PEMBROKE

January 2018

Pembroke at 50

As we mark the start of a new year, we also start the celebration of an important anniversary for Pembroke. The company was founded in 1968, making this our 50th anniversary.

For 50 years, we have invested in entrepreneurial growth companies and served the investment needs of our clients. More than the simple passage of time, 2018 is an opportunity to reaffirm and celebrate our core values, our consistent investment philosophy and, most importantly, what we have achieved for our clients.

We have witnessed tremendous change and innovation over the past half century, and we have invested in many wonderful companies that have created significant wealth for their shareholders. We have also learned some tough lessons along the way. The wisdom gained every year has helped us focus on what matters; creating wealth for our clients over the long-term.

We thank all of our clients for having confidence in Pembroke, and we all look forward to celebrating our 50th anniversary with you as we continue the journey.

ON THE ROAD AGAIN

The investment team at Pembroke meets regularly during the year to examine and refine our approach to both stock selection and portfolio management. As we have witnessed over five decades in the investment business, to remain competitive in any industry, a certain degree of evolution is necessary. One constant, though, is the necessary effort of travelling to visit companies. It is an important part of the due diligence process that helps us to assess the calibre of management teams and the strength of their businesses. Depending on the company and the industry, travel can take many different forms. In the fourth quarter of 2017, Pembroke had the opportunity to get a behind-the-scenes tour of the new World Trade Center from the perspective of the telecommunications company responsible for outfitting the New York city landmark with wireless communication capabilities.

Boingo Wireless ("WIFI") is an investment that Pembroke has held since the end of 2015. Headquartered in Los Angeles, Boingo is a company that many people recognize only as a provider of WiFi access in North American airports. This service proved to be increasingly popular with the proliferation of mobile devices during the latter years of the 2000s.

Following the company's IPO in 2011, however, the environment changed as data costs plummeted and users relied less on WiFi hotspots. Boingo's stock suffered in the public markets for years as the management team engineered a change in focus and parlayed the expertise they built in their legacy business into network architecture services to wireless-carriers. This transformation went undetected by many investors. The powerful trend that Boingo positioned themselves for was that of mobile data consumption – a trend which has been robust and shows no signs of slowing.

Pembroke spent six months studying the business and the addressable market before buying the stock. At the time, the investment case was not without skeptics: only three brokerage firms published research on the stock, investors did not properly understand the real opportunity for the company, the operating leverage in the business model was underappreciated and the income statement was difficult to interpret. These circumstances created an excellent buying opportunity for Pembroke. The stock dropped from $9, when we first met the company in the summer of 2015, to below $6 by the end of that year.

During our visit in New York City, we examined maintenance closets and underground bunkers to appreciate and grasp the scale and complexity associated with building a dual WiFi-cellular network for the iconic World Trade Center. Boingo plays a critical role in the supply chain. Event venues and wireless carriers want their visitors and subscribers to have problem-free service experiences. Only a robust network can deliver this level of service. Venues do not have the capabilities and wireless carriers do not have sufficient capital to reach all venues. Boingo provides this architectural expertise, and their independence pleases both venues and wireless carriers who pay much less than they would if they built the network themselves.

The stock increased from $6 to $23 as earnings expanded and the company, now discovered, earned a higher earnings multiple. Pembroke portfolio managers call this powerful combination of earnings growth and earnings multiple expansion a “double play”. That’s what we’re in search of on the road: powerful earnings stories undiscovered or unappreciated by the market. Pembroke has been careful to risk manage the weight – both trimming and adding - during periods of volatility.

Following our tour of the World Trade Center, we are just as excited about the opportunity for Boingo Wireless today as when we first invested in the stock. With a market capitalization of roughly $1 billion, the company is hitting more investors’ radar screens. The share price increase from two years ago reflects a solid record of fundamental execution. We remain impressed by the number of venues still available to Boingo (“total addressable market”), the high returns on capital, the high free-cash flow generation and the dominant competitive position.

Just the Facts

Before providing qualitative comments on the quarter, we present some quantitative information regarding our top five Canadian and U.S. holdings.

