MARCH 2021

Cardinal Update

The Banking Bounce-Back

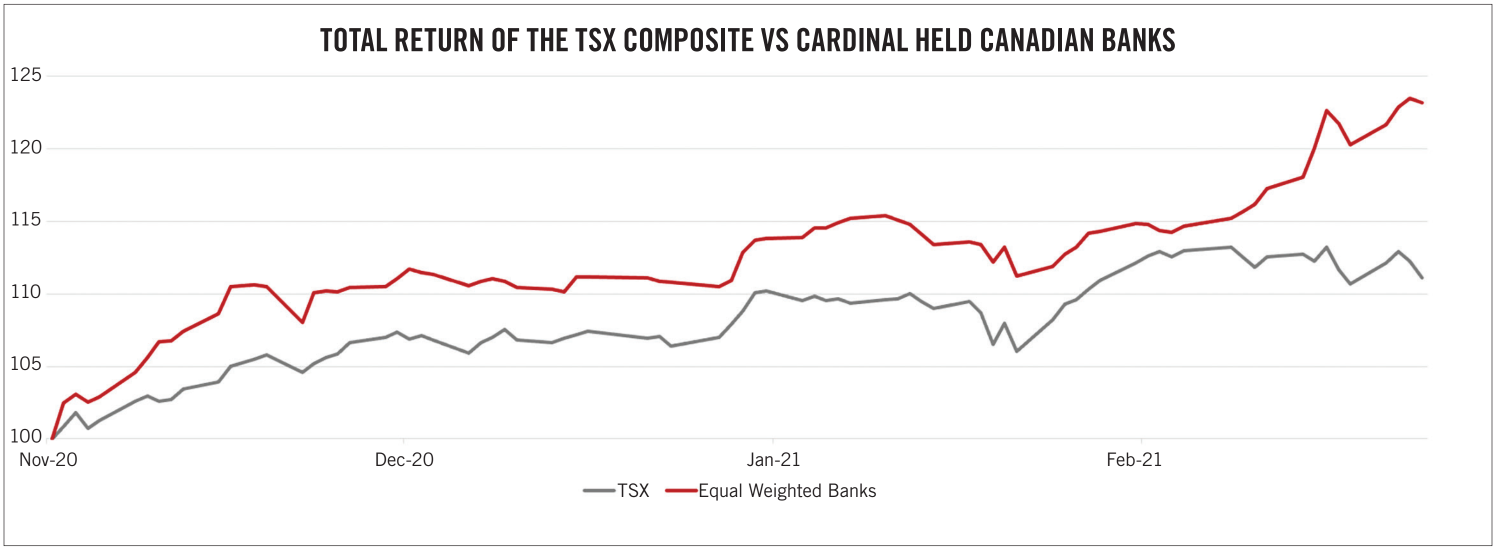
Since the first vaccination approval was announced by Pfizer-BioNTech on November 9, 2020, the Canadian banks and U.S. banks held in the Cardinal portfolios have tracked an average return of ~27% and ~50% as compared to the total returns of the S&P/TSX at ~12% and the S&P500 at only ~8%. What has led to the banks' comeback and what drivers keep us confident in the space?

The most apparent driver of the strong returns from the sector is the vaccination news itself which signals a hopeful beginning of the end to the current COVID-19 health crisis. With an end to the pandemic comes expectations of renewed economic growth of which banks are historically strong participants in the early cycle recovery through lending growth and capital markets activity.

The second driver of optimism has been the ability of the banks to weather the credit impact of the pandemic with help from government stimulus programs. These have helped bridge some of the economic gap created by the pandemic and have effectively socialized a portion of the economic losses that would have otherwise been borne by the banks. As a result, bank credit losses through this cycle will be far less severe than once thought at the onset of the health crisis.

A third driver has occurred more recently, and it relates to the steepening yield curve which has given rise to some optimism around improving lending margins. This is not a complete panacea to the margin pressure that we have seen over the past year, since commercial lending is driven by the short end of the curve which remains dictated by the Fed Funds / Bank of Canada target rate, but is still helpful nonetheless.

With all these drivers working in the banks' favour, there are a few other reasons why we continue to have confidence in the sector. First is that capital restrictions are expected to be lifted by regulators later this year, with the U.S. most likely to lift them before Canada. Capital levels have built up over the pandemic and all the banks we own



Banks have been equal weighted and include RY, CM, TD, BNS, BMO, NA. Assumes all dividends are reinvested. Holding period November 9 - March 4. Source: Cardinal Research, Bloomberg.

