VOLUME 21 • ISSUE 1 • JANUARY 2017

cardinal QUARTERLY

MARKET OUTLOOK

BY EVAN MANCER, CFA

After a weak 2015 and a dismal start to 2016, global markets ended up doing reasonably well with Canada being a star performer. The fact that oil prices increased by 70% from their 2016 lows certainly helped, but so too did the continued strength of the U.S. economy. This allowed the market to shrug off concerns of slowing Chinese growth earlier in the year as well as surprise negative events like Brexit. Markets even jumped after Donald Trump's election victory even though up to the election they had been falling every time he inched ahead in the polls. There is a saying that bull markets climb a wall of worry as they move higher and 2016 certainly fits the bill.

The Canadian S&P TSX had the highest return among developed countries in 2016, increasing by 21.6%, just ahead of the British FTSE-100, up 18.6%. However, the rise in the FTSE was more than offset by a 20% decline in the Pound relative to the U.S. dollar. Other global markets also performed well. The S&P 500 advanced by 11.7%, the ASX-200 rose 12.9%. The weakest developed country stock market was the Japanese Nikkei -225, which increased by 2.4%.

So have we scaled the wall of worry only to fall off the other side in 2017? We don't think so. Investors are less pessimistic than at the start of last year but still far from the euphoric bullishness that is typical of a market peak. Investors are still sitting on record amounts of cash and until the beginning of this year net funds were still flowing from equities to bonds. This trend has started to reverse over the past three quarters and could accelerate if interest rates start to increase and long-term bond prices suffer as we suspect will occur.

Valuations on the S&P TSX and the S&P 500 have moved above their historical averages, but are far from extreme levels such as what

continued on page 2...

25 YEARS

INSIDE THIS ISSUE

CARDINAL CAPITAL MANAGEMENT, INC.

occurred in the late 1990's. Given the energy market recovery and the prospect of a faster growing U.S. economy in 2017, corporate earnings should grow much faster than most investors expect, which will make valuations seem more reasonable. We think 2017 will prove to be another good year, and quite possibly an exceptional year for the markets.

Our primary thesis for 2017 being a year of good returns is the absence of normal bear market risk indicators. Bear markets are typically preceded by some combination of high energy and commodity prices, rising unemployment and/or a negative sloping yield curve (i.e. when short-term rates are higher than long-term rates) – none of which are currently present.

In our view, the most accurate of these three bear market predictors is the yield curve. A negative yield curve is bad because it discourages banks from lending since a bank's expenses are in short-term rates (deposits) and its revenues are in longer term rates (mortgages, commercial loans etc.). Recently, the yield curve has actually been steepening, even though the Fed raised short-term interest rates in December. This is because long-term rates have risen even faster as investors factor in the prospects for higher economic growth and inflation. We expect the Federal Reserve to increase rates three or four times in 2017, but also expect long-term rates to increase, keeping the yield curve positive. The Bank of Canada will likely hold off until the end of the year before considering increasing interest rates.

WTI oil prices have increased from a low of $30 to over $50 but are still cheap relative to most of the past ten years. The OPEC/Russia agreement to cut 1.2 million barrels per day of global oil production should continue to push oil prices higher, and we expect the group to keep the agreement this year unless oil prices move to the high $60's per barrel. In that case some members of the cartel may not be able to resist breaking the agreement. A recovering oil price alongside an accelerating U.S. economy should ensure strong GDP growth for Canada. Unemployment has been rising in oil dependent provinces for the past two years, but will start to drop again in 2017. We are already seeing reports of Canadian oil companies increasing their depressed capital budgets to take advantage of higher oil prices.

