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PERSPECTIVES

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As significant shareholders in our own funds, Pembroke employees pay close attention to our monthly statements, our quarterly newsletters, and our annual reports. We also write these documents and produce the results that fill the accompanying tables and performance charts. When a quarterly report coincides with the end of a decade it necessarily causes a little more reflection in us. We are inclined to take a few steps back and reflect at such a moment, not only on the results of our efforts, but on our methods and the meaning of our work.

One of the goals we strive for is to strike balance in our lives. This edition of Perspectives, like the others before it, draws on the work of our investment, sales, and operations teams. The **On the Road** piece reflects the belief of our investment team that to understand the changing world, you need to go into that world and experience its changes first-hand. In this edition, we focus on some of the changes we've witnessed over the decade but also on some of the timeless aspects of our philosophy of growth investing.

Our **Business Update** introduces new employees and developments at the firm but can never quite capture the flurry of activity going on inside. As we welcome new employees, we are also inviting new insights about how we can improve our business and make it more sustainable. This is a key dimension of growth. A firm that prides itself on continuity, we opened ourselves in the past decade to new people, to new ideas, to new strategies, and new systems.

Finally, we reflect on our activities **in the community** and the meaning of our work. We believe in the value of what we do: creating wealth for families and institutions, helping to allocate savings capital to the economy's most productive investment uses, and fostering the next generation of innovative entrepreneurs. Over the decade we have supported our community and the inspirational contributions being made in the world of arts, education, sports, medicine, and the environment and open spaces. It has been a memorable decade and we are privileged to enter the 2020s with colleagues and clients who share our values and support our vision.

On the Road

The Future Isn't What It Used to Be

As we reflect on the end of the second decade of the 21st century and look back at the events that shaped the last ten years, we are reminded that long-term forecasts carry a high degree of uncertainty. This is one reason we continue to go out on the road in search of great growth companies, instead of trying to forecast GDP growth, market returns or political outcomes. Real world outcomes always surprise us and turn out to be quite different from the forecasted outcomes. In this piece we reflect on some of the surprises of the past decade and also on some of the timeless characteristics shared by some of the best investments we found out on the road.

After experiencing two stock market crashes and two recessions during the 2000-2009 period, including the worst recession since the Great Depression, many were predicting more of the same for the next ten years. Popular business books such as "Fault Lines" and "The End of the Free Market" were highlighting structural failings in world economies and systems. If you had asked investors in 2009 if the 2010-2019 decade would be a rewarding one for investors, the answers, in that time of low morale, might not have been optimistic.

Looking back at these investments through the lens of our 51-year old rear-view mirror, they stand the test of time. While we live in an unpredictable world, many of the ingredients to successful investing in North American innovation and entrepreneurship remain the same.

The 2010s started where the last decade ended, with a sovereign debt crisis in Europe and rapidly rising bond yields in Greece, Italy, and Spain. That's where the similarities ended though and this decade turned out to be very different from its predecessor. It was the first one since the 1850s without a single recession![1] The Federal Reserve Bank and European Central Bank skillfully navigated their respective economies back on track, driving unemployment rates lower, and promoting slow and controlled economic growth. Accommodative monetary policy persisted throughout the decade with 10-year US government bond rates declining from 4% to 1.5% and borrowing rates even falling below zero in some countries.

[1] Source: BusinessInsider.com, For the first time in US history, a decade will pass without the country falling into a recession, December 8, 2019, Joseph, Zeballos-Roig.

The benign economic backdrop led to spectacular stock market returns, especially in the US. In December 2009, few forecasted that the next decade would be one of the best. It was possibly the most unloved bull market in history too as many investors were busy licking their wounds from the recent financial crisis, decrying low interest rates, predicting "normalization", or warning about the next crash. The current bull market began in March 2009 and has lasted 129 months. The next longest uninterrupted rally lasted 113 months and ended with the bursting of the dot-com bubble.

10-year compound annual returns (2009-2019)

In Canadian dollars unless otherwise noted

S&P/TSX Composite Index	6.9%
S&P 500	15.9%
Russell 2000	14.1%
NASDAQ	18.6%
MSCI All Country World Index	11.7%
FTSE Canada Universe Bond Index	4.3%
FTSE Canada All Corporate Bond Index	4.9%
Gold (USD)	3.3%

Source: Bloomberg

Looking back, it's fair to say it has been the decade dominated by tech companies, particularly Google, Apple, Facebook, Amazon, and Microsoft which have grown to unprecedented scale and brought us the first trillion-dollar sized private-sector companies. Advancements in smartphones, broadband speeds, and cloud computing had a major impact on the way people interacted and communicated during the decade. Indeed, online media sites facilitated the decade's major social movements such as the Arab Spring, Me Too, LGBT rights, and protests to combat climate change. Technology companies delivered outstanding stock market returns during this period (NASDAQ annualized returns of 18.6% for the decade, see table above).