Top Five Canadian Holdings

December 31st, 2017

Company	Q4 Price Change (CAD)	Revenue Growth, Current Fiscal Year	EBITDA Growth, Current Fiscal Year	Revenue Growth, Next Fiscal Year	EBITDA Growth, Next Fiscal Year
Gildan Activewear	4%	-1%	5%	5%	7%
Canadian Western Bank	17%	21%	16%	10%	11%
Solium Capital	6%	5%	-5%	18%	26%
DIRTT Environmental Solutions	23%	15%	26%	17%	69%
Stella-Jones	5%	1%	0%	3%	16%
Average	**11%**	**8%**	**8%**	**11%**	**26%**

Top Five U.S. Holdings

December 31st, 2017

Company	Q4 Price Change (USD)	Revenue Growth, Current Fiscal Year	EBITDA Growth, Current Fiscal Year	Revenue Growth, Next Fiscal Year	EBITDA Growth, Next Fiscal Year
BofI Holding	5%	17%	20%	14%	23%
Carbonite	14%	19%	31%	9%	31%
Installed Business Products	17%	32%	44%	13%	25%
HMS Holdings	-15%	4%	27%	10%	13%
National General Holdings	3%	19%	-33%	5%	100%
Average	**5%**	**18%**	**18%**	**10%**	**38%**

Source: Consensus and Pembroke estimates

Overview of the Quarter

Introduction

North American equity markets rose in the fourth quarter of 2017, capping a strong year of gains. Economic health and growth showed up in data from falling unemployment rates to oil prices above $60 a barrel. The much anticipated corporate and personal income tax cuts promised by the US Republican administration were successfully passed in December, raising investor hopes that the positive economic climate and corporate earnings growth will continue in 2018. Controversial regulatory rollbacks across sectors from financial services to energy exploration are also serving as a positive catalyst for businesses. Currently, concerns such as North Korean belligerence and troubling trade negotiations - from Brexit to NAFTA - are being brushed aside as investors focus more on the here and now than the "what ifs" and associated risks. At the same time, certain industries have found themselves mired in uncertainty. The healthcare sector has been affected by policy shifts from the Obama administration to the Trump administration. As always, uncertainty has led hospitals and other players in the sector to temporarily pull back from discretionary spending and investment.

Pembroke's funds performed well over the course of 2017 and each equity strategy outperformed its primary benchmark. The investment team is cognizant of the strong economic backdrop and has many investments that are benefitting from the current climate. For example, the firm's US portfolios have four holdings directly tied to home construction. At the same time, Pembroke makes investments on a bottom-up basis, assessing each holding's long-term growth prospects, balance sheet, and respect for shareholder capital. Even holdings that are benefiting from economic tailwinds must offer a secular growth opportunity that is largely independent of the overall economy. Similarly, Pembroke does not exit sectors due to temporary headwinds. In the case of the healthcare sector, trends in demographics and cost increases are not abating and should continue to drive long-term growth in the sector.

Most importantly, Pembroke continues to respect valuations while pursuing growth opportunities. The firm's portfolios are diversified across numerous industry groups; holdings are generally cheaper and faster-growing than their benchmarks, and are generally financed in a conservative manner.

The firm has taken the upcoming tax cuts into consideration and believes that its holdings are reasonably valued using traditional metrics. For companies whose valuations have become a concern, the positions have been carefully risk-managed. Pembroke has invested in growth stocks for five decades and has seen what happens when valuations become extended and investor appetite for risk suddenly dissipates. In these instances, the firm has been willing to sell expensive positions that still show positive price momentum and to redeploy the gains into other investments. The investment team is optimistic about 2018 but will continue to manage its portfolios with valuation discipline.