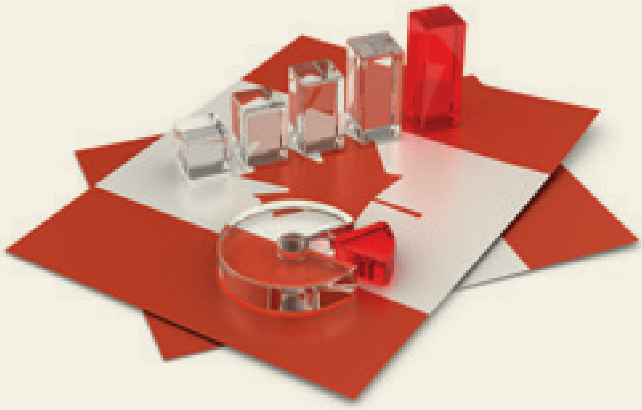
We continue to worry about high housing prices in much of B.C. and Ontario. Prices in Vancouver are clearly in bubble territory and Toronto is not far behind. The best scenario would be a flattening out or slight decline in prices over the next year or two, while the Canadian economy is doing well and employment is increasing. Hopefully, the B.C. government's 15% Property Transfer Tax will be a catalyst for this to occur.

The U.S. economy had good momentum going into the election and should continue to accelerate in 2017. Donald Trump's economic platform of lowering corporate taxes and increasing infrastructure spending creates long-term risks but should boost GDP growth, employment and wages in 2017. We believe that the big positive surprise for 2017 is that U.S. business spending will jump higher after years of slow growth as businesses look to increase productivity to deal with a tighter labour market and take advantage of continued consumer spending growth.

Of course, there is always the risk that an unexpected geopolitical event spoils our positive forecast. The Trump administration appears to be serious about renegotiating trade deals and many investors are worried about a disruptive confrontation with China. If the U.S. puts tariffs on Chinese goods, China will certainly retaliate, harming both sides. The possible election of Marine Le Pen and a further weakening of the EU is another risk. While these scenarios could cause a sharp downturn in the market, the downturn would likely be short, as the resulting economic pain would cause both sides to work quickly to come to a new agreement.

We continue to believe that financials could be some of our best performing companies under our forecast of a stronger economy with rising inflation, rising interest rates and still low unemployment. And we believe that our current high weighting in financials should help the portfolio experience another year of strong performance in 2017. Despite our positive view on the markets for 2017, our goal for the portfolios is to keep up with markets if returns are strong. We have been careful to maintain a healthy weighting in core defensive stocks such as utilities, telecoms and pipelines. Although higher interest rates tend to be negative for these companies, the companies we own are growing earnings and dividends and should do fine in a continued bull market. When markets do correct, we believe that these companies will allow our portfolios to do much better than the overall market.

We continue to believe that the Canadian dollar will inch higher versus the U.S. dollar, probably toward the high seventies, even though U.S. interest rates should increase faster than in Canada. First, we think most investors have already priced in a cycle of rising interest rates, and next, we believe that the Canadian economy will have a decent year in 2017, which will cause investors to start factoring in Bank of Canada interest rate hikes as well.



CARDINAL RULES

AVOID MARKET TIMING

BY HENRY HUDEK, MBA, FCSI, CFA

Here we go again. The Dow hits a new record at 19000 and threatens the 20000 mark. Other indices play in record territory. The phones start to ring: "I'm worried that the markets will take a hit and back off from these levels. Maybe we should sell some (or all) of my portfolio?" Market timing is once again an issue.

It is a perfectly logical question, until you start to consider reality. And reality can be summed up in three little questions: 1.) If the market keeps going up, when will you buy back in? 2.) If the market goes down, when will you buy back in? Now if you are retired, and taking money out of your portfolio, the most important is #3.) How will you replace the dividends you forego if you are not an owner?

The only reason one would consider trying to time a market is if one cares what the market value of your portfolio is on any particular day. If I believe that share prices will be higher in ten years, and I don't need the money in the meantime, then why would I sell today or tomorrow? When we ask clients why they care whether the market value of their account goes down by 10%, or say $100,000, the usual answer is "Because I don't want to lose money!" But by owning dividend payers, your money is making money. The only way you actually lose money, is by selling. Then you are actually losing out on collecting the dividends.

