BROADVIEW
Capital Management Inc.

January 13th, 2017

These letters are a means by which we communicate with our investors and others interested in what we do and how we do it. One of our very first investors and recipients of these letters was Mr. Pat Hodgson. We lost Pat recently and unexpectedly. We would dedicate this letter to his memory except that after such a mediocre year it would be a bit of a slight to Pat and his investing acumen. Instead, we'd just like to take a moment to say, "thank you Pat".

Thank you for being a mentor to Lee over the past decade. Thank you for all the discussions on your hometown of Buffalo and its beleaguered football team with Anthony. Thank you for believing in Broadview back when no one else even knew who we were.

What we appreciated most about Pat was that he had both the sage wisdom befitting his 76 years and an enthusiastic energy for investing that belied those years. As an investor he was both what we are and what we hope to become. We are all deeply saddened by his sudden passing and will very much miss his guidance and support. Our thoughts go out to his wife Camille, his daughter Sayre and his son Patrick.

Suffice to say, 2016 was a disappointing one for the Dark Horse and its investors. For the first time in the fund's eight years, we ended the year below where we started. In the past we've used a golf analogy in talking about our long game (stock selection and hedging) and our short game (trading). This past year we got both wrong.

Imagine a veterinarian being told that for the next year some random guy off the street would be removing tennis balls from the stomachs of Great Danes or performing Tommy John surgeries on gerbils[1]. Not only would this individual with no training, background or exceptional skill be able to perform these procedures, they would actually be able to perform them better than the experienced veterinarian could. For investment professionals this bizarre scenario is a reality.

Over a given period of time, anyone – *literally anyone* – can produce better results than even the most seasoned professional can. You know that Uncle you have who gets those great ideas from his buddies on the message boards? He had a banner 2016. What about the dreadlocked barista hippy who makes your latte every morning? We may be bringing her coffee soon as she was up huge last year. Thanks, weed stocks!

For our investors, 2016 would have gone far better if Lee and Anthony had simply not shown up for work. This is objectively true and the humbling part of our profession. It is also, unavoidable. Every once in a while every investor just steps in it…and step in it we did. This unavoidability (apparently that's a word) is why we manage the fund the way we do – we have position limits, we have sector

[1] Clearly Anthony is showing his ignorance of animals and their medical needs. Gerbils rarely, if ever, require Tommy John surgery.

limits and we don't use leverage. On top of these tangible limits we also exercise more intangible risk management through a healthy dose of skepticism and self-doubt. These restraints ensure that when we bugger things up, which is the technical term for what happened the past 12 months, we don't dig ourselves into such a massive hole that we cannot emerge from.

Just as we have written seven year-end letters not-so-humblebragging about our results, we now have to write one detailing how poorly we did. It was certainly more fun writing the previous letters, as we're sure it was to read them, so let's just get to it.

2016 in Review: Apparently a rising tide does *not* lift all boats

We have not been enthused by the overall risk-reward of the equity markets for the last couple of years. As such, we have kept our net exposure low. In 2016, particularly in Canada, that positioning had us fighting with one hand tied behind our back. It was clearly the wrong approach to a Canadian equity market that, despite a horrific start to the year, rocketed higher.

Having a net long position of between 30-50% and a beta-adjusted exposure of between 0-20%, as we did over the course of the year, explains why we would likely lag a levitating market. It does not explain the meaningful delta between the market and the Dark Horse.

The broad explanation for our relative crapulence, even after factoring in our low net exposure, is that we backed the wrong horses. Last year we attributed our success to "disaster avoidance" – winning by not losing. Conversely, 2016 was characterized by "success avoidance" – losing by not winning. Our long book was almost entirely devoid of material winners and had more than its fair share of losers.

The year's enduring theme of sluggishness culminated with a miserable finale in December. Maxim Power, which had been one of our few meaningfully positive contributors year to date, announced as we expected, that it had reached a deal to sell its U.S. operations. Unfortunately the price was at the very low end of our expected range and apparently far less than what the market had hoped for.

Furthermore, the company indicated in the press release announcing the sale that proceeds could be re-invested back into Alberta power generation assets. This statement flew in direct contrast to our belief that with the sale of Maxim U.S.A. (MUSA), the company would essentially wind up operations, liquidate its last few assets and, in some form or another, return all the proceeds to shareholders. Upon further analysis and investigation our original belief has been confirmed. The statements from the company are likely meant to maintain a negotiating stance that it doesn't *need* to sell the remaining few assets.

