PEMBROKE

Serving Private Clients and Institutions

April 11th, 2017

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On the Road Again

Pembroke often goes the "extra mile" with due diligence and our work on **DHX Media ("DHX")** is a good example. DHX is a leading independent producer of children's programming with a large library of shows distributed around the world through online channels and conventional broadcasters. We recently travelled to London to meet with its Founder and Chairman. Meeting at the headquarters of Wildbrain, we witnessed the company's fast growing on-line division that addresses the distribution of children's content primarily on YouTube.

YouTube started as a site for user-generated content. Over time, a growing part of the content posted by users was copyrighted material. That created a challenge for the content owners as this is, technically, piracy! As opposed to a legal fight, many content owners have embraced the challenge of learning how to monetize these "eyeballs" through advertising. They now regularly serve ads to viewers of authorized, and sometimes, unauthorized content. In the last decade YouTube has become a destination site that siphons a significant audience from conventional outlets. As YouTube has evolved it has created "channels" that aggregate and organize content by subject matter or special interest group. Tablets and smartphones allow children to become large consumers of YouTube content. Twelve of the top twenty "channels" are directed to them.

DHX created Wildbrain to exploit its own content and, where advisable, third party content. Wildbrain is a "multi-channel network" or "MCN". MCN's work with YouTube to offer content owners and advertisers a platform to help optimize revenue opportunities. For example, Wildbrain enhances content quality, directs traffic to content and conducts paid ad campaigns to drive awareness. As young viewers move from conventional television, this large and growing audience going on-line is clearly appealing to the toy advertisers.

At present there is a disconnect between the size of the viewership for these children's channels and the advertising rates charged for reaching this coveted demographic. If this market segment follows the same pattern as the specialty cable channels 25 years ago, then advertising rates will grow to reflect the number of viewers. On line advertising's benefit is that it allows advertisers to reach a specific audience while measuring the efficacy of its ads.

Wildbrain creates a revenue stream for DHX's existing library of content and from original content created exclusively for Wildbrain. During our site visit, we witnessed the team of animators creating new content and saw in real-time the advertising revenue being generated by DHX properties on the network. Wildbrain splits this revenue with YouTube, keeping 55%.

Wildbrain offers a dynamic work environment and the employees recognize and are energized by the large growth opportunity. The underlying increase in viewership and increasing advertising rates are driving rapid revenue growth. WIldbrain's revenues are expected to grow by more than 50% and should exceed $30m this fiscal year. The longer-term opportunity is significant as Wildbrain also selectively adds new channels to its universe by buying or licensing content. This additional content expands the total audience and the ad rates that can be charged. As total viewership continues to migrate from linear television to on-line viewing, these networks will siphon an increasing portion of the $70 billion currently spent on television advertising in the United States.

The shares of DHX have languished over the past 18 months as investors have worried about the decline of conventional broadcasting and the significant buildup in the production business which consumed capital. We remain optimistic because of our longer-term view. DHX is expected to return to free cash flow as new properties hit the market, the consumer products licensing business is growing nicely and the Wildbrain division is under-appreciated with substantial room for growth.

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

March 31st, 2017

Company	Q1 Price Change (CAD)	Revenue Growth, Current Fiscal Year	EBITDA Growth, Current Fiscal Year	Revenue Growth, Next Fiscal Year	EBITDA Growth, Next Fiscal Year
Descartes Systems	6%	15%	22%	11%	14%
BRP	10%	3%	11%	4%	7%
DIRTT Environmental	11%	17%	89%	16%	29%
DHX Media	-20%	3%	39%	9%	14%
Gildan Activewear	6%	8%	9%	5%	7%
Average	**3%**	**9%**	**34%**	**9%**	**14%**

Top Five U.S. Holdings

March 31st, 2017

Company	Q1 Price Change (USD)	Revenue Growth, Current Fiscal Year	EBITDA Growth, Current Fiscal Year	Revenue Growth, Next Fiscal Year	EBITDA Growth, Next Fiscal Year
HMS Holdings	12%	10%	7%	11%	14%
BofI Holding	-8%	20%	14%	16%	16%
j2 Global	3%	32%	17%	9%	15%
National General Holdings	-5%	10%	34%	10%	16%
Gentherm Incorporated	16%	7%	3%	7%	9%
Average	**4%**	**16%**	**15%**	**11%**	**14%**

Source: Consensus and Pembroke estimates

OVERVIEW OF THE QUARTER

US COMMENTARY

Successful investing requires that we constantly observe and check our behavioral biases as we appraise existing investment holdings and new opportunities. Pembroke's portfolio managers give each other the same advice and counsel we give our clients. One of our main refrains is: don't chase performance. Whether it is reversion to the mean or simple contrarianism at work, one period's worst performers can often be the next period's best performers. Why? In part because stocks are moving targets – sometimes they disappoint or uncertainty leads to short-term caution, but those factors are often quickly reflected in valuation. The lower valuation presents an attractive entry point if the long-term opportunity is intact. Chasing performance is a backward-looking strategy.