When it comes to housing, most people seem to get it. If we ask, "why don't you sell your house? You can make $100,000 more than you paid." They naturally respond – well I have to live somewhere, and I can't buy a house now for what I paid before. And that is the point: your money also has to live somewhere, and that somewhere had better earn you income. If you move it into a bank account – it sits there, earning nothing, while house prices go up or down, and you are stuck wondering when you should buy a place for your money to live.

The market value that shows up at the bottom of your statement is a measure of wealth, but you cannot live on wealth. You live on income, and income comes from where your money lives – from the dividends it earns, or the interest the bank will pay you. If it's not earning enough income, then you have to cash in some of your wealth, and if you are cashing in some of your wealth to take as income, then your wealth won't last forever. So don't forgo income just because you don't want to see the market value of your wealth bounce around. The more income you can earn with it, the less you have to sell to live on, and the longer it will last! And for people who aren't depending on income, reinvesting dividends is a great way to compound the growth in your portfolio.

In regard to the possibility of successfully timing the market, one must remember that the market is not usually driven by economics or financial considerations, but rather by mass psychology interpreting the economics. This particular bull is driven by expectations of a changed economic reality, predicated largely on Trumponomics. We do see record highs being set, but individuals are still being tempted to take their profits and sell out. This in itself is an indicator that there is still a lot of fear out there and that perhaps there is more upside to come. The market doesn't peak when it surpasses a certain ratio, or value; the market peaks when every investor is as fully committed to the market as they can be.

Lastly, is just a reminder, that we don't own the market; we own individual stocks. While most stocks to some degree move up and down together, individual stocks also move on their own merits. Some stocks even go up when the market goes down. Successfully predicting the movement of the market does not predict the movement of individual stocks. In the end, what investors own are individual stocks, and it is how those stocks move that determines an investor's total portfolio value at any particular time. To some degree this is how Cardinal does market timing. For every stock we watch, we have a firm view as to what that stock is worth based on its earnings potential. When the price of one of "our" stocks gets materially above what we believe it is worth, we sell it, or decline to own it. Instead of moving out of the market as a whole because we believe it is at risky levels, we move out of individual stocks that we believe are at risk of being overvalued. This has the added value of protecting value in downturns. Most Cardinal accounts do not decline as much as the market in a downturn. In 2011 the TSX dropped 8.7% while Cardinal dropped 3%. In 2008, the TSX dropped 33% and the S&P500 37%, but Cardinal was down 30% and 27.8% respectively. Don't let your fear of lower market values control you. Collect and grow income from quality companies and leave your wealth decisions in the hands of your Portfolio Manager.

REPORT ON FIXED INCOME

BY BRETT PURDY, CFA

When interest rates peaked in 1981, it marked the beginning of what would be a bull market spanning over 35 years. The fourth quarter saw a dramatic increase in yields that has investors wondering whether this bull market is finally at an end after reaching new historic lows in bond yields. The catalyst for the fourth quarter increase was the election of Donald Trump. His promises of higher infrastructure spending and tax cuts increased expectations of higher economic growth, as well as higher inflation and government debt which caused the spike in long-term bond yields in the U.S. with Canada following suit. The yield curves in both countries steepened as a result.

After reaching a low of 0.95% at the end of September, the Government of Canada 10-year bond yield surged 77 basis points to end the year at 1.72%. This is also 33 basis points higher than at the beginning of the year. Thirty-year bond yields only increased 16 basis points to 2.31% compared to the start of the year, but rebounded from a July low of 1.55%. Due to the inverse relationship between bond yields and prices, when yields rise, prices inevitably fall. The FTSE TMX Canadian Universe Bond Index reflects this decline in yields as the fourth quarter return for the index was a dismal -3.44%. For the year, the index gained 1.66%.