US Commentary

Pembroke's US equity portfolios generated positive absolute results in the fourth quarter but trailed the Russell 2000 index. For the year, the portfolios performed ahead of the benchmark. Large capitalization indices, such as the S&P 500, generally outperformed smaller cap indices, led by strength in high profile technology and consumer stocks. Further, the rise in global currencies such as the euro helped fuel multi-national companies' results. Growth stocks significantly outperformed value stocks, reversing the trend of 2016. Pembroke's portfolios fared well in this environment, but returns were tempered by the investment team's discipline around valuation and profitability. As holdings broke out of their historic trading ranges, Pembroke frequently reduced their weights in the portfolio to reflect increased price risk. Similarly, the firm continues to avoid unprofitable companies and industries, including biotechnology. Pembroke will hold currently unprofitable companies if the path to cash flow generation and profits is clear. Typically, the portfolio weights of such holdings are limited. The investment team is confident that the portfolio is well-positioned heading into 2018 from both a growth and valuation perspective.

The shares of **GTT Communications ("GTT")** rose from $31.65 at the end of the third quarter to $46.95 at year end. GTT is led by a proven team of telecommunications executives who together with other insiders own more than 10% of the outstanding shares. GTT employs a capital-light model, leasing space on competitors' networks to provide global telecommunication services to Fortune 2000 customers. The company's main competitive advantage is its high-touch customer service in a market dominated by oligopolistic providers. GTT continues to consolidate smaller competitors and drive cross-selling and impressive profit margins. The company's capital-light model and high customer retention help compensate for annual price declines. GTT's intermediate goals of $1 billion in revenue and $250 million of pre-tax, cash operating profit are well within reach. While Pembroke has managed its weight in GTT, the company remains reasonably valued; its execution has been strong and growth prospects remain in place.

Pembroke's US equity portfolios have investments in two companies directly benefitting from the skyrocketing demand for data across an ever-expanding number of devices. Increased volumes of calls, texting, internet surfing, and video services are jamming telecommunication networks. One of those companies, **Boingo Wireless ("WIFI")**, is building WIFI networks in areas of high congestion to help large carriers manage spikes in data demand. Another example is **Dycom ("DY")**, which helps companies such as AT&T lay fibre-optic cable. DY's customers are large and their demand trends, when measured over months, can be lumpy.

Pembroke took advantage of short-term customer spending delays to build a position in DY. The firm added to its position after another such delay in the second quarter of 2017. Subsequently, Dycom management reported a 10% sequential increase in revenue backlog, and carriers such as AT&T highlighted that they expect to accelerate their fibre deployments on the back of the US's recently passed tax reform package. Both pieces of news contributed to a sharp increase in DY's share price in the final quarter of 2017. Most importantly, Pembroke believes the long-term opportunity for DY remains robust as carriers are under significant competitive pressure to deliver high-speed, reliable service to their customers.

Shares in generic pharmaceutical company **Teligent ("TLGT")** declined after the company posted third quarter revenue well below expectations. Teligent is a sub-$100 million revenue company with a robust pipeline of over 30 drug filings targeting $2 billion of addressable markets. While the company has had significant success filing applications and winning FDA approval with four abbreviated new drug applications (ANDAs) approved in 2017, the approvals to date have generally targeted relatively small revenue opportunities. In the meantime, its current portfolio faced unexpected competition and price declines, leading to the third quarter's disappointing results. Nonetheless, the available opportunity from future approvals far outweighs the downside seen in recent results. Pembroke expects a significant number of positive developments in the first three to four months of 2018. Pembroke's team will be carefully monitoring the company's near-term progress. In the meantime, Teligent's current revenue, pipeline of drug filings, and manufacturing facilities are encouraging.

Long-time holding **Acadia Healthcare ("ACHC")** was sold from the portfolio after delivering results and forward guidance below expectations. While ACHC was a successful investment for Pembroke's clients from inception to final sale, the last chapter was disappointing. ACHC, which builds and acquires mental health facilities, is run by some of the same senior executives who helped expand and sell Psychiatric Solutions, also a large player in the mental health market, in 2010. They were following a similar playbook at ACHC for the first several years of Pembroke's investment. In 2016 the company made a sizeable acquisition in the UK. While initial results were positive, the UK government's efforts to move mental health patients from the public system to private operators were slower than expected.

Canadian Commentary

2017 was a strong year for Canadian equity markets, with gains driven by improving economic conditions both domestically and abroad. Market gains were broadly based across industry groups, with the notable exception of the energy sector which struggled with volatile underlying commodity prices. Pembroke's Canadian equity portfolios generated positive absolute returns that outpaced the S&P/TSX Composite Index. The mandates benefited from strength in their information technology, real estate and industrial holdings.

