cardinal UPDATE

JUNE 2013

DIVIDEND INCREASES

CAP REIT	2.6%
CIBC	2.1%
Canadian REIT	6.4%
Domtar Corp.	22.2%
National Bank	4.8%
Potash Corp.	25.0%

(During the period: May 1 – 31, 2013)

U.S. MARKETS SETTING NEW HIGHS – HOW HIGH IS TOO HIGH?

During the last month the S&P500, the broad U.S. market index, set a number of new records as it plodded steadily higher. The Dow 30 has followed suit. The S&P/TSX in Canada, by contrast, with its dominance in Energy, Financials and Materials, is still below its 2007 highs. Are we too late to invest in the U.S.? Should we brace for a Crash? What is the Market telling us? The short answer to this last is "Nothing". Markets will go up as long as more people want to buy than sell. With the U.S. economy gradually recovering, corporate profits on the rise and Europe apparently stable (at least for the moment), investors are finally taking the bait that the Central Banks have been dangling in front of them for months. Equity markets are finally going up as a result.

Are stocks now overpriced? By most measures, valuations (based on Price/Earnings ratios) are still reasonable and in-line with history. The nay-sayers point to the fact that corporate profit margins are higher than average and predict that they will come down. Therefore they say P/Es are actually higher than warranted. Others look at the Shiller P/E ratio, which takes average earnings over the past ten years in order to smooth out history. In rebuttal, Wharton finance professor Jeremy Siegel points out that U.S. corporate margins are higher than historically because U.S. companies have more international business than ever before which traditionally is a higher margin business. Information Technology businesses also have higher margins than other sectors and now represent a bigger share of the U.S. economy. It has also been pointed out that looking back at ten years of earnings from 2003 to 2012, the Shiller ratio is actually now skewed, rather than smoothed. The last ten years include both the "tech-wreck" and the financial crisis of 2008/2009. These years are terrible outliers for corporate earnings and therefore do not present a 'normalized' historical average.

Regardless of the debates, any advisor should make sure that investors are always prepared for market downturns. While currently there may be no particular reason for one, the market doesn't always need a reason. It is the sum of the actions of millions of emotionally motivated participants and volatility should be expected at any time. But of course, predicting when a correction will occur, and how much the market will go up before it corrects, is impossible. All we at Cardinal can do is make sure we only own companies that are fairly priced, that our companies have sustainable profit levels, and are likely to be providing high and/or growing dividends. If we can do that, our companies are worth their price, no matter what the market does.

COMPANY FOCUS

CISCO

Cisco was founded in 1984 and went public in 1990. We favour Cisco for its leading industry position, strong customer base, attractive valuation, rising free cash flow, and favorable shareholder distribution policy.

Cisco offers a broad portfolio of highly integrated hardware, software, and services to their core customers who include telecommunication providers such as AT&T and Verizon. They are squarely positioned to benefit from the trends in cloud, mobility, and video.

With a 3-5 year projection of annualized sales growth at 5-7% and EPS growth of 7-9%, we expect that given Cisco's current position, double digit dividend growth , high single digit EPS growth, and rising investor sentiment the shares are poised to continue moving higher.

Cisco has raised its dividend three times since they first began paying a dividend in April 2011. They intend more than half of their free cash flow to be paid out to shareholders each year in the form of dividends and share buybacks which aligns well with our investment philosophy. We believe Cisco is poised to be a leading IT provider to businesses and telecommunications service providers for many years to come.

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