A rising rate environment presents a challenge for bond investors. For risk-averse investors and those who want to reduce the volatility in their portfolios, fixed income can be an important part of their investment strategy. One way to mitigate the risk of rising interest rates is to invest in short-term bonds. A 100 basis point increase to a 5-year bond yield will result in a smaller price hit than if it were a 10-year bond. Consider the yield of the Government of Canada 5-year bond, which is currently 1.12%. If the yield went up 100 basis points, the price would fall from $98.35 to $94.00 – a decrease of 4.4%. Now consider the Government of Canada 10-year bond, currently yielding 1.72%. The same 100 basis point increase in yield would result in the price falling to $89.97 from $98.12 – a decrease of 8.3%, almost twice the loss of the 5-year bond. These price changes are commonly referred to as duration. Duration is the percentage price change that occurs for every 100 basis points (or 1 per cent) change in yield.

At Cardinal we have kept the duration of our portfolios well below the benchmark duration, which is about 7.4, in order to minimize interest rate risk. We invest in shorter-term bonds with maturities less than 7 years. In a rising rate environment, the prices of the bonds in our portfolio will decline much less than the benchmark. We also continue to invest only in investment-grade, high quality corporate and provincial bonds in order to help provide a less volatile portfolio. ■

The Cardinal Foundation

2016 YEAR IN REVIEW

BY EMILY BURT, MBA, CFA
CHAIR, THE CARDINAL FOUNDATION

As our 9th year of The Cardinal Foundation wraps up, we are reminded of the positive impact we have had on our community over the years. The Cardinal Foundation was established so that we could take a more organized approach to corporate giving. Through the Foundation we have been able to assist charitable organizations that are in great need of support and may not otherwise be able to continue providing their services to those who need it most. Our hope is that each grant the Foundation makes will directly impact the lives of those in our communities. The Foundation's Board and Grants Committee really made 2016 something to celebrate. The following were some of the grants we made:

- Funding the repairs to a Monastery elevator for the St. Benedict's Foundation
- Purchasing kitchen supplies for Katie Cares' new kitchen in their respite home in Winkler, MB
- Supporting the Habitat for Humanity's Handyman Project with the purchase of a trailer, and tools
- Assisting the Oak Table by helping to fund new storage and furnishings to meet greatly increased demands on the organization

The Cardinal Foundation would not be possible without annual funding provided by Cardinal Capital Management and the ongoing commitment by our board members and grants committee. Thank-you to everyone for the time and energy you have put into the Foundation over the last 9 years!

The Board of Directors includes Emily Burt, Leah Cochrane, Brian Coughlin, Lauren Fischer, Sean Lawton, Ron Malech, DeWayne Osborn, and Terry Wong. The Foundation Grants Committee also includes David Aime, Melanie Burt, and Juanita Gielen. ■

INVESTMENT Q&A

How will the OPEC decision affect my portfolio?

Positively. First, it already has had a positive effect. Since the November 30th OPEC meeting where member countries agreed to reduce production by roughly 1mmbbl/d and the subsequent agreement from non-OPEC countries to cut 582mbbl/d, oil prices have risen by over 15%. Our holdings of Suncor, Cenovus, and Canadian Natural have increased by 9%, 7%, and 5% respectively.

Second, we believe the OPEC and non-OPEC supply cuts should continue to have a positive effect in 2017, contingent on a few items. First is compliance: there is skepticism due to OPEC's history and we will need high compliance (70+ %). Second is an extension of the cuts: the current deal is only for 6 months, after which it could be extended for another 6 months. Supply and demand forecasts from major agencies (taken with a grain of salt) require the extension for the requisite reduction in global inventories. Third is continued tumult in Nigeria and Libya: these countries are exempt from the OPEC cuts as conflict within these countries has reduced supply. Both nations returning to full production would result in a continued oversupply. And lastly the rebound in U.S. production will be constrained: U.S. production will rebound as oil hits $50/bbl; however, constraints on labour and increased services costs will likely keep the increase to 200-300mbbl/d.