The forgoing discussion highlights the fact that it is very difficult to accurately forecast stock markets. Great new opportunities emerge at all stages in a stock market cycle. This is a good reason to stay invested and keep looking for companies able to grow through the economic cycle. While popular technology stocks received most of the attention in the past ten years, our travels led us to some of the less well-known winners in Canada and the United States, including Axos Financial, Boyd Auto Group, Colliers/First Service, Constellation Software, and Gentherm. It is worth reflecting on some of the common characteristics of these businesses.

During the decade, Axos skilfully evolved from an on-line jumbo mortgage lender to a full-fledged US digital bank. From its humble Canadian beginnings, Boyd now operates one of the largest collision repair shop networks in North America with over 500 locations. Through numerous acquisitions, Constellation Software has successfully built a portfolio of mission-critical software solutions to serve customers in over 100 different countries. Colliers/First Service rebounded from the recession to become a global industry-leading real estate services firm. Finally, Gentherm successfully penetrated the new car market with their heated and cooled car seats evolving from a niche supplier into a systems provider for most of the leading car companies in the world.

While sound judgment and intuition were required to identify these investments early on, a strict and consistent process discipline forced us to focus our intuition and judgements on some key decision areas for each of these very different businesses. All five shared some key characteristics at the time of investment: all offered competitive products or services to large and growing addressable markets allowing for many years of growth, all were run by shareholder-focused management teams, and all funded their growth through internally-generated free cash flow. Looking back at these investments through the lens of our 51-year old rear-view mirror, they stand the test of time. While we live in an unpredictable world, many of the ingredients to successful investing in North American innovation and entrepreneurship remain the same. With this memorable decade of stock market returns behind us, we think there are as many exciting long-term investment opportunities ahead for our clients as ever. That is why we continue going out on the road.

Just the Facts

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

Top Five Canadian Holdings

December 31st, 2019

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
Colliers International Group I	2%	8%	17%	7%	11%
Kinaxis Inc	16%	26%	30%	11%	2%
BRP Inc	15%	14%	23%	10%	13%
Evertz Technologies Ltd	9%	4%	1%	6%	6%
Canadian Western Bank	-3%	6%	4%	8%	9%
Average	**8%**	**12%**	**15%**	**8%**	**8%**

Top Five US Holdings

December 31st, 2019

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
Stoneridge Inc	-5%	-5%	-16%	0%	11%
Installed Building Products In	20%	13%	17%	9%	15%
BioTelemetry Inc	14%	9%	8%	12%	13%
Euronet Worldwide Inc	8%	9%	23%	11%	16%
Woodward Inc	10%	5%	12%	6%	9%
Average	**9%**	**6%**	**9%**	**7%**	**13%**

Source: Bloomberg Consensus estimates

Overview of the Quarter

Out with the Old, In with the New…Welcome to the 2020s

The last decade began with markets emerging from the worst financial crisis since the Great Depression and ended with an exclamation point on one of history's longest-running bull markets. Historically low interest rates, tightening employment, and persistently low inflation were the hallmarks of the past ten years, creating dynamics previously unseen in the economy and certainly in public equity markets. Plain vanilla fixed income investments generated exceptional returns, outperforming most expectations significantly for this safe-haven asset class. Long-dated assets such as biotechnology and high-growth software stocks soared, while shares in profitable, steady-growth or cyclical businesses failed to keep pace. The rise of passive investing has exacerbated these trends, with money continuing to move into the largest index stocks.

Real estate prices surged as a result of low borrowing costs, leading many experts to warn of a bubble, only to see prices rise even further. Oil prices gyrated, challenged by changes in demand patterns and new global sources of supply. Fossil fuels are also facing the long-term reality of newer, alternative sources of energy, with innovation continuing unabated. Underappreciated amidst these cross-currents and the increasingly sour political climate, however, has been the enormous progress made in many areas. For example, while the move to alternative energy sources has vexed oil investors accustomed to ever-increasing demand, it offers the prospect of a cleaner world not dependent on the vagaries of politically unstable countries. That level of innovation has not been unique to the energy sector; technological leaps in the worlds of software and healthcare have created vast new opportunities for investors. While the 2010s played out differently than many forecasters had predicted, the constant of "change" and "new" was no different than in prior periods. In fact, some lessons from history seem to repeat themselves no matter the circumstances:

1) confronted by enormous risk and pressure, people and their governments generally find a way to press forward,

2) human ingenuity is a relentless driver of change and progress, and

3) public equity markets reward investors who stay the course during turbulent times.

