



## News Highlights

### Financial Services Companies

Bank of Nova Scotia reported Q2/14 cash earnings of \$1.71 billion, or \$1.40 per share, compared with \$1.49 billion, or \$1.23 per share, in the year-ago period. The year-over-year improvement is due to higher asset growth and core banking margin, positive operating leverage, increased banking and wealth management fees, exceptionally high securities gains, and strong trading revenues (namely in fixed income). This was partly offset by increased operating expenses, higher provisions for loan losses and a higher effective tax rate. Provisions for loan losses increased 5% sequentially to \$375 million (36 bps of loans and acceptances) due to higher loan losses in Canadian personal lending coupled with higher international provisions in the Caribbean, partly offset by lower provisions in Latin America. Capital exceeded expectations with the Core Equity Tier 1 ratio improving 40 bps to 9.8%. As a result of their strong capital position, BNS announced a 1% share buyback program.

BNP Paribas- Sunday Times article suggested Sumitomo Mitsui and Mitsubishi UFJ may be keen to expand their US operations and may be keen on BNP's businesses. There appeared little in the Japanese press its expected MUFG to be the best placed of the two. SMFG may be interested but unlikely they would outbid MUFG, who were rumoured to have been negotiating with BNP over Bank of the West a few years ago. It would be a good fit for integration with their existing Union Bank subsidiary in California and they have long desired to expand in the US. Its expected a sale of BancWest could generate 27bps of Core Equity Tier 1 capital or higher if cost synergies were reflected in a higher consideration. Separately, New York state's top banking regulator, Benjamin Lawsky, is understood to be asking BNP Paribas to fire some senior executives as part of a settlement of allegations that the French bank violated U.S. sanctions. A junior minister in French President Francois Hollande's government criticised a U.S. criminal probe against BNP on Sunday, saying France would not allow itself to be pushed around by its ally.

CIBC reported adjusted cash earnings of \$2.17 per share compared to consensus expectations of \$2.02 per share. The beat in the quarter was mainly due to strong adjusted earnings in Wholesale Banking of \$228 million, up 22% year/year, mainly due to better-than-expected trading revenues of \$255 million and solid corporate and investment banking revenues. Retail & Business Banking also had a solid quarter with adjusted earnings of \$563 million driven by strong volume

growth in CIBC-branded mortgages (+15% y/y) and lower loan losses, partially offset by lower Net Interest Margin (-5 bps q/q) due to the sale of the Aerogold credit card portfolio. Wealth Management reported record adjusted earnings of \$121 million, up 32% year/year due to higher fee-based earnings from asset growth, the Atlantic Trust acquisition, and higher contribution from its investment in American Century. Asset quality, excluding the Caribbean charge, improved this quarter to \$185 million, down 15% quarter/quarter and 24% year/year. Capital is strong with an industry-leading Core Equity Tier 1 ratio of 10.0%. The dividend was increased 2% to \$1.00 per share.

CI Financial Group: Last Wednesday, after the close, Scotiabank announced a secondary offering, on a bought-deal basis, to sell 72 million CI shares at \$31.60 (6% discount) for ~\$2.3 billion. The offering was a success and so Scotia exercised the overallocation and so now owns just 7.7%. In our view, this largely removes the overhang on CI shares. According to management, CI did not participate in the bought deal, which in our view allows CI to increase share buybacks and potentially pursue large acquisitions.

Citigroup Inc. CFO John Gerspach said second-quarter trading revenue could be down 20% to 25% from year-earlier levels in a market he described as "becalmed." The decline might curtail overall institutional revenue for the period, Gerspach, 60, told analysts and investors last week. He spoke during an investment conference in New York. The market feels like participants are "sitting on the sidelines," Gerspach said, referring to both fixed-income and equity trading. "There isn't a lot of direction." ( source :Bloomberg).

Lloyds Banking Group expects to float about 25% of its TSB Bank business on the London Stock Exchange next month through an Initial Public Offering with the remainder to be sold before the end of 2015, the bank said last Tuesday. Banking industry sources said last week they expect TSB to be priced at less than its book value of £1.5bn (\$2.73bn), meaning Lloyds would make a loss on the sale of the 200-year old brand. Lloyds is required to sell the 631 branches making up TSB because of a European Union requirement that Lloyds creates more competition in the British market after receiving state aid in the financial crisis. "TSB has a national network of branches, a strong balance sheet and significant economic protection against legacy issues," Lloyds CEO Antonio Horta-Osorio said in a statement.