The reality of the situation hardly seemed to matter as the stock, our largest position, fell 25% on the first day of trading after the Christmas break. That hit wiped away any hope we would stay positive on the year. To repeat a Tina Fey joke from her SNL days, "Happy Birthday Jesus. I hope you like crap".

Maxim was not, in any way, the sole culprit. There were 18 positions that we were long the entire year (i.e. we owned some position in each for the entirety of 2016). This group serves as a decent proxy for what we'd call the core of the portfolio. Of this middling group, only 7 outperformed the "market"[2]. Of those that did, there were none that we would characterize as homeruns. 6 of those positions, a full one-third, were actually down on the year.

Our individual short book was not a relative detractor though it was, in aggregate, an absolute detractor. Our security selection on the short-side wasn't entirely bad. What was lacking was any sort of trading acumen. We actually made money on three shorts this year (Alaris Royalty Corp., Concordia

[2] For shorthand reference we used the S&P/TSX in Canada and the S&P 500 in the U.S..

Healthcare Corp. and Stella Jones Inc.) and only got hit hard on one (Westshore Terminals Ltd which we covered way too late). Where we absolutely should have done better on the short side is in trading. We had an opportunity to monetize gains on most every name we shorted this year. On top of that we covered our Concordia short far too early. This part of our "short game", specifically our trading around individual shorts, is one that we can and must improve on.

One notable winner from the long book, and there may really only be one worth mentioning, was our position in the convertible debentures of Guestlogix Inc. Don't bother looking up the ticker as the company is bankrupt[3] and has now been liquidated.

We acquired the publicly-traded convertible debentures in late 2015 with the belief that the equity had little to no value. Our underwriting indicated, however, that there was material value to be had between the senior debt and the equity layer in the capital structure. The vast majority of this value was represented by OpenJaw Technologies Limited which Guestlogix acquired in late 2014. The rest of Guestlogix was, in our mind, worth very little. This is despite the pre-OpenJaw Guestlogix having somehow enjoyed a market cap of over $200 million in early 2014.

When we accumulated our position we knew the company was short on cash. That's usually the case when bonds are trading at less than 50 cents on the dollar. As such, we underwrote the notes as if the company would be liquidated as opposed to it being a going concern. We didn't think that would happen but knew it was a legitimate possibility.

We, along with everyone else, were surprised by the announcement in early February that the company was filing for CCAA Protection[4]. While the announcement was initially jarring we went back to our files and realized that this turn of events could actually accelerate our returns.

Thankfully for debenture holders, there hadn't been sufficient time for the Board and management team who destroyed the value of Guestlogix to mess up OpenJaw as well. The acquired company was never fully integrated which meant it never got a Guestlogix stink to it and, more importantly, was much easier to sell as a standalone business. If OpenJaw could be sold for anywhere near fair value, the proceeds, in our estimation, would be sufficient to generate a solid return on our cost basis regardless of what the other assets fetched or how much money was frittered away by greedy CEOs or exorbitant banking and legal fees.

In the end, OpenJaw was sold for essentially what Guestlogix paid for it, representing upside to our base case estimates. The majority of those proceeds have since been distributed to debenture holders representing a substantial crystalized gain for our investors. For the year, our Guestlogix holding generated more than 200bps of total return for the fund easily making it the biggest single contributor.

To ensure the rights of debenture holders were being considered, an ad hoc credit committee was formed at the beginning of the onset of the process with Lee serving as one of its members. Lee's involvement, along with that of other committee members, certainly played a role in the positive outcome. Broadview currently has positions on the Boards of three investments (two are material holdings – WesternOne Inc. and RDM Corp) and is actively engaged behind the scenes (alone or, more often, with like-minded partners) on multiple other files. While in a bull market this level of active engagement may not be necessary to make money, it remains an important part of how Broadview manages and protects its investors' capital. We have seen our activism pay off in the past and expect it to continue to bear fruit in the coming year.

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[3] In a year when anyone could have made a great return just by buying an index ETF or Canadian bank stocks our biggest winner came from taking an airline software company through CCAA. Is there anything more Broadview than that?

[4] The Canadian version of Chapter 11

To wrap up 2016, it was as if we had a batting order where our #9 hitter managed to go 3-4 with a couple doubles while the heart of our order went a combined 0-16 with 13 strikeouts and grounded into three double plays. That's not a formula for winning baseball. It is however, not a permanent formula. Slumps can be broken and players can be switched out of the lineup. With a tweak here and there, along with a healthy dose of mean reversion, we should have the Dark Horse back to its winning ways sooner rather than later.