Several stocks made significant positive contributions to performance in 2017.

Shares in **Tucows ("TC")**, a provider of mobile telecommunication services, domain name services, and fiber optic high-speed internet access, posted strong gains in 2017. Tucows acquired a competitor in the domain-name registrar business early in the year, and this transaction proved to be additive to the company's results. The company's financial performance exceeded the expectations of investors and shares performed accordingly through the year.

Shares in **BRP ("DOO")**, a manufacturer of recreational products such as snowmobiles, all-terrain vehicles, and side-by-side vehicles, performed well in 2017 as the company delivered impressive financial results. BRP enjoyed business momentum from market-share gains, successful product launches, and improving operating leverage. Moreover, the company returned capital to shareholders through share buybacks and dividends.

Shares in **Pure Technologies ("PUR")**, an industrial technology company providing systems for the inspection, monitoring, and management of water and energy infrastructure, surged in the fourth quarter of 2017 as the company announced it would be acquired by an industry peer at a significant premium. While business progress at Pure has been uneven at times, this transaction highlights the value of the long-term investments made by management in the company's technology platform and infrastructure.

Two stocks were significant detractors to performance in 2017.

Shares in **DHX Media ("DHX.B")**, a leading owner and producer of children's media content, underperformed during the year as operating results failed to meet investor expectations. The company completed the acquisition of the Peanuts and Strawberry Shortcake brands earlier in the year, but performance from DHX's existing businesses was disappointing. Despite the short-term setback, we remain convinced in the underlying value of DHX's properties. The board of directors of the company has announced the commencement of a process to evaluate potential strategic alternatives focused on maximizing shareholder value.

Shares in **Birchcliff Energy ("BIR")**, a natural gas producer with assets focused on the Montney geological formation in the Peace River Arch, were weak during the year due to persistently low commodity prices. Infrastructure constraints and supply dynamics have combined to depress natural gas pricing, offsetting productivity gains made by producers such as Birchcliff. The company remains poised to deliver production growth in 2018 while maintaining a flexible capital budget and a low-cost profile.

The Pembroke team continues to perform company-specific research to identify attractive investment opportunities across a variety of sectors. While the geopolitical and economic environment is dynamic and ever-changing, the small cap universe continues to offer investors the opportunity to deploy capital into fast-growing companies with attractive risk and reward characteristics.

Balanced Fund Commentary

Pembroke's balanced portfolio, the **GBC Growth and Income Fund**, generated positive returns in 2017. The fund's gains were driven largely by capital appreciation in the equity portion of the portfolio. The fixed income portion of fund, represented by the **GBC Canadian Bond Fund**, earned modest absolute returns in 2017 in a challenging environment for bond investors.

Income in the balanced fund is generated from a combination of dividends and interest. The equity portion of the fund has a current annualized gross yield of 3.3%, while the fixed income segment of the fund is primarily invested in securities rated "A+" that, on average, have a collective yield to maturity of 2.6% and an adjusted portfolio duration of 4.7 years. The asset mix of Pembroke's balanced mandates did not change materially through the year, with approximately 28% of the portfolio invested in fixed income securities at December 31, 2017.

Two stocks stood out as outperformers for Pembroke's dividend mandates in 2017.

Shares of **Pollard Banknote ("PBL")**, a supplier of instant tickets and related services to the lottery industry, more than doubled in the past year as the company delivered excellent operating results to shareholders. Pollard has benefited from market-share gains driven by successful product innovation and the uptake of expanded production capacity. Moreover, Pollard completed the acquisition of INNOVA Gaming Group at a valuation that was accretive to shareholders.

Shares of **TECSYS ("TCS")**, a provider of supply chain software and solutions for the healthcare and distribution industries, delivered significant returns to investors in 2017. While an uncertain healthcare spending environment in the United States under a new presidential administration served as a headwind, the company nonetheless reported operating results that were viewed positively by investors. Growth in the company's distribution-oriented business and progress in realizing operating leverage surpassed market expectations.