In the fourth quarter of 2016 we noted that the healthcare sector was the only sector in the Russell 2000 Index to post negative returns during the year. We highlighted that the US healthcare sector's powerful demographic tailwinds, myriad areas of innovation, and strong nexus with technology to cut costs and improve patient care were all at odds with the poor sentiment and falling valuations. In addition to adding to our US healthcare positions in late 2016 and early 2017, we visited several of our healthcare holdings and highlighted two of those visits in our newsletter: **Lifepoint ("LPNT")** and **HMS Holdings ("HMSY")**.

It was not entirely surprising that the healthcare sector reversed course during the first quarter of 2017 and was the Russell 2000 Index's top-performing sector. The low valuations and positive fundamentals at year-end 2016 created an attractive set-up heading into this year. The experience was a positive one for Pembroke and our shareholders and a reminder of the importance of focusing on the fundamentals that drive future performance. During the first quarter, Pembroke's US growth strategy performed well in both absolute terms and relative to the Russell 2000 benchmark. We were particularly pleased that the strategy's strong performance was widespread, coming from stocks in many sectors and from long-time significant portfolio holdings as well as newer "farm team" holdings that have recently entered the portfolio.

Pembroke's US strategy benefitted significantly from the healthcare sector including contributions from the names highlighted last quarter: LPNT and HMSY. The latter helps state governments recover improperly-paid Medicaid funds. Following Trump's victory, the stock dropped as fears spread that the Medicaid program would be cut. Pembroke's view was that even in a worst-case scenario, state governments would seek HMSY's help to stretch federal funding to the greatest possible degree.

More importantly, the company's long-term growth and upside are driven by its commercial initiatives, which now represent more than 50% of total company revenue and are growing at over 15% per annum. The company has made two compelling acquisitions in the past year and won a potentially significant federal healthcare contract. As the overall healthcare picture becomes clearer, Pembroke expects investors will focus on HMSY's growth potential, margin expansion, and robust free cash flow. In the meantime, we accept that the stock may be volatile around political machinations and are ready to take advantage of market opportunities.

MASONITE

Another area of the market that enjoyed strength was US housing. Stocks related to housing and homebuilding performed well as US housing starts continued their recovery. February's seasonally adjusted rate of privately-owned housing starts of 1.29 million units was up 6.2% over the same month last year. One of the portfolio's positions, **Masonite International Holdings ("DOOR")**, a manufacturer of residential and commercial doors, is ideally positioned to compete and gain market share and has also been making significant progress independent of the cycle.

The company reported strong results for 2016, with North American residential door sales up 13%. In addition to volume growth, the company has seen average unit price growth over the past 15 consecutive quarters. The company continues to increase its profit margins and its return on invested capital. DOOR also repurchased $110M of equity in 2016. Despite the impact of foreign exchange rates on its European results and a slowdown in the UK housing market caused by Brexit uncertainty, Masonite provided better than expected guidance for the current year and consensus earnings estimates have been increasing. Looking further out, the company expects 1.5M housing starts in the US by 2019 as well as favourable pricing for its products. While the outlook is strong, the stock has performed (too) well and Pembroke recently reduced its exposure to take the higher valuation risk into account.

BOFI HOLDING

Against the overall forward momentum of the strategy during the first quarter, some of the portfolio's holdings took a break. The shares of **Bofi Holding Inc ("BOFI")**, highlighted as strong performers in the fourth quarter of 2016, retreated in the first quarter of 2017, giving up some of the gains posted following the election of President Trump. Financial stocks had moved upwards as a group in anticipation of potential regulatory relief and higher interest rates, but investor expectations for progress on these fronts became more tempered as the quarter progressed. Our focus, again, is not on the past share price performance but on the fundamental progress and value of the business. Fundamentally, BOFI continues to perform well. The company's fourth quarter results showed robust loan growth, excellent credit quality, and attractive cost and return on capital metrics. Moreover, BOFI trades at an attractive valuation both on an absolute and relative basis compared to its peers in the banking industry.