Pembroke's portfolios participated in the broad rally of 2019. Supported by strong fundamentals and a favourable valuation backdrop created by the decline during the fourth quarter of 2018, many of Pembroke's Canadian and US holdings hit new highs. Of note, Pembroke's portfolio of high-quality Canadian small/mid capitalization stocks (which underperformed larger-cap stocks in recent years) recorded a very strong year. Pockets of

significant undervaluation, nevertheless persist and leave us encouraged as we head into 2020. We characterize the current portfolio as a mix of:

1) growth companies that have exceeded expectations, reached North American or even global scale, and enjoy commensurate valuations, and

2) under-appreciated shares in less well-known growth companies that still show compelling valuation upside.

In the US, a strong overall year for markets belied significant underlying shifts. The first half of the year was led by growth stocks, which benefited from low interest rates, limited exposure to US-China trade tensions, and secular growth in the face of muted economic expansion. The market surge in the second half of the year, and specifically the final four months, appeared driven by cyclical and value companies as investors seemed to position themselves for a resolution to the US-China trade war and potential economic acceleration.

While certain sectors and styles may fall in and out of favour for brief periods, Pembroke remains focused on investing in profitable, well-capitalized, shareholder-focused growth companies. The firm is also committed to running portfolios diversified across multiple industries and sectors. As the bull market passes the ten-year mark, the team is focused on balance-sheet strength to protect capital in the event of an unforeseen recession. Additionally, with many economists predicting another year of global economic growth below 3%, shares in companies able to grow their revenue and earnings at a solid pace, even in this constrained environment, should be rewarded. Finally, it would not be surprising for the trade war between the US and China to rear its head again, with companies exposed primarily to the US economy well-positioned to prosper regardless of these geo-political tensions. The underlying fundamentals and valuation characteristics of the portfolio, discussed in the "US Portfolio Commentary" section below and for the largest holdings in "Just the Facts", leave the Pembroke team confident in the US portfolio's positioning as we head into 2020.

Canadian Portfolio Commentary

Pembroke's Canadian equity portfolios posted gains in the fourth quarter of 2019, in tandem with buoyant equity markets worldwide. The easing of global trade tensions and continued accommodative monetary policies provided a healthy backdrop for stocks. While concerns remain about the duration of the current economic expansion and the potential for a recession, the imbalances that typically lead to a downturn are not clearly evident and Canadian corporate earnings growth is strong. In this environment, Pembroke's Canadian equity mandates outperformed the S&P/TSX Composite Index during the period.

While most industry groups were in positive territory during the fourth quarter, holdings in the technology, consumer discretionary, and financial sectors showed particular strength. In contrast, Pembroke's investments in the industrial sector declined in value during the quarter.

Two stocks made significant positive contributions to returns in the fourth quarter.

Shares in **Enghouse Systems**, ("ENGH CN"), which has a proven record of acquiring software companies at attractive valuations and subsequently raising their profitability levels, rose on the back of the impressive profit margins delivered in its fiscal fourth quarter of 2019 (October). Including the acquisition announced on January 2nd of 2020, the company has deployed $130m of capital in the past 12 months after deploying less than $40m in 2017 and 2018 combined. Management added to its ranks and invested in its back-office systems during that period, setting itself up to do more deals and integrate them at a rapid pace. With a strong balance sheet and consistent free-cash-flow generation, we believe the company is well positioned to make further acquisitions in 2020 and to continue its record of earning high returns on capital for shareholders. The company's CEO, Steve Sadler, is the company's largest shareholder.

Shares in **BRP** ("DOO CN"), a manufacturer, distributor, and marketer of recreational powersport and marine products worldwide, delivered fourth-quarter gains as investors embraced the five-year strategic and financial targets laid out by management at its investor-day presentation. The company anticipates driving double-digit revenue growth through market share gains in its side-by-side vehicle business, and through product innovation within its portfolio of marine products. Moreover, management foresees that revenue growth will be accompanied by margin expansion as benefits of scale are realized. Quarterly operating performance was also received well by the market, and BRP remains well capitalized.

Two stocks made significant negative contributions to returns in the fourth quarter.

Shares in **DIRTT Environmental Solutions** ("DRT CN"), a provider of custom, modular interiors for offices and other institutional settings, declined in the fourth quarter as the company reported softer-than-anticipated operational results and lowered its guidance for the remainder of its fiscal year. DIRTT is enduring a challenge with sales force productivity, which is dampening its revenue and profit outlook in the short-term. While a restructuring of its sales force will take some time and effort, we believe that DIRTT remains an innovative force in the interior construction industry and that its long-term prospects are attractive.