We believe there is a high probability that the above items come to fruition. Further, forecasts do not take into account unplanned outages in unstable places like Venezuela. With this backdrop, we believe oil prices should rise to $60/bbl or higher as we see clear signs of the oil market rebalancing in the second half of the year. This would have a positive effect on energy holdings as current share prices factor in a price below our long-term oil price assumption of $70/bbl. JEFF RANCE, CFA

What has led to Sun Life's stellar stock performance over the past few years?

Over the past five years, Sun Life has been the best performing large-cap Canadian financial company with an absolute total return of 239%. For context, the next best performer over the same timeframe had an absolute total return of 161%. So the question to be asked is: what can this strong performance be attributed to? While recent expectations for higher rates stemming from the U.S. election have helped, it only accounts for a sixth of the total return.

During 2012, the new CEO, Dean Connor, made a series of strategic decisions to de-risk Sun Life's business model, capped off with the sale of its U.S. annuity business. This move was harshly criticized at the time due to the near-term earnings dilution (almost 9% of earnings at the time) and the potential upside to higher rates that was being given up. We, however, thought the company was making a very prudent move, citing specifically at the time that the transaction was a positive, longer-term move for Sun Life and that a de-risked insurance profile should command a better premium valuation. This thesis has played out just as we had hoped. The company ended up growing its core earnings by more than 50% through a combination of organic growth and acquisitions in more appropriately capital-light segments. The balance sheet has become one of the best among Canadian lifecos, and they have de-risked their business model. Investors have since been rewarded with a premium multiple.

In short, the strategic pivot made years ago helped to significantly strengthen the company's business profile and, along with help from recent macroeconomic conditions, has led to the strong performance of Sun Life shares. ROB LAM, CPA, CA, CFA

Will rising interest rates impact dividend stocks?

The impact of higher interest rates varies by sector and by the outlook for each individual stock. Sectors such as Utilities are seen as bond proxies or an alternative to bonds, particularly when bond yields are low and investors can earn a higher yield on stocks. Rising bond yields cause the spread between interest rates and utility stock dividends to narrow, prompting some investors to switch from utility stocks into bonds.

The rotation into bonds can cause Utilities to underperform the broader market although nothing has changed with the underlying businesses. Even if a utility's borrowing costs rise due to higher interest rates, a regulated utility is generally able to recoup those higher costs. When an entire sector underperforms, it can also provide the opportunity to buy a stock with better growth prospects than its peers. Fortis, for example, looks set to grow earnings faster than the sector as a whole and is expected to continue to increase the dividend annually.

For sectors like Insurance and Banking, rising interest rates can be beneficial. With banks, the spread between what they borrow at versus what they earn from investing or lending, tends to expand with rising rates. The benefit extends across the curve at this time, as we are coming off historically low interest levels.

While interest rate moves impact stock prices to varying degrees in the short-term, growth in earnings and dividends are the real key drivers of company valuations over the long-term. Dividend paying stocks often increase dividends in line with earnings growth, which provides inflation protection. Rising inflation and rising interest rates often go hand in hand. A fixed rate bond on the other hand pays interest at a set coupon rate; the coupon will not increase in the future. This means that with fixed rate bonds there is no protection against rising inflation, and the value of the bond will decline as rates rise. With quality dividend stocks, investors benefit twofold from rising dividends and owning companies that become more valuable as their earnings grow over time. SHEILA WILSON-KOWAL, CFA ■

WHAT IS YOUR LEGACY?

BY CLINTON REBEC, FCSI, MBA, CIM

True wealth planning isn't just about you and your financial needs. It also addresses the long-term needs of your family, including your loved ones living today and future generations. Financial planning is a lifelong process to help you make prudent financial decisions to further your goals in life. As you approach retirement, that plan will evolve to include your legacy. For those who are nearing or currently in retirement, a question should ultimately arise - what is your legacy?