The shares of **GTT Communications Inc ("GTT")** corrected during the first quarter of 2017 following a strong performance in 2016. GTT is an advanced communications provider to large corporate customers and is winning market share from the large incumbents. Late in 2016, the company completed its most important acquisition by adding state of the art assets and blue chip customers. The shares traded down in March following the fourth quarter earnings report. Management indicated that the organic growth rate for 2017 would be below the 8-10% target as the company completes the integration of its recent acquisition. Prior to this reduction in guidance, GTT has executed flawlessly and its capital-light business model generates significant free cash flow.

Pembroke is pleased with its US portfolio's positioning and the fundamental performance of the companies held. As part of our ongoing practice of improvement, we reviewed our investment process in 2016 and made subtle enhancements to portfolio construction and risk management. Mindful of market uncertainties, the outlook for the companies that we hold combined with these enhancements gives us confidence in the long-term return potential of the portfolio.

Canadian Commentary

In the first quarter, Pembroke's Canadian small capitalization ("small cap") equity portfolios earned positive absolute returns that modestly lagged the TSX Composite Index. As has occurred in previous periods, the portfolio's underweight position in the financial services sector was a headwind to relative performance as "large capitalization" bank stocks continued to show strength. Partially offsetting this effect was the portfolio's underweight position in energy as oil prices retreated from fourth quarter levels.

Several stocks suffered short-term disappointments that weighed on performance. Shares in **Lumenpulse ("LMP")**, a provider of LED-based systems to the architectural lighting industry, declined sharply during the period as the company reported quarterly results that lagged expectations and lowered financial guidance for the fiscal year. The company continues to grow at a rapid pace; however, volatility in US sales following the presidential election, sales force productivity issues and product delays led to a tempering of expectations. We view the issues as temporary and continue to believe that LMP's long-term growth opportunities are attractive.

Shares in **DHX Media ("DHX")**, an owner and producer of children's media assets, were weak in the first quarter as investors digested lower guidance from management for the remainder of the fiscal year and diminished free cash flow generation. Timing issues affected the outlook, as several program launches were delayed into future periods. While the lower expectations and stock price correction were disappointing, we believe DHX's media properties have strong underlying value unappreciated by the market.

In this quarter, two stocks made significant contributions to returns. Shares in **Tucows ("TC")**, an Internet services and telecommunications company, performed well as investors reacted positively to the company's acquisition of eNom, a domain name registrar. The deal was consummated at attractive valuation levels and is expected to be immediately accretive to Tucows' earnings. Pembroke believes that Tucows has a significant opportunity to grow its mobile and internet services businesses under the Ting brand, while concurrently deploying capital in a shareholder-friendly manner by buying back shares.

Shares in **Colliers ("CIG")**, a provider of a wide array of services to the commercial real estate industry, posted strong returns driven by interim results that exceeded market expectations. Colliers' international operations performed particularly well in the period, offsetting more tepid conditions in North America. Moreover, the company delivered impressive levels of profitability. Colliers' pipeline of work is robust, and should result in continued organic growth for the next several quarters.

Overall, we are encouraged by the performance of the strategy's holdings and believe the companies are well positioned to deliver continued earnings and cash flow growth and create, over time, value for the portfolio.

Dividend Commentary

The balanced **GBC Growth and Income Fund** had a strong start to 2017. The strategy not only performed well on an absolute basis but was ahead of its benchmark too.

The asset mix remained largely unchanged with 68% of the portfolio invested in equities. The fixed income component remained primarily invested in securities rated "A+" that, on average, had a collective yield to maturity of 2.2% and an adjusted portfolio duration of 4.3 years.

The income component of the strategy is generated from both dividends and interest. The gross yield is currently an annualized 3.4%. The growth component of the strategy stems primarily from the 41 dividend-paying companies that are expected to appreciate over time. Seventeen of these holdings, representing 40% of the equity exposure, are also held in Pembroke's standard Canadian growth mandate. The holdings unique to this portfolio generally have business models that are less volatile, pay meaningful dividends, and are expected to grow their earnings at a more moderate rate. Companies are selected for attractive well-funded, sustainable dividends as well as reasonable growth opportunities. Management quality and aligned interests with shareholders are also key investment considerations. The equity holdings in the **GBC Growth and Income Fund** mirror those held in the **Pembroke Dividend Growth Fund** and are reviewed in the following paragraphs.