Shares in **Gildan Activewear** ("GIL CN"), a leading global manufacturer of activewear and socks, declined significantly in the fourth quarter as the company lowered its financial outlook for 2019 and 2020 as a result of weak end-market demand and customer destocking. In light of the lowered outlook for the company, we have divested our position in its shares and redeployed the capital into more attractive opportunities.

US Portfolio Commentary

Pembroke's US portfolios rose in the fourth quarter of 2019 to close out the decade, with 23 holdings closing within 10% of their 52-week highs and some eclipsing prior all-time highs. The portfolio's returns were buoyed by strong US markets; the S&P 500 Total Return Index jumped 9% in the final three months of the year, pushing 2019's total returns to over 31%. Pembroke's performance was supported by strong fundamentals in the underlying positions. (see further: Just the Facts). The portfolio's characteristics reflect Pembroke's approach to creating wealth: invest in growth businesses supported by strong balance sheets and stewarded by shareholder-focused management teams. At the same time, Pembroke runs US equity portfolios that are very different than their benchmarks. These differences can lead to brief periods of out/underperformance that may be more tied to fund flows and shifts in investor sentiment than company-level fundamentals.

After a strong first half of 2019 relative to the Russell 2000, Pembroke's US funds trailed the benchmark in the final quarter of the year. In fact, the portfolio's performance turned negative relative to its benchmark in early September. Three major factors contributed to this result:

1) the software and services sector, which is over 20% of Pembroke's US equity portfolios, was largely flat despite a strong move higher in the overall market,
2) biotechnology stocks, a sector in which Pembroke does not generally invest due to its low level of predictability and binary outcome risk, rose sharply, and
3) economically cyclical capital goods stocks, in which Pembroke has little exposure, rose from attractive valuation levels as investors anticipated a resolution to the China-US trade war.

Pembroke is sticking to its knitting despite these short-term market dynamics, convinced that while our investment approach does not deliver superior relative performance all the time in all markets, it will meet our objectives over longer periods of time.

Two stocks made significant positive contributions to returns in the fourth quarter.

Shares in **Paycom Software** ("PAYC") continued their march higher on the back of strong third-quarter 2019 results and a robust outlook for the remainder of 2019. In the third quarter, revenue rose over 31% and adjusted EBITDA jumped over 44%. Paycom is run by its founder, who holds over $2 billion of stock in the company. The company sells payroll and human capital management solutions, displacing older technology with its cloud-based software that is quick to implement, easy to use, and comprehensive. The company has a proven ability to cross-sell services into its existing customer base as well as to open offices in new regions and win significant market share from its competitors. Pembroke took advantage of the stock's weakness during October to add to our position.

Shares in **SiteOne Landscape** Supply ("SITE") appreciated approximately 22% in Q4 and 67% for the year, following solid organic revenue growth, an increasing contribution from M&A, and better-than-expected margin expansion. We believe that SITE is at a virtuous point in its lifecycle. The company is the lone business of scale consolidating the highly fragmented landscape supply distribution market. It is funding its acquisitions from internal free cash flow and reducing net debt on its balance sheet. Furthermore, SITE has reached sufficient scale whereby it is now starting to leverage its historical distribution center and technology investments and expanding margins.

Two stocks made significant negative contributions to returns in the fourth quarter.

The shares of long-time position **HMS Holdings** ("HMSY") declined after the company reported disappointing results for the third quarter of 2019. HMS, with a focus on the Medicaid market, helps state governments and insurance companies recover improperly paid medical expenses. The company has a unique and powerful data set which would be difficult to replicate and is reflected in its strong profit margins and dominant market share in the government sector. In recent years, the company has made several strategic acquisitions to grow into the population health management business, where it helps payors, such as insurance companies, identify and manage high-risk patients who can become quite costly. While some of the profit shortfall stemmed from growing pains in this emerging segment, much of the miss was caused by volatility in the timing of collections in its core business. Pembroke believes the company is well-positioned to grow revenue and profitability in 2020 and beyond.

Albany International ("AIN") shares declined during the fourth quarter. The company remains uniquely positioned to help aircraft manufacturers reduce weight through the use of their proprietary, woven composite materials. The company's first major win was with CFM (a joint venture between GE Aviation and French aerospace and equipment manufacturer Safran) to produce the fan blades, separators, and engine casings on roughly half of the Airbus A320 and all of Boeing's 737 MAX aircraft. In a well-publicized move, following two fatal crashes, Boeing recently terminated its CEO and temporarily stopped production of the MAX. While this development is unfortunate for Albany, it does not derail the MAX opportunity, nor does it change the company's ability to win business from other manufacturers seeking to reduce the weight of their aircraft. In fact, the company recently announced a collaboration with Airbus's "Wing of the Future" project to investigate the use of Albany's woven composites in future Airbus wing designs. In the meantime, Albany's core business, related to the manufacture of componentry for converting pulp into paper, is performing well and generates strong free cash flow. Nothing about the current situation changes Pembroke's view of the company's long-term prospects.