At life's major junctures, it's common for people to start thinking about how they'll be remembered and what they'll leave behind. Even for those who are passionate about charitable giving, there will typically be financial assets that remain. In most cases, leaving a legacy for your spouse, children, grandchildren, and other causes you are most passionate about takes careful thought and planning.

Over the years, responses to the question "what is your legacy" come back ranging from a long directive of wishes to as short as writing the last cheque to Revenue Canada and hoping it bounces. Again, this is your money. You've worked extremely hard to build your life, and it's your planning that will lead to what will happen to your life's work. A survey by TD Bank in 2014 found that many Canadians aged 65 or older want to leave as much of their estate as possible to their family or charitable causes, but only 40% feel well prepared when it comes to making sure that will happen. Of those surveyed, more than a third don't take regular steps to keep their estate plan up to date. As a result, 25% of those surveyed have concerns their estate will pay too much in taxes or their heirs will disagree with their decisions or squander the inheritance.

When looking to take action to remedy those concerns, those who openly discuss their financial assets with their heirs, their children and generations to follow will see a significant benefit to how smooth the wealth transition may be. Communication is the fundamental key to building a legacy. The role that financial advisors play, including estate planning, investment management and tax plans, while extremely crucial to the wealth transfer process, can have a minimal impact on your lasting legacy. The information and roles that are bestowed onto your professional advisors, heirs and family today, as well as how clearly the message has been relayed, can help ensure your legacy wishes are respected.

With that said, people can benefit from looking at their legacy from two very distinct views. The first area is the much more tangible financial impact, while the second area deals with the emotional and intangible life aspect. When we look at the financial planning area of a legacy, a strong plan with prudent advice may contain and cover areas such as a will, health directives, insurance policies, tax and investment information. This list can go on, but the idea is you will answer questions as to where your funds are located, who are the beneficiaries and what is to happen with your assets.

As stated in past surveys, the concern rests on the lack of continued discussion and planning regarding succession and legacy. In 2015, a CIBC survey highlighted that the vast majority of Canadians planning to leave an inheritance have not discussed the topic with their family or a financial advisor. If people can openly communicate about their financial assets and allow their heirs a clearer understanding of what that picture will look like, they will be forming a foundation of trust and empowerment that will allow their values to carry forward. That brings us to the second area of legacy planning and undoubtedly the most important part - what you want your family to know.

Aside from the financial impact, legacy planning is an opportunity to pass on what you know. The same 2015 CIBC survey found that of those Canadians looking to leave wealth behind, almost half at 47% have not discussed the inheritance with the recipients. Additionally, 79% have not discussed the financial and tax implications of an inheritance with a financial advisor. Lack of communication about wealth transfer continues to create a gap between generations. This gap extends not just to the financial legacy, but to passing on your value-based traditions. When people plan a legacy, the most important thing they want to hand down is values and life lessons, not personal assets.

Once a financial plan is completed around your legacy, you can move forward by leaving behind those values and life lessons you wish to proudly cultivate in the generations to follow. Experts in the field of legacy planning consider a video as one way to get your values across, but there are other options that can yield a greater return, particularly because they're done with your heirs while you're still here.

Zig Ziglar was quoted as saying "in many ways, effective communication begins with mutual respect. Communication that inspires, encourages others to do their best." That is the platform from which core family values and life learning lessons stand a strong chance of being passed to future generations. Constant communication and storytelling have always been an effective means of engaging future generations. Talking about your values to your family, whether you do it formally or informally, isn't as easy as writing a will to lay out who'll get the family heirlooms.

Planning your legacy means discussing your legacy. You have the ability to create and pass on a legacy in your way. In a life far too short, you can never start soon enough to initiate conversations about your intentions with your professional advisors to develop a plan. Once this plan has initially been completed, make sure to consistently review it and revise accordingly. Then, introduce and communicate these plans to your heirs.