The **Pembroke Dividend Growth Fund** increased during the first quarter and was ahead of its benchmark. Pembroke's overall goal is to provide a higher level of capital protection than our traditional growth funds while still securing a modest level of growth and current income. While we invest in business models that generally have more earnings visibility than companies in Pembroke's core growth funds, the dividend strategy still has a large exposure to equities that can, and likely will, experience volatility. As equity prices are, in part, a function of investor sentiment, the valuations and multiples that investors associate with public companies can vary widely, even if the underlying businesses do not experience such swings in their profitability and cash flows. Pembroke is encouraged by the long-term performance of this strategy and confident in its future.

The strong performance during the first quarter of 2017 was driven by improving earnings growth and a broad, positive contribution from many holdings. Despite stock price appreciation, the valuations for the portfolio declined during the quarter. The two most notable performers were **Collectors Universe ("CLCT")** and **Chesswood Group ("CHW")**. Shares of Collectors Universe, a provider of grading and authentication services for collectors of coins, sports cards, and memorabilia, performed well as investors responded to strong quarterly results. The company's initiatives to build a coin grading business serving Asian markets and to win market share in its bulk grading operations appear to have gained traction. Moreover, management indicated that spending that was undertaken to fund these initiatives should diminish going forward, allowing for greater cash flow generation to fund dividend payments.

Chesswood Group operates in the specialty finance industry providing loans to small and medium sized businesses for equipment and working capital purposes. Following the U.S. elections last November, shares in the company failed to participate in the sector rally. This set up a reasonably-priced stock to move higher in the first quarter after the company reported encouraging fourth quarter results. Credit losses were up, as expected, but more importantly, loan originations were strong – presaging growth in the coming year. The multiple expanded on this news but the valuation remains reasonable.

MEDIAGRIF

The two stocks that detracted the most from performance during the first quarter were **Sylogist ("SYZ")** and **Mediagrif Interactive ("MDF")**. Sylogist, a provider of software solutions to the municipal, non-profit, and industrial markets, saw its shares lag in the first quarter of 2017 as investors digested quarterly results that showed revenues declining on a year over year basis. The company is moving its customer base from one-time license sales to a subscription model with recurring revenues. While this change in the revenue model is pressuring near-term results, we remain confident in the underlying strength of the business. Management has been adding functionality to each of its software suites, and a reseller relationship with Microsoft should help the company win new accounts. Sylogist maintains a debt-free balance sheet and its dividend remains well funded.

Mediagrif is a technology company that owns several web and mobile platforms that provide customers solutions for managing business-to-business relationships. They reported weak growth from some of their properties during the most recent period. This result prompted investors to question the underlying growth potential of the business and we reduced the size of this position in the portfolio.

Pembroke continues to find attractive new opportunities for the **GBC Growth and Income Fund** and the **Pembroke Dividend Growth Fund**. We invested in three new holdings during the first quarter. These additions came from three very different companies spanning the real estate, materials and consumer discretionary sectors.

We are encouraged with the start to 2017 and our outlook remains constructive given the sound fundamentals being reported by most of the Fund's holdings. Travel by the portfolio managers remains a constant; both to monitor existing holdings and search for potential new investments. We continue to make appropriate changes to stock and sector weights and have sold three investment since the beginning of the year to buy new names that offer a more attractive combination of yield and growth.

INTERNATIONAL EQUITY COMMENTARY

Pembroke's international equity portfolio, the **GBC International Growth Fund**, posted a positive return for the first quarter and slightly trailed the Morgan Stanley Capital International (MSCI) All Country World ex USA Small Cap index benchmark.

Lower growth/low valuation companies within the international small cap growth universe outperformed the Fund's emphasis on higher growth companies. Low valuation leadership represents a continuation of the 2016 trend. Stock selection in the Information Technology (IT) and Materials sectors detracted from performance but was offset by positive selection in the Consumer Discretionary, Financials and Healthcare sectors. Within the IT sector, China-based **Hollysys Automation Technologies** was hampered by market share losses and a weaker outlook for its industrial automation business. Within Materials sector Japan-based **Nissan Chemical's** share price pulled back after a strong run in 2016.

The effects were mitigated by the high performance Italian braking company **Brembo** which reported ongoing rapid growth in its China business. The portfolio was also bolstered by positions in India's **Yes Bank** and **Indiabulls Housing Finance**, both of which rebounded on better than expected earnings results and a reduction in anxiety over the government's currency demonetization program.

The Fund's underweight position in the Emerging Asia region combined with overweight positions in the U.K. and the EMEA region (Eastern Europe, Middle East & Africa) detracted from performance; however, it was largely offset by positive stock selection in Japan, Developed Asia ex-Japan, and Emerging Asia. The exclusion of Canada was also positive for the quarter.