Pembroke Concentrated Fund Commentary

The Pembroke Concentrated Fund is a Pooled Fund. This is a prospectus-exempt product that is only offered to investors who meet the definition of an "accredited investor" under securities legislation.

The strategy gained during the quarter but did not keep pace with gains in its benchmark, the Russell 2000 Index. This was a departure from the previous three quarters during which the strategy outperformed the benchmark significantly. Overall, the Fund's full-year 2019 performance was

well in excess of the Russell 2000 benchmark. Contribution was evenly-distributed, with no noteworthy outliers and consistent contributions from the Fund's top holdings. Only seven of the 26 stocks owned throughout the year impeded absolute performance. At the end of the year, the fund held 18 stocks with approximately 90% of the portfolio weight in the US and the balance in Canada.

Two stocks made significant positive contributions to returns in the fourth quarter.

Shares in **Paycom Software** ("PAYC") continued their march higher following strong third-quarter 2019 results and a solid outlook for the remainder of 2019. In the third quarter, revenue rose over 31% and adjusted EBITDA jumped over 44%. Paycom is run by its founder, who holds over $2 billion of stock in the company. The company sells payroll and human capital management solutions, displacing older technology with its cloud-based software that is quick to implement, easy to use, and comprehensive. The company has a proven ability to cross-sell services into its existing customer base as well as to open offices in new regions and win significant market share from its competitors. Pembroke took advantage of the stock's weakness during October to add to our position.

Shares in **Kinaxis Inc** ("KXS CN") appreciated approximately 16% in Q4 and 52% for the year. The leading provider of cloud-based, software-as-a-service (SAAS) solutions for supply chain management reported third quarter revenues and adjusted EBITDA that gained 29%. The company announced several large new customer wins during the quarter that highlighted the global strength of this Canadian firm. Strong bookings and backlog provided increased visibility into future earnings and the company increased "all aspects" of its guidance.

Two stocks made significant negative contributions to returns in the fourth quarter.

Albany International ("AIN") shares declined during the fourth quarter. The company remains uniquely positioned to help aircraft manufacturers reduce weight through the use of their proprietary, woven composite materials. The company's first major win was with CFM (a joint venture between GE Aviation and French aerospace and equipment manufacturer Safran) to produce the fan blades, separators, and engine casings on roughly half of the Airbus A320 and all of Boeing's 737 MAX aircraft. In a well-publicized move, following two fatal crashes, Boeing recently terminated its CEO and temporarily stopped production of the MAX. While this development is unfortunate for Albany, it does not derail the MAX opportunity, nor does it change the company's ability to win business from other manufacturers seeking to reduce the weight of their aircraft. In fact, the company recently announced a collaboration with Airbus's "Wing of the Future" project to investigate the use of Albany's woven composites in future Airbus wing designs. In the meantime, Albany's core business, related to the manufacture of componentry for converting pulp into paper, is performing well and generates strong free cash flow. Nothing about the current situation changes Pembroke's view of the company's long-term prospects.

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company has made several strategic acquisitions to grow into the population health management business, where it helps payors, such as insurance companies, identify and manage high-risk patients who can become quite costly. While some of the profit shortfall stemmed from growing pains in this emerging segment, much of the miss was caused by volatility in the timing of collections in its core business. Pembroke believes the company is well-positioned to grow revenue and profitability in 2020 and beyond.

Dividend/Balanced Fund Commentary

The Pembroke Dividend Growth Fund is a Pooled Fund. This is a prospectus-exempt product that is only offered to investors who meet the definition of an "accredited investor" under securities legislation.

The **Pembroke Dividend Growth Fund** appreciated in value in the fourth quarter of 2019 in tandem with broad-based strength in equity markets. The apparent smoothing of global trade frictions and continued accommodative monetary policies from central banks provided a supportive environment for stocks. Fears of a recession persist, though growth trends and corporate profits remain reasonably healthy. The Fund outpaced the S&P/TSX Composite Index but trailed the S&P/TSX Dividend Aristocrats Index during the period.

Equity market strength was broadly based in the fourth quarter. The Fund's investments in the technology, industrial, materials, and real estate sectors were the most meaningful contributors to performance, while in contrast the Fund's holdings in the consumer discretionary sector suffered losses.

Two stocks made significant positive contributions to returns in the fourth quarter.