Several stocks were significant detractors to performance during 2017.

Shares of **Mediagrif Interactive Technologies ("MDF")**, a provider of e-commerce solutions through online marketplaces and through publishing and procurement services, declined markedly in 2017. The company has been challenged with negative organic growth in some of its core businesses leading to a corresponding deterioration in its

margin structure. While Mediagrif has a track record of making acquisitions to bolster its growth profile, acquisitions have been insufficient to offset the headwinds within its existing businesses.

Shares of **Peyto Exploration & Development ("PEY")**, a producer of unconventional natural gas in Alberta's Deep Basin, were weak through 2017 due to deteriorating natural gas pricing. While Peyto has established itself as a disciplined allocator of capital and one of the lowest cost natural gas producers in Canada, the challenging environment has led to uncertainty regarding the appropriateness of the company's dividend policy. As such, Pembroke has divested its position in Peyto from its dividend-oriented mandates.

The performance of the equity portion of the fund has been strong. As a result, the Pembroke team is continuously looking for opportunities to redeploy capital into more attractive risk/reward investments. While the fixed income market has been difficult for investors given the prevailing environment of low yields, the fund's bond portfolio is well positioned for higher interest rates given its exposure to floating rate securities and its relatively short-term maturity profile.

International Equity Commentary

The fund's emphasis on high growth companies with favorable earnings trends supported relative performance during the period. The **GBC International Growth Fund** earned a positive return for the year, ahead of its benchmark, the MSCI ACWI ex-US Small Cap Index. From a sector perspective, positive stock selection effects within the consumer discretionary, consumer staples and industrials sectors were notable contributors, more than offsetting negative stock selection in the information technology and materials sectors. From a geographic perspective, stock selection effects were strongest within Japan and the emerging Asia region, offsetting underperformance within Europe and Latin America.

Consumer discretionary stock selection was bolstered by strong fundamental business trends at hotel operator **China Lodging Group (HTHT US)**. Within consumer staples, UK-based **Fevertree Drinks (FEVR LN)** was another notable contributor, driven by solid sell-through trends at existing accounts in addition to distribution gains as retailers added more shelf space for higher margin premium mixers. In contrast, information technology stock selection was hampered by do-it-yourself website development company **Wix.com (WIX US)**. Although Wix posted better than expected financial results, the market was disappointed in management's higher R&D spending outlook for 2018 – which could weigh on near-term profit margins. Materials stock selection was adversely impacted by wood-based cellulose fiber producer **Lenzing (LNZ AV)**, which lagged on concerns about viscose capacity additions and weaker pricing.

The fund maintained overweight positions in the financials and industrial sectors during the period, offset primarily by a continued underweight position in the real estate sector. Geographically, the fund's allocation to Europe was reduced during the period, while allocations to Japan and emerging markets were increased.

The low-volatility regimes in the equity and fixed-income markets carry potential risks. When change comes, it will likely be difficult, because markets have been shielded for some time from the natural cyclical behavior of negative economic and market forces. Sudden inflationary pressures and wage growth acceleration could alter investor return expectations, driving bond yields and volatility materially higher, while potentially triggering equity leadership rotation both across and within sectors. Financials, for example, would be expected to benefit from higher rates, but increased caution would be warranted for financially leveraged companies. We are mindful of these risks.

Despite the growing likelihood of a cyclical slowdown within the technology sector, we believe that strong secular growth will continue. From a geographic perspective, we believe that emerging markets continue to offer attractive investment opportunities. Opportunities exist to invest in China's growth, for example, but significant share-price gains in 2017 pose the threat of a near-term reversal in share price momentum.

FIXED INCOME COMMENTARY

The **GBC Canadian Bond Fund** earned a positive return for the year, but underperformed its benchmark, the FTSE TMX Canada Universe Bond Index.

Markets were strong with healthy economic news in both the US and Canada. The US Federal Reserve raised rates in December for their third increase of 2017, with the promise of more to come, especially after the US Congress enacted substantial tax cuts. The Bank of Canada held rates steady during the quarter, with concerns about the coming effect of tighter mortgage lending rules and the ongoing NAFTA negotiations.