Notable sector positioning adjustments during the quarter included a reduction in Energy and an increase in Healthcare. The Fund remained overweighted in Financials and Industrials, offset by a continued underweight position in Consumer Staples, Materials and Real Estate. Geographically, the Fund remained overweighted in Europe and the U.K., and underweighted in Emerging Asia.

FIXED INCOME COMMENTARY

The **GBC Canadian Bond Fund** posted a positive return for the quarter but slightly trailed its benchmark FTSE TMX Canada Universe Bond Index. The **Pembroke Corporate Bond Fund** posted a positive return for the quarter slightly behind the benchmark FTSE TMX Canada Corporate Index.

Short bond yields continued to climb higher as the Federal Reserve made clear it expects to continue raising the fed funds rate this year. However; longer term yields fell towards the end of the quarter as investors began to raise doubts about economic growth and inflation. As expected, the Federal Reserve raised rates by a quarter point believing that the labour market has strengthened and inflation is creeping higher. The Fed signaled continued monetary tightening in 2017 as well. In Canada, yields were roughly unchanged in the short and long term end of the yield curve but fell in the medium-term. Corporate bonds outperformed government bonds as spreads narrowed across all maturities.

Both the **GBC Canadian Bond Fund** and the **Pembroke Corporate Bond Fund** continue to profit from their higher running yield in comparison to the benchmark indices. The **GBC Canadian Bond Fund** benefited from price appreciation in its holdings of longer dated TransCanada Pipelines and Highway 407 while the **Pembroke Corporate Bond Fund** had strong performance in its holdings of Bombardier, Sobeys and Teck Resources. The positive performance was slightly offset by the lower yielding floating rate note holdings in both portfolios.

At quarter end, the **GBC Canadian Bond Fund** yield-to-maturity stood at 2.2% and the duration at 4.3 years while the **Pembroke Corporate Bond Fund** duration was 2.2 years and yield to maturity 3.0%. The duration of both portfolios is significantly shorter than their benchmarks as we expect yields to rise as investors seek higher compensation from rising inflation. We have also gradually increased the credit quality of the portfolios as yield spreads have narrowed. We believe that certain parts of the market are trading at expensive levels and both Funds are well positioned to take advantage of opportunities that may arise.

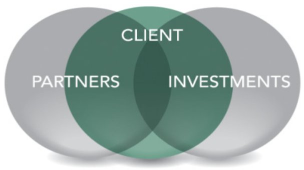
Outlook & Conclusion

It's almost a given that we can warn of the potential for market disruption or provide a list of economic and political concerns. Market fears generally prove to be road bumps, as innovation and progress power ahead and create opportunities for investors willing to look past the noise and a little further to the future.

For example, US healthcare policy since the election has been hard to discern. Will Obamacare be repealed and how will it affect hospitals and their suppliers? Though Pembroke studies these issues and takes them into account, the team is more focused on innovation, the demographic tailwinds provided by an aging population, and the ongoing need to reduce costs. The demise of the Affordable Care Act (Obamacare) did not come to fruition and contributed to the excellent performance of health care stocks this quarter. Had it been rolled back, would the drive to deliver superior care at a lower price or demands of an aging population have been materially altered? Pembroke does not think so. Whether it happens next quarter or whether it remains an ongoing battle within the Republican Party between the ultra-conservative "Freedom Caucus" and the more moderate wing is beyond our purview. The same can be said for tax and banking reform. A few executive orders relating to coal and the environment have been written but the major one regarding immigration has stalled – twice!

What Pembroke knows is this. We acknowledge that systematic forces and exogenous factors will affect the markets but the firm does not forecast nor can it be expected to know the severity (up or down) of these forces. Will Obamacare be rolled back? Will Trump be able to pass significant tax cuts or ease banking regulations? In Canada, will the government raise capital gains taxes in the foreseeable future? Too many factors are at work to know the answer to these questions in advance. Pembroke seeks companies that have a long runway for growth and the balance sheet or free cash flow to sustain a reasonable level of growth regardless of market conditions. Building our portfolios is a continual process of finding businesses like these and determining the right prices to pay for them. Our patience with our healthcare names during the final quarter of 2016 has paid dividends in the early part of 2017. Similarly, some of the stocks we held for a long time without significant price appreciation have finally been recognized by the markets, although they had been executing well for years. Overall, Pembroke continues to invest in a manner substantially in-line with the philosophy and principles first proposed at its inception some 49 years ago. The markets will bounce around and find new things to worry about daily. Pembroke remains focused on company-level opportunities and disciplined on valuation.

The Firm



ALIGNMENT *of* INTERESTS

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

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