Shares in **Tecsys** ("TCS CN"), a global provider of supply chain software and solutions to the healthcare and distribution industries, gained in the fourth quarter as the company reported bookings and backlog statistics that demonstrated the traction it is gaining with customers. The addressable markets for Tecsys' solutions are large, providing an extended runway for revenue and profit growth for years to come. While we believe near-term results are being held back as the company transitions to a software-as-a-service model from an on-premises model, the move should ultimately lead to greater profitability and persistency of the business. Insider alignment with minority shareholders is high at Tecsys and the company's dividend is secured by a solid balance sheet and cash flow generation.

Shares in **Richards Packaging** ("RPI-U CN"), a distributor of packaging products to the pharmaceutical, cosmetics, food, and personal care industries, performed well in the fourth quarter following quarterly results underpinned by strong organic growth rates and attractive profitability. The company has a record of making disciplined acquisitions to augment organic growth and we believe it is well positioned financially to make future transactions while funding a conservative

dividend. Richards has minimal coverage from sell-side analysts and a low-key profile with financial market participants.

Two stocks made significant negative contributions to returns in the fourth quarter.

Shares in **Gildan Activewear** (“GIL CN”), a manufacturer of clothing such as t-shirts, sport shirts, fleeces, socks, and undergarments, declined in the fourth quarter as the company issued disappointing financial guidance for 2019 and 2020 as a result of weak end-market demand and customer destocking. In light of the challenging outlook for the company, we have divested from our holding in Gildan and redeployed the capital into other opportunities.

Shares of **Collectors Universe** (“CLCT”), a leading provider of third-party authentication and grading services for high-value collectibles such as coins and trading cards, declined in the fourth quarter after having performed strongly in the first three quarters of the year. The company’s operating results were stellar in 2019, with coin grading volumes rebounding from a lull in 2018 and trading-card grading activity reaching record highs. Moreover, the company has a strong balance sheet, earns high returns on capital, and pays a dividend that is well funded by cash flow generation. While the fourth quarter decline in CLCT’s shares was disappointing, we believe the fundamentals of the business remain strong.

Pembroke’s balanced portfolio, the **GBC Growth and Income Fund**, delivered gains in the fourth quarter of 2019 driven by the equity portion of the portfolio represented by the holdings of the **Pembroke Dividend Growth Fund**. Equity returns of the Fund were buoyed by general strength in risk assets as well as positive company-specific drivers.

The fixed income portion of the Fund, represented by the **GBC Canadian Bond Fund**, declined in value in the fourth quarter and offset some of the positive return generated by the equity portion of the portfolio. While the Fund’s fixed income investments generated positive returns for the year, fourth quarter results were negatively impacted by adverse interest rate fluctuations.

Income in the balanced fund is generated by a combination of dividends and interest. The equity portion of the fund has a current annualized gross yield of 2.9%, while the fixed income segment of the Fund is primarily invested in securities rated “AAA” that, on average, have a collective yield to maturity of 2.5% and an adjusted portfolio duration of 5.3years. The asset mix of Pembroke’s balanced mandates did not change materially through the year, with approximately 29% of the portfolio invested in fixed income securities at December 31, 2019.

International Commentary

The **GBC International Growth Fund** outperformed its benchmark, the MSCI ACWI ex-US Small Cap Index, during the fourth quarter and calendar year 2019, bolstered by favorable stock selection across most sectors.

Two stocks made significant positive contributions to returns in the fourth quarter.

Strength within the industrials sector was supported by UK-based **Diploma PLC** (“DPLM LN”), a globally diverse distributor of essential technical products across a range of industries. Diploma’s product portfolio is focused on aftermarket, services, and replacement demand. Spending on Diploma’s products is typically funded from operating cash flows rather than capital expenditures, contributing to revenue stability despite cyclical end markets. The company’s close customer relationships, strong market position, and replacement-driven demand have resulted in high and stable cash flow generation. We believe the combination of organic growth and value-accretive M&A should continue to produce strong earnings growth.

Sweden-based **Indutrade** (“INDT SS”) also contributed to fourth quarter performance. Indutrade is a leader in the Northern European market for industrial component distribution. The company is differentiated by its high proportion of proprietary products (38% of sales), a range of product offerings from high-quality suppliers, and a technically-savvy sales team, all of which help to reinforce close relationships with customers.

Two stocks made significant negative contributions to returns in the fourth quarter.

Partially offsetting these positive effects were stock selection in the information technology and financials sectors. Within the information technology sector, Japanese IT services provider **Nihon Unisys** (“8056 JP”) underperformed during the quarter despite solid quarterly earnings results which reaffirmed our investment thesis. Traditionally, Nihon Unisys was a big mainframe integration and services provider, but this business has fallen to 2% of revenues over the past decade from 25%. The company’s push into standardized products is timely as Japanese businesses are moving their technology into the new era, driven by better connectivity speeds (cloud computing).