2017 and Beyond: DeMar the Visionary

We now go back to the issue of what it is we do well and how we add value in a crowded, competitive field. It is our firm belief that 2016 was an anomaly for the Dark Horse and that the previous seven years are a far better indicator of what we bring to the table. To back this up we naturally move to the Hardwood for a discussion of basketball.

DeMar DeRozan has had a wonderful start to the season as has his team, our hometown Toronto Raptors. The team's leading scorer, DeRozan ranks fourth in the entire NBA racking up more than 28 points per game. Great, "Let's go Raptors" you say, "but isn't talking about sports just an effort to distract us from your mediocre year"?

The answer, of course, is "yes" but there is also a more salient point to this. The NBA game has changed over recent years with far more emphasis being put on the three point shot. Over the past twenty seasons, three point attempts per game have increased from 12.7 to 26.8. In a typical NBA game there are now more threes attempted than free throws. There are a number of reasons for this but much of the increase, particularly in recent years, has been driven by analytics. The study of probabilities and shooting percentages has determined that the three-point shot is a "better" shot than a two-point shot – better meaning that it has a higher expected point outcome.

DeRozan is an outlier. There is only one player in the top 50 scorers who has attempted fewer three point shots per game than DeMar has. That player is Hassan Whiteside who has not attempted a single three-pointer all season. The Miami Heat center ranks 48th in the league in scoring with 17.3 points per game, 11 less than our man DeMar. Unlike Whiteside, DeRozan is not a seven-footer scoring all his points off of tap-ins and dunks. He is a shooting guard – a perimeter player.

Consensus is firm that the game has changed and that shooting from downtown is the key to scoring more points. Scoring more points means winning more basketball games. Despite these widely-accepted truths one weirdo up in Canada is doing the exact opposite.

DeMar's season begs two questions:

1. Why does he insist on playing the game differently than everyone else?
2. Why is it working?

The first answer is simple. DeMar is doing what he's good at. He is a uniquely talented pull-up shooter and a terrible three-point shooter. Conventional wisdom is now unanimously stating that the average player should shoot threes as opposed to twos. The consensus belief is held even more fervently when it comes to the mid-range twos that DeMar favours[5] taking, yet DeMar is not changing and nor should he. He has been playing long enough to know what his strengths are and that after eight years in the league he is not about to turn into the next Dell Curry[6].

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[5] Canadian spelling. We'll also use the metric system where applicable. Take that, Antonio Davis!
[6] We understand the next Dell Curry, being his son Steph, already exists.

The second question is a little more difficult to answer. Why has DeMar's game elevated from solid all-star level to elite, "in the conversation for MVP" level despite the fact that he is supposedly "doing it all wrong"? He is averaging five more points a game than he did last year which is a nearly unheard of leap for a player at this stage in his career with no material change in health, playing time or schemes. He didn't get laser eye surgery, lose 50 pounds or suddenly learn how to dribble. He's basically the same guy doing what he's always done but with far better results. What gives?

Sports, like investing, are complex and competitive systems. Everyone involved, be they coaches, players or front office personnel, are devoted to creating advantages for their teams while shutting down any advantages the opponents may have gained. Those who are visionary and forward-thinking can identify such unique advantages that can be exploited until others catch on. Remember the Wildcat formation that swept the NFL a few years back? It worked for a while until defensive coordinators caught on and effectively shut it down. The Neutral Zone Trap and its relative demise is perhaps an equivalent that hockey fans can relate to[7].

While the thinking around the superiority of the three-point shot was once revolutionary, it has now become entirely mainstream. Perhaps we have reached the stage where it is now, through the evolution of the game, being competed away. The inefficiency that the early adopters exploited with their unique approach to the game may be gone. DeMar, who the analytics crowd derides as a dinosaur for his insistence on playing the game the way it was played twenty years ago, may be the only true visionary in the game today. With not just the early adopters but also the fast followers and the begrudging laggards shooting and defending the three, is it not unreasonable to believe that space has opened up for DeMar's now "one of a kind" game? DeMar appears to be embracing his uniqueness and is taking more "bad shots" as a percentage of his total shots than ever before….and they're going in!

"So now we get to the DeMar is actually Broadview part of the metaphor, right?"