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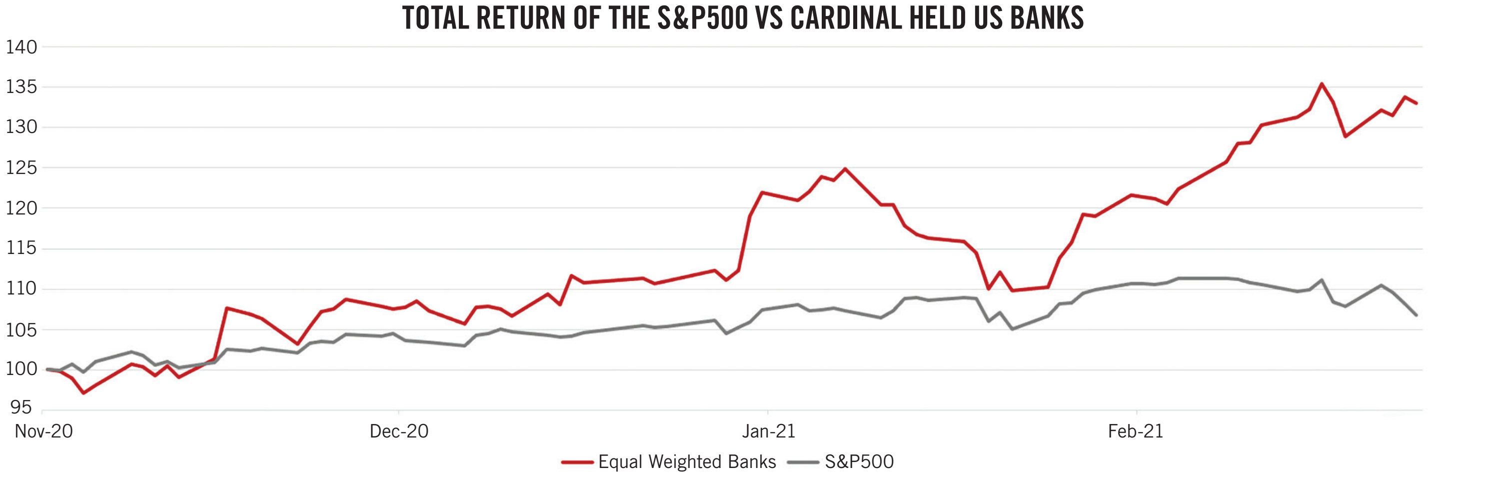
Cardinal Capital Management, Inc.



Banks have been equal weighted and include JPM, WFC, BAC, USB. Assumes all dividends are reinvested. Holding period November 9 - March 4. Source: Cardinal Research, Bloomberg.

now sit on significant levels of excess capital that can be deployed towards acquisitions, share buybacks, or increased dividend payouts – the last of which we of course welcome and expect to see some catch-up as a result of last year's pause.

It is hard to ignore the significance of the excess deposits on bank balance sheets due to the government stimulus. Banks have kept much of this in shorter-duration assets, but as time elapses and there is a clearer picture of how much of this will remain sticky, the banks can deploy this towards higher rate assets (i.e. loans or longer-dated investment securities) or reduce wholesale funding.

Lastly and at the core of our investment philosophy, we continue to believe that most of our bank holdings remain very reasonably valued, with this being particularly true in Canada where the banks trade at below average valuations despite what appears to be a very favourable operating future backdrop.

In all, we are pleased with how most of the banks we own have navigated the challenges of the pandemic and the overarching uncertainties that accompanied it. Our outlook is positive for the sector in the near term now that it has seen a reversal in sentiment over the last few months.

DEERE & COMPANY

Deere & Company was added to Cardinal portfolios in mid-2020 as a pullback in Deere's share price provided an opportunity to add this high-quality company with a proven long-term track record. It is not a new name for Cardinal either, as we have held it in the past. At the time of this purchase, we believed that there was good upside potential in Deere's share price due to an aging U.S. agriculture equipment fleet that would need to be replaced as well as the continued strong uptake of new technologies which typically come at a higher price point. The share price has more than doubled since our purchase as there has been a perfect storm of catalysts. Prices of corn and soybeans have been driven up to levels not seen since 2013 and this has led to a significant uptick in equipment demand for farmers. Outside of agriculture, the construction portion of Deere's business also stands to be a beneficiary from U.S. President Biden's highly anticipated infrastructure bill. Deere is now expected to grow earnings at a rate that exceeds 60% in 2021 and recently announced an 18% increase to its annual dividend.

DIVIDEND INCREASES

Cisco Systems	2.8%
Deere & Company	18.4%
Gilead Sciences	4.4%
Roche Holding	1.1%
SAP	17.1%
TC Energy	7.4%
Unilever	4.0%

(During the period February 1 – 28, 2021)