Your legacy is your personal story, tying together what you've accomplished, how you've lived your life and what you hope your heirs will take from you – in terms of both wealth and values. ■

CARDINAL RESEARCH

IN DEPTH WITH THE INDUSTRIALS

BY ANDREA CHAPUT

The last twelve months presented a tough environment for the industrial sector. However, through the diversity of the businesses and expansion of technology, there were bright spots that continued to drive company progress.

Sustainable energy and industrial software automation have been steadily gaining steam for many years. In 2016, it became evident how important these segments could become. In renewable energy, for example, GE and Siemens are now two of the top three players in the wind turbine market. Their businesses account for close to 50% of worldwide sales and gaining. Although the renewable businesses still account for less than 10% of their total respective revenues, this is expected to increase in the next five years. They have each made a concerted effort to invest in renewables and are experiencing well above average growth in these segments. The profile of an industrial company is changing, not only by business line but by the way they generate sales. The force of digitization and automation in the industrial world has taken hold, which has increased customers' needs for connected equipment and devices. Honeywell, for instance, now employs more software engineers than technical engineers. United Technologies has developed an App Store for its products, which will help mechanics in productivity and customer interaction for service requests. Remote monitoring capabilities for products (such as connected machinery or smart buildings) allow the industrials to optimize use and servicing schedules to enhance the customer experience. It also allows companies to improve their products through the analytics they receive from machine data. This in turn creates better customer loyalty and the ability to charge higher prices once the client is fully integrated into the technology. This is big business for these companies. For example, product embedded software already accounts for more than 50% of revenues in Honeywell's Aerospace and Climate Solutions businesses, which is expected to expand to 2/3s of revenues by 2020. Couple that with the added bonus that these revenues are generally recurring, which provides stability vs. the core equipment sales, and it's a win-win.

The second unifying story for the industrials in 2016 is the focus on enhancing margins to improve profitability for the long term. With nearly every industrial company across the board, there was a strong emphasis on finding ways of improving efficiencies in factories, managing raw material costs, and increasing automation. We also saw more drastic changes with asset sales and divestitures of lower margin businesses occur for several of our industrial companies, in order to better align their portfolios in higher growth areas. While GE has undergone a massive reconfiguration of its business away from financials, Honeywell has also spun off a low margin segment of its chemicals business, and UTX sold Sikorsky to focus on its core growth initiatives. These efforts should allow them to strengthen their business profiles and subsequently, help them achieve their growth initiatives for the long term. With the majority of these large shifts now behind them, the associated restructuring charges will diminish in 2017 and the benefits will begin to play through in their financial statements going forward.

While there are many moving parts, cash flows remain healthy with the industrials. The resulting cash from divestitures mentioned above will be re-invested into key initiatives and the remainder will be returned to shareholders. New acquisitions will likely focus on enhancing technological abilities and capitalizing further on green/smart trends. The majority of these should be small tuck-in acquisitions, as we do not foresee any significant portfolio changes in the next year for our companies. As for dividends, we continue to have a healthy growth forecast for increases in 2017. Honeywell remains committed to growing dividends faster than earnings, and United Technology sits in the mid-range of its target 35-40% payout ratio. Siemens has a wider bracket with a payout of 40-60% of net income which leaves ample room for growth as the newest proposed dividend is only 52%. The only caveat to that healthy growth forecast is that GE has been a special case with its portfolio transformation. It has temporarily shifted its focus towards share buy backs as it right sizes its share count to reflect the new business structure. Once the restructuring is out of the way, the core earnings double digit growth rate should support a return to double digit increases for GE's dividend.