We see you've read a few of our letters before. We will now ask the same two questions about the Dark Horse that we did about DeRozan, with one slight amendment to make the response more relevant to the upcoming year:

1. Why are we still doing what we do?
2. Why *will* it work in the future?

Why do we continue to invest in obscure securities that often require active engagement and don't often trade with any relation to the market as a whole? Furthermore, why hedge? The answer is that this is how we know to invest and this is what we do well. While the definition of "Broadview Stocks" can broaden over time it is limited to a certain segment of the market. In times of extreme ebullience that segment shrinks even further.

Those who just joined us recently may question this claim but our track record suggests a certain level of acumen in doing things the Broadview way. Conversely, we are as capable at making momentum calls or day trading as DeMar is at making threes. We will stick to where we have proven an ability to generate returns commensurate with the risk we are taking.

A unique approach offers the possibility of finding opportunities that others can't or won't find. This is true in investing, sports and most any other field. We know what we do is not commonplace. We are also certain that our way of investing is not likely to become more widely practiced. The reasons for this are as much structural to the industry as they are based on human factors.

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[7] In actuality, it was likely the enforcement of obstruction and interference penalties post the lockout, as opposed to any competitive strategies, that lessened the effectiveness of the dreadful and excitement-killing trap.

Certainly after such an upwards run on the equity markets, the human aspects of investing will push investors more towards that which has worked, i.e. owning large, liquid, high-growth stocks and not holding any cash or going short. Enthusiasm, much like reticence, is highly contagious. #FOMO is perhaps a more modern way to express this sentiment.

That dynamic, however, could be switched off in short order with another plunge in oil prices or one inadvertent Russian phrase slipping out during an inauguration speech. Much like other contagions, enthusiasm can be eradicated suddenly. A structural change that we are seeing with the buy side should, however, have more staying power than the typical ebbs and flows of fear and greed.

Increasingly pools of capital are growing larger and more passive. Many factors are driving this with none appearing to abate anytime soon. It is this change that gives us confidence in answering question number two that, yes, our approach will work even better in the future. We touched on this dynamic a bit in our September letter as it related to the opportunities in spin-offs. There we discussed how large passive and quasi-passive (i.e. most mutual funds) are unable to invest in smaller, more nuanced investments that don't fit neatly into one narrative or can't be measured with a single simple metric.

As these pools come to dominate more and more of the equity market the issue will become even more acute. The threshold in terms of size and simplicity for public companies to find an audience will inch higher and higher. More and more companies will simply find themselves in a void of attention and interest.

That void is exactly where we operate and where we do our best work. Everyone else will be fighting it out to find value amongst a smaller and smaller pool of companies. Going back to the hoops analogy, the three point line is becoming increasingly crowded with taller and more athletic defenders. Meanwhile, if you take a few steps towards the basket there is literally no one to stop you from scoring. Just ask DeMar.

Certainly the movement of capital towards these larger pools may create more volatility for those few investors who chose to invest as we do. The disconnect between intrinsic value and quoted price may grow ever wider before correcting. This may test the patience of investors in this growing void. Ultimately, however, the rewards will more than justify the increased volatility that could occur.

2017: No, *specifically*, what's going to happen next year?

So this whole DeMar Dark Horse analogy attempts to make the case that what we do is differentiated and will exploit growing inefficiencies over time. It doesn't speak directly to the environment we currently operate in and how we are approaching it.

Let's first go back eight years to when we launched the Dark Horse. In early 2009, America had just inaugurated a black man to be President for the first time in the nation's history. The election of the young and oratorically-gifted Senator from Illinois represented a rare glimmer of enthusiasm and hope for a populous dealing with the crippling aftermath of the 2008 financial crisis. The stock market had been crushed leaving great businesses at, in retrospect, once in a lifetime type valuations. Less than great businesses could be had for next to nothing.

On Bay Street, market participants were still paralyzed by fear. Those who had survived the crisis were moving to "high grade" their portfolios populating them with the few names that had performed well during the preceding year – Telcos, pipelines, Wal-Mart etc.

With the benefit of hindsight, we should have invested everything we had, and more. The more risk, the better. That being said, we did see enough opportunity to leave our steady jobs and strike out on our own to launch the Dark Horse. Anthony's daughter was about to turn two and his wife was pregnant with their first son. Talk about risk-on!

Fast forward to today. America is just about to inaugurate its first ever orange muppet. The stock market sits at, or ever so near, all-time highs. Great businesses trade at nosebleed valuations as do most not so great businesses. Optimism is in abundance while skepticism is nowhere to be found.

On Bay Street, the "game" is back on with greed being the dominant emotion. Every day just before the close our inboxes are being filled with notices of new issues – a significant number with insiders selling. Many of those who haven't been able to keep up with the escalating indices are buying what has worked – junior resource companies, leveraged financials and weed stocks[8].