Within the financials sector, UK-based specialty insurer **Beazley** (“BEZ LN”) underperformed during the quarter. The company’s earnings results were reassuring after investor skittishness following an earnings disappointment from a competitor firm. Despite investor concerns, Beazley’s catastrophe losses were within expectations and investment returns benefitted from falling bond yields. Management reported that they continued to experience double-digit premium growth across the business as a whole, with particular strength in cybersecurity—where Beazley is unique among insurers in having a dedicated business unit that assists policyholders at every stage of incident investigation and breach response.

Fixed Income Market Commentary

Most bond markets reversed course in the fourth quarter and gave up some of the earlier year-to-date gains. This performance appeared to be driven by strong equity markets and a US Federal Reserve indicating there would not likely be any further rate cuts through the election year of 2020. Markets also looked to sustained economic expansion, labour market strength, and contained inflation in the coming year.

Canadian yields rose during the quarter but narrowing credit spreads meant corporate bonds outperformed. Longer duration A-rated bonds underperformed both their higher and lower rated cohorts with short duration financials being the strongest performers in the corporate sector. Given their low yields, bonds still turned in an impressive return for the year. The Universe Index returned 6.9% and significant spread narrowing led to Corporates posting an 8.1% gain.

GBC Canadian Bond Fund Commentary

The Canadian Bond Fund returned -0.2% for the quarter which was 0.7% ahead of the FTSE Canada Universe Bond Index. For the year, the 5.7% return was strong in absolute terms, but was 1.2% behind the benchmark. The shorter duration of the Fund detracted from full-year performance as yields fell during 2019. Additionally, the Fund has a higher-quality bias which suppressed returns in the period as spreads narrowed. The floating rate note exposure contributes to the Fund being 2.7 years shorter than the benchmark duration of 8 years, yet it provides a healthy yield for the Fund. Canso continues to believe that the shorter duration positioning of the Fund is prudent as it will be protective in a rising rate environment. Although the Fund is shorter in duration, it maintains a yield of 2.5% which is approximately 0.2% above the yield of the benchmark index.

GBC Corporate Bond Fund Commentary

The GBC Corporate Bond Fund returned 1.5% for the quarter which was 1.4% ahead of the FTSE Canada Corporate Bond Index. For the year, the 5.7% return was strong in absolute terms, however 2.4% behind the benchmark. The Fund benefited from strong performance in issues such as General Electric, Maxar Technologies and Ford, however Teva lagged and the Fund's allocation to floating rate performed as expected, however underperformed the benchmark as Canadian yields fell for the year. At year end, the Fund had approximately 62% invested in floating rate issues which yield more than comparable fixed rate issues and support the Fund yield of 3%. This yield is approximately 0.20% higher than the index. Canso believes this is prudent positioning given the significant potential downside of a longer duration Fund if interest rates were to rise. At year end, the Fund continues to be positioned in higher-quality issues with approximately 47% of the Fund invested in A or higher rated issues. The Fund continues to focus on maintaining strong liquidity which would be utilized to fund purchases should the market deteriorate materially and buying opportunities arise.

GBC Global Balanced Fund Commentary

During the fourth quarter, the Fund reported a 4.4% return. In comparison, the Fund's custom benchmark index, comprised of 25% S&P/TSX Composite Index, 30% FTSE TMX Canada Universe Bond Index, and 45% MSCI All Country World Index, posted a 3.6% return for the period.

The Fund's gains were primarily driven by strength in the equity portion of the portfolio. International equities turned in the strongest returns followed by Canadian and US equities. The fixed income portion of the Fund, represented by the **GBC Corporate Bond Fund** and the **GBC Canadian Bond Fund**, delivered solid risk-adjusted returns in the context of a low interest rate environment.

Two funds were significant positive contributors to the Fund's performance during the quarter.

The **Guardian Capital Fundamental Global Equity Fund**, with a weight of approximately 15% in the Fund, was buoyed by large cap holdings in Europe and the United States. **The GBC International Growth Fund**, with a weight of approximately 7% in the Fund, delivered a strong performance supported by gains in positions in small cap companies in Europe, Asia and Latin America.

Two funds were neutral or negative contributors to the Fund's performance during the quarter.

The bond portion of the fund was affected by developments in the Canadian bond market where yields increased during the quarter. Narrowing credit spreads caused corporate bonds to outperform. Longer duration A-rated bonds underperformed both higher and lower rated bonds with short duration financials being the strongest performers in the corporate sector. Against that backdrop, **The GBC Corporate Bond Fund**, an approximately 24% weighting in the Fund, delivered positive absolute results that were ahead of the returns of its benchmark.