With capital expenditure budgets starting to bounce back in the oil and gas sector, 2017 should see better revenue and profit growth than the prior year. Further, the pro-business policies of the new Trump administration may also help to boost confidence with the industrials' customers who have been previously cautious to make new purchases. After weathering difficult conditions in 2016, the industrials in Cardinal's portfolio look poised to make 2017 a good year.

THE CARDINAL STORY:
A QUARTER CENTURY IN THE MAKING

BY EMILY BURT, MBA, CFA

In 1992, Timothy Burt founded one of Manitoba's first independent Portfolio Management firms. By far the riskiest endeavor this risk-averse money manager would ever take, the idea of going out on his own had been germinating for a few years. After years of experience and developing confidence in managing money, he decided to become his own boss. This finally meant that Tim could put his enhanced Warren Buffett value philosophy to work. Fast forward 25 years and Cardinal now exists as a team of 37 employees who continue to spread the gospel that was Tim's own investment philosophy which has become known as The Cardinal Rules of Investing. These rules continue to drive our research, through fundamental security analysis, our portfolio construction, and our disciplined approach to helping clients preserve and enhance their wealth.

While much has changed in the world in a 25-year period, much with Cardinal has remained the same: our conservative, value investment philosophy; our buy-and-hold, dividend-focused approach suitable for long-term investors; seeking to earn above-average returns while taking below-average risk. Since inception, Cardinal's Canadian Equity mandate has performed at 11.30% per annum net of fees, vs. the S&P/TSX at 8.47% per annum.

We continue to believe that balanced, diversified portfolios of high quality stocks and bonds that are held for long-term performance objectives are the best way to achieve superior investment performance. The proof of using this consistent approach to build wealth is found in the numbers and is truly felt when our long-term clients thank us for protecting and growing their wealth over the last quarter century. We will continue to measure our success by how well our clients achieve their dreams and live fulfilling lives for the next 25 years, because that is really the point of Tim's dream. ■

Q4 DIVIDEND INCREASES

Canada	% Increase
Allied Properties REIT	2.0%
Bank of Montreal	2.3%
Canadian Natural Resources Ltd	8.7%
CIBC	2.5%
Granite REIT	6.9%
National Bank of Canada	1.8%
Sun Life Financial Inc.	3.7%
TELUS Corp.	4.3%

United States	% Increase
Becton Dickinson and Co.	10.6%
General Electric Co.	4.3%
Honeywell International Inc.	11.8%
VF Corporation	13.5%

International	% Increase
Siemens AG	2.9%

Source: Bloomberg
Reported in domestic currency

WHAT'S THE DIFFERENCE?
TIME WEIGHTED VS. MONEY WEIGHTED RETURNS

A recent regulatory change requires investment managers to now display Money Weighted returns to individual investors once per year, which Cardinal will provide after each year end. This change may go nearly unnoticed for the vast majority of clients, but have a significant effect on a select few. What is the difference and why will it affect some client returns differently than others?

Consider a simple example: Investor Bob invests $1 today and then loses 50%. In year two, he invests another $10 million and gains 100%, then Bob would be left with $20,000,001. However, in this extreme example, the Time Weighted and Money Weighted return calculations would be very different. The Time Weighted return does not take into account dollar values and so would calculate the total return as 0% (I.e. a 50% loss followed by a 100% gain, net out to zero). On the other hand, the money weighted return would be 41%, reflecting that Bob has doubled his money in two years.

Which approach is best? That depends on what you are measuring. Time Weighted returns are the best way to measure the manager since in most cases the manager has little control over cash flows. Regardless of whether Bob only had $1 invested in year one, his manager still lost 50% that year. Money Weighted returns on the other hand may be a better way to measure the actual client experience. Clearly, Bob will feel like his returns were much better than 0% if he has doubled his money, and the money weighted return captures this.

The vast majority of clients at Cardinal do not have such extreme inflows or outflows and will not see a meaningful difference in these two calculations. If however, you have invested like Investor Bob and you are wondering why your money weighted returns look different, now you know why. ■