The investing environments of early 2009 and early 2017 appear about as opposite as two could possibly be. This is not apples and oranges. This is apples and a dumpster full of oranges on fire, outside a propane factory, in the fireworks district. The first clearly turned out to be a wonderful time to be long and strong. Maybe the current period will also turn out to be a great time to throw money at the market. We're not so sure. That whole dumpster fire thing seems *kinda* dangerous.

Needless to say, the younger versions of us are not quitting their jobs to launch value funds right now. While everyone is somewhat susceptible to the fear of missing out (that FOMO we referenced earlier) we cannot rouse ourselves into an enthusiastic bullish stance no matter how much we want to join the party. Anything short of "it's different this time" and we can't craft a fundamental explanation as to how stocks are attractive. Certainly this is not for lack of trying and we continue to progress though new files looking for opportunities to invest.

We'd like to end this letter by expressing a sentiment that may seem very unusual coming from us – we are very excited and optimistic about the opportunities to come for the Dark Horse and its investors. While that may appear to come out of left field given the previous narrative of dumpster fires and weed stocks, it actually doesn't. Eventually all this complacency and over-valuation will likely give way to some sort of correction. In the aftermath there is certain to be opportunity. The scale of this opportunity will only be exacerbated by the structural changes in the Canadian market we highlighted earlier.

We thought such opportunities would have already presented themselves and so did our friend Pat Hodgson. We met with him just weeks before his passing. In between telling us about his daily tennis matches and bemoaning the lack of cheap stocks, he described to us how he stayed up late and still got in early to the office the day Trump was elected. He was giddy with excitement, so he told us, about all the bargains that could be had as the market was surely to implode. Unfortunately for us and Pat that washout we all thought was coming never happened.

Rest assured Pat we will continue our search for great deals just as you would have. Your nose for value, willingness to look where others can't or won't and appetite to actively fight for the rights of shareholders will continue to serve as a model for how Broadview invests.

Thank you all (wherever you may be) for your continued commitment and support. All the best to everyone for 2017,

Anthony Hammill   Lee Matheson

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[8] Yes, weed stocks. For those of you with far more interesting things to do than follow the Canadian equity markets, there are at last count 34 publicly-traded marijuana stocks in Canada with a combined market cap of over $4 billion. Yay Canada! (souce:marijuanaindex.com)

Series	November 30, 2016	December 31, 2016	Monthly Return	YTD Return	Annualized Return Since Inception (April 3, 2009)
Master – Class A	$239.80	$235.24	-1.90%	-2.21%	11.7%
Series 5 - June 2015 – Class A	$239.55	$234.99	-1.90%	-2.21%	
Series 1 - Feb 2016 – Class A	$238.93	$235.27	-1.53%	2.23%	
Series 2 – Mar 2016 – Class A	$239.16	$235.27	-1.63%	1.55%	
Series 3 – Apr 2016 – Class A	$239.81	$235.24	-1.90%	-2.48%	
Series 4 – May 2016 – Class A	$239.71	$235.15	-1.90%	-3.34%	
Series 5 – June 2016 – Class A	$239.81	$235.24	-1.90%	-3.08%	
Series 6 – July 2016 – Class A	$239.51	$234.95	-1.90%	-4.19%	
Series 7 – Aug 2016 – Class A	$239.27	$234.72	-1.90%	-4.81%	
Series 8 – Nov 2016 – Class A	$239.38	$234.82	-1.90%	-4.77%	
Series 9 – Dec 2016 – Class A	$239.80	$235.24	-1.90%	-1.90%	

**From inception return used for series launched during the year*

All numbers reported after fees and expenses. See subscription confirmations for your Series.

About Broadview Capital Management Inc. and the Broadview Dark Horse LP:

Broadview is the manager of the Broadview Dark Horse LP ("The Dark Horse"), a fundamental-based long/short investment partnership. Broadview utilizes its relatively small size, contrarian nature and willingness to perform extensive due diligence to deliver strong risk-adjusted returns for its investors. The managers concentrate on going where others can't or won't to find investment opportunities.

The firm is run with the philosophy that it will manage "as much money as it deserves to manage" and that a dedication to working hard for existing clients is the best way to grow the business in a sustainable fashion. It is not Broadview's intention to take on additional investment mandates for the foreseeable future beyond the Dark Horse LP. Broadview was founded in October of 2008 and the Dark Horse was launched in April of 2009.

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