In the Canadian bond market, strong demand for significant new issuance early in the quarter helped initially to push yields lower. As the quarter progressed, better than expected job, wage growth and unemployment news buoyed short term interest rates and the yield curve flattened. Falling long yields created a large difference in returns between long and short maturities. For the quarter, corporate bonds outperformed Canada bonds, but underperformed the broader market because of the outperformance of long maturity Provincials. Long maturity bonds were strong performers, especially names such as 407 and TransCanada Pipelines.

With over 22% of the fund invested in floating rate notes at the end of the quarter, the **GBC Canadian Bond Fund** continues to be well positioned if rates rise in 2018. Canso Investment Counsel continues believe this stance is prudent, as investors are not adequately compensated for duration risk with long Government bond yields at 2.3%.

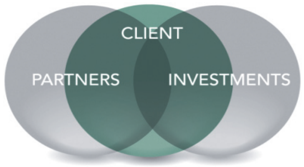
Outlook & Conclusion

2017 was a successful year for Pembroke's funds. A combination of growth in per-share earnings, improving fundamentals and recently enacted US tax cut, have the potential to drive equities higher over the medium term. In Canada, natural resources stocks have started to react to rising commodity prices. Pembroke's investment team is cognizant that valuations have expanded over the past year and we are taking appropriate action within the portfolios to manage risk. At the same time, new and exciting opportunities have been identified across all mandates, leaving your manager optimistic about the outlook for 2018. When it becomes difficult to find new investments at attractive prices, it can be a sign that markets are overvalued. Despite a generally high level of valuations, Pembroke's investment team continues to find opportunities to invest. Indeed, herding into high profile stocks and sectors appears to have left some companies significantly undervalued. The takeover of Canadian holding **Pure Technologies ("PUR")** in late 2017 at more than a 100% premium demonstrates just how far private and public markets can diverge. The US's decision to lower taxes on repatriated funds could very well lead to more takeovers of small and mid-sized companies. Pembroke does not invest in companies based on takeover expectations, but more capital chasing after investment opportunities may continue to support the valuations of smaller companies. We wish all our clients a prosperous 2018.

Business Update

Further to the special meetings of holders of the GBC Mutual Funds held on January 8, 2018 (the "Meetings"), Pembroke Private Wealth Management Ltd., the manager of the GBC Mutual Funds and Pembroke Management Ltd. (collectively "Pembroke") are pleased to announce that the unit holders overwhelmingly approved the new fee payment model. The management fees in the GBC mutual funds will now be paid by the unit holders through the redemption of units rather than by the funds. This new approach results in enhanced fee transparency, aligns the mutual fund fee structure with the pooled fund fee structure and in certain cases results in reduced fees.

It is expected that the changes approved by the holders of the GBC Mutual Funds will be implemented at the end of January when regulatory approval is received.



ALIGNMENT *of* INTERESTS

THE FIRM

Pembroke Management Ltd. was founded in 1968 and is based in Montreal. Pembroke's business and investment philosophy is rooted in the concept of ownership. Owners do what is in the long-term interests of their customers and stakeholders to maximize their own wealth. For this reason, Pembroke will, more often than not, back management teams that either own significant stakes in the companies they manage or whatever they own represents a significant part of their personal wealth. Furthermore, Pembroke tries to not take unnecessary risks in its investment portfolios because the Pembroke partners are large shareholders in the firm's funds. The result is a powerful alignment of interests.

Pembroke is registered as an Investment Advisor in Quebec, Ontario, British Columbia, Alberta, Manitoba, the United States, Denmark and Ireland. The firm manages segregated portfolios for institutional and high net worth clients. Pembroke Private Wealth Management is a subsidiary of Pembroke Management and is a mutual fund Manager and Dealer for the GBC family of mutual funds and the Pembroke family of pooled funds.

PEMBROKE PRIVATE WEALTH CONTACT

For additional information regarding Pembroke Private Wealth Management please call us in Montreal at 514-848-0716 or 800-667-0716 or in Toronto at 416-366-2550 or 800-668-7383, or refer to our website **www.pml.ca**.

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