segment to Assa Abloy. The parties to the deal intend to contest the DOJ's position as Assa Abloy has agreed to divest assets to satisfy antitrust concerns.

Although Cardinal was disappointed to trail the benchmark this quarter, relative performance has been similar at economic inflection points in the past. During these periods, investors generally exhibit a higher risk aversion, shorten their time horizons, and rely less on valuations due to decreased confidence in earnings. The amount by which the strategy lagged was nonetheless greater than expected because there has not been a period of both economic weakness and rising interest rates since the early 1980s, which may have added to investors' risk aversion. This environment has negatively impacted business valuations and brought the mergers and acquisitions market to a crawl as interest costs rise, allowable leverage levels decline, and business forecasts become less reliable. The Biden administration's more aggressive antitrust enforcement has also decreased the likelihood that deals will get consummated. As a result of these factors, the valuation floors that the strategy's portfolio companies carried due to their strong cash generation and the private market values of most of Cardinal's portfolio companies have been reduced, as was the case during the Great Financial Crisis.

Despite these challenges, as long-term investors, the investment team is optimistic because of the fundamental soundness of the strategy's portfolio company operations, their substantial free cash flow generation, ability to repurchase stock at very depressed prices, and compelling absolute valuation. Cardinal's portfolio is now the least expensive since late 2014, measured by forward-looking enterprise value to EBITDA. When viewed through a historical lens, the portfolio's current valuation level generally precedes three and five-year periods of solid relative returns for Cardinal's investors, even in periods of higher interest rates.

The annualized net return of Cardinal's Small Cap Value Composite since inception (July 1, 1992) is 10.8% versus 9.8% for the Russell 2000 Value Index and 8.9% for the Russell 2000 Index. Cardinal managed $3.5 billion in small and SMID cap value assets as of September 30, 2022.

Highlighted Investments

DT Midstream

DT Midstream is an owner, operator, and developer of natural gas gathering systems, interstate and intrastate pipelines, and storage facilities. Based in Michigan, DT delivers natural gas to utilities, power plants, marketers, large industrial customers, and energy producers across the Gulf Coast, Northeastern, and Midwestern United States, as well as into Canada. The company's infrastructure is in the attractive Marcellus/Utica and Haynesville formations which should supply half of U.S. natural gas by 2035. DT Midstream was spun-off from DTE Energy in the middle of 2021. Cardinal was attracted to the business because of its predictable revenue, with ninety percent coming from long-term take-or-pay contracts and fees paid to transport gas from producing wells. DT's cash operating margins are impressive and operating cash flow has grown nicely over time. At the time of the spin-off, management laid out a five-year plan to grow its EBITDA by forty percent, driven mainly by investments in lower-risk expansion projects for which they have signed customer contracts. Recent geopolitical events which have triggered a natural gas shortage in Europe have only increased the strategic value of the company's long-haul pipelines to the Gulf Coast, where liquified natural gas is processed and exported. DT currently has a five percent dividend yield and plans to grow the dividend in line with its EBITDA. In addition, the company plans to achieve net zero emissions by 2050, focusing on carbon capture. The combination of growth, predictability, and yield should produce attractive risk-adjusted returns.

Nexstar MEDIA GROUP, INC.

Nexstar Media Group, Inc. is the largest local television broadcaster in the United States. It owns or operates 200 full-power television stations in 116 markets and reaches 39% of U.S. television households. Cardinal has owned shares in the company for the last five years, and the stock has provided an attractive return. The initial investment thesis was based upon the company's prospects for strong net retransmission revenue growth and accretion from television station acquisitions. Net retransmission growth should remain significant given that broadcast television's share of retransmission revenue at 24% is still well below its equivalent ratings share at 39%. However, with Nexstar's station holdings at the FCC National Ownership Cap, television station acquisitions have given way to content acquisitions that it can leverage over its distribution channels. Nexstar recently purchased a controlling stake in The CW Network, where it owns a third of the affiliates and can now better control the programming. Although forty percent of Nexstar's revenues are core advertising based, revenue visibility through 2024 is very high because the company will renew over half of its retransmission subscribers in 2023 at higher rates, the pace of political advertising spending in 2022 is up almost 80% versus 2018, and the prospects for political spending during the next Presidential race are even stronger. Despite higher interest rates, management continues to favor share repurchase over debt repayment when attractive acquisition opportunities are unavailable. Over the past two and a half years, the company has repurchased 15% of its outstanding shares. With Nexstar stock trading at a high-teens average free cash flow yield and the company possessing significant business visibility over the next three years, Cardinal feels that Nexstar shares offer the potential for strong returns despite a very uncertain macroeconomic environment.

Market & Portfolio Outlook

Cardinal's near-term outlook for equities remains cautious. The economic outlook for 2022 growth continues to moderate due to rising inflation and interest rates and the strong U.S. dollar. Inflation is likely to remain well above the Federal Reserve's 2% target for the balance of the year and into 2023. However, inflation should begin to trend lower as the economy weakens and supply chains improve. Price pressures in the labor and housing markets may take more time to dissipate but could improve faster if businesses and consumers pull back spending more rapidly. Nonetheless, the risk of a recession over the next year has increased, though valuations in the equity market may already reflect that. Since interest rates have risen significantly and quickly from the pandemic low, both the equity and credit markets are looking for stability to affect price discovery. The mergers and acquisitions market has slowed due to these factors but should recover once valuations and interest rates stabilize. Regardless, Cardinal continues to prefer investments whose success is dependent on company-specific drivers with as many as possible under management control rather than solely relying on near-term economic growth to produce sustainable growth in free cash flow.

Performance Track Record

Cardinal Small Cap Value	**Gross**	**Net**	**Russell 2000 Value**
Inception-to-Date (July 1, 1992)	11.7	10.8	9.8
10-Years	8.4	7.7	7.9
5-Years	2.2	1.5	2.9
3-Years	2.4	1.6	4.7
1-Year	-17.4	-18.0	-17.7
Year to Date	-22.0	-22.5	-21.1
3rd Quarter	-7.5	-7.7	-4.6

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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 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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