The GBC Canadian Bond Fund, an approximately 4% weighting in the Fund, declined slightly but outperformed its benchmark.

The GBC Corporate Bond Fund and the GBC Canadian Bond Funds have yields to maturity of 3% and 2.5% respectively.

Global Balanced Fund Outlook

Global equity markets continue to appear relatively attractive with healthy valuations and yields between 2% and 4% in major markets. Exceptions appear in some US and international information technology stocks. Earnings growth has decelerated in many markets but remains positive. Risks include political instability, continuing trade frictions, economic slowdown, and the accumulation of corporate and sovereign debt in some regions. The fixed income market has been difficult for investors given the prevailing environment of low yields. Both GBC bond funds continue to invest in high-quality issues, to maintain relatively short duration and strong liquidity. These characteristics position the Fund well in the event of either an increase in interest rates, as occurred during the quarter, or a deterioration in credit market fundamentals.

Business Update

Addition to The Team

During the quarter, Pembroke welcomed **Ksenia Chevtchenko** to our Montreal Office. Ksenia joins Pembroke Private Wealth Management Ltd. as a client services associate with over eight years of experience in the securities industry, most recently serving as an associate investment advisor at an independent Canadian wealth management firm. Ksenia is a graduate of the Moscow Institute of Economics, Politics, Law and Finance and the Concordia University John Molson School of Business. Ksenia speaks English, French and Russian.

Reinforcing Our Commitment to Responsible Investing

During the fourth quarter of 2019, Pembroke became a signatory to the United Nations Principles for Responsible Investment (**UNPRI**). The PRI is a non-profit organization of members dedicated to achieving a sustainable global financial system underpinned by good governance, integrity and accountability. The PRI is supported by the United Nations and other global policy makers although it is not part of the United Nations or affiliated with any government. Signatories to the PRI acknowledge the benefit to the environment and to society of an economically efficient, sustainable, global financial system and commit to supporting the following six voluntary principles:

1) We will incorporate Environmental, Social and Governance (**ESG**) issues into investment analysis and decision-making processes.
2) We will be active owners and incorporate ESG issues into our ownership policies and practices.
3) We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4) We will promote acceptance and implementation of the Principles within the investment industry.
5) We will work together to enhance our effectiveness in implementing the Principles.
6) We will each report on our activities and progress towards implementing the Principles.

Pembroke's Managing Partner **Ian Aitken** stated: "We are pleased to be signatories of the UN's Principles for Responsible Investing as these principles are aligned with our investment philosophy and should help create value over time." **PRI CEO Fiona Reynolds** said: "We are very pleased to welcome Pembroke as a signatory to the PRI. In joining the PRI, Pembroke is highlighting its commitment to consider E, S and G factors as part of investment strategies for its private wealth and institutional clients in Canada and beyond. We look forward to working with the Pembroke team."

As long-term, fundamental investors, Pembroke's mission is to help our clients secure their financial futures. As fiduciaries acting on behalf of our clients, we analyze the return and risk characteristics of all potential investments. Pembroke believes that sound ESG practices can reduce a firm's risk and improve its operational, financial and stock price performance and believe that the firm's clients will benefit from our support of the UNPRI.

The Pembroke Brand

On March 8, 1929, eight months before the great stock market crash, the Great Britain and Canada Investment Company was incorporated under Quebec charter. The investment trust traded on both the Montreal and the London Stock Exchanges under the ticker GBC. In September 1968 Pembroke Management was formed to provide the management services to GBC. Our GBC funds reflect this heritage. Almost ten years ago, Pembroke started a brand transition to unify the Pembroke brand and make Pembroke strategies and solutions more easily identifiable to clients. Pembroke will complete this transition and will unify all of our funds under the Pembroke brand name when we renew our prospectuses in 2020.

Pembroke In the Community

Pembroke Private Wealth Management is pleased to be the title sponsor of the **Canadian Ski Marathon** again this year. This two-day cross-country ski tour sees almost 2,000 participants cover all or part of the 160-kilometer course. First established in 1967, the event is North America's longest and oldest Nordic ski tour. It will start in the Laurentians on February 8th and end the following day in Lachute, Quebec. "As in investing, preparation, focus and persistence are key character traits of marathon skiing," says **Ian Aitken**, Pembroke Managing Partner. "This isn't a race; it's a great outdoor adventure and a wonderful way to celebrate winter. Pembroke is pleased to support an event that has become an annual tradition for many skiers and widely recognized as one of the longest events of its kind in the world."

PEMBROKE

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SINCE 1968

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.

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 1-800-668-7383 or refer to our website www.pml.ca.

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