National bank of Canada ; reported operating Earnings Per Share of \$1.05 which was slightly ahead of the consensus estimate of \$1.04. Overall, an in-line quarter with good results from Wealth Management, positive operating leverage in P&C Banking and stable credit; partially offset by softer trading revenue. The bank's Core Equity Tier 1 ratio improved to 8.7% (from 8.3% last quarter). Any share buyback remains on hold until the Core Equity Tier 1 ratio reaches the stated target of 9%. National increased its quarterly dividend by 4% to \$0.48.

Royal Bank of Scotland is shrinking in the US under regulatory pressure from the Federal Reserve, with the loss of hundreds of jobs, mainly in mortgage trading, executives told staff on Tuesday. The bank will eliminate about 300 jobs over the course of two years as part of an effort to reduce its assets ahead of new rules set out by the US central bank, according to people familiar with RBS's strategy. The new Fed rules require higher capital and liquidity levels and impose tough stress tests on foreign broker-dealers with more than \$50bn in assets. RBS, which has \$85bn of assets in its broker-dealer, is choosing to shrink below the threshold in order to escape the Fed's clutches instead of adapting to the new regime. (Source : Financial Times)

Standard Chartered announced it appointed John Cusack as its new head of global compliance, the latest move by the bank to bolster its financial crime unit in the face of increasing regulatory pressure. Mr. Cusack, who was the deputy head of global compliance at UBS, succeeds David Howes, who will continue to work at the bank's financial crime risk mitigation program, the bank said in a statement Wednesday. Mr. Cusack, will start his job in August and will be based in London.

Wells Fargo & Co. doesn't intend to grow its investment bank beyond the United States, though it hopes to boost its market share in the next few years, Chief Financial Officer John Shrewsbury said at a financial services conference in New York last Wednesday. "We're very U.S.-centric," the new CFO said during his second public presentation. "We're likely to largely remain that way." But Wells Fargo has an opportunity to grow its market share beyond the 6% it currently holds, he said, and is likely to "pick up a couple of points" without drastically changing its risk model. ( Source : Wall Street Journal)

## Dividend Payers

Hutchison Whampoa : European Commission has conditionally approved Hutchison's move to become the second largest mobile player in Ireland through the acquisition of O2 Ireland from Telefonica. Hutchison announced the acquisition in June 2013, and will pay Eu780 million plus performance-based future consideration of Eu70 mn for O2. The combination of 3 Ireland and O2 Ireland will result in a much stronger #2 player with 2.1 million active subscribers and 38% market share behind Vodafone's 2.4 million subscribers and 44% market share. For Hutchison, scale benefits will be material as the active subscriber base is nearly 4x higher than the 548,000 it had at end-2013.

Roche/Genentech held an analyst meeting at ASCO on Sunday. The company spent time highlighting its efforts in immunology (I/O), both in South San Francisco (Genentech) and Basel (Roche). It covered some of the basic science behind I/O, and gave various updates specific to its efforts. The presentation also included a discussion of the various cancer areas it has a significant present, apart from I/O. The near-term outlook for Roche is favorable in our view. The company should be able to post reasonable revenue and EPS growth in 2014, and it sits in front of various pipeline catalysts throughout the year both in oncology and in other disease areas. In oncology, most closely watched will be various data sets with its anti-PD-L1 cancer drug MPDL3280A, and also combination studies of PD1s/PD-L1s with Avastin; in the non-oncology space, it will be interesting to learn what the development plans are for ophthalmology drug lampalizumab that has suddenly been put on the radar screen of investors, and that could eventually become a major product for the company.

Tesco to sell House of Fraser goods on its website. The Daily Mail reported over the weekend that Tesco has signed a deal to sell c2,000 of the House of Fraser department store chain's products through its Tesco Direct website. Customers will be able to collect Clubcard points with House of Fraser purchases and collect their items at supermarket outlets through the Click & Collect service. House of Fraser should benefit from Tesco's large customer base and marketing power while Tesco should benefit though extending its range into a more premium area. Tesco has significant online growth ambitions under its multichannel chief Robin Terrell, who has worked for House of Fraser and John Lewis in the past. House of Fraser multichannel chief Andy Harding said there was "huge potential to create a great working relationship between our businesses", which will begin with dining and bedroom products and include the store's



own-brand lines such as Linea and Pied a Terre. The deal is a clear step forward for Tesco's plan to build a 'marketplace' business with similarities to that of Amazon. Baby products chain Mamas & Papas and electronics retailer Maplin have already signed deals like this, but the greater the number of retailers that do deals with Tesco, the more other retailers are likely to want to get involved as the critical mass builds.

## Economic Activity, Consumer and Business Conditions

U.S. manufacturing activity, a sector which accounts for just over 10% of the national private sector economy, grew in May but the pace was slower than expected. The manufacturing ISM shed 1.7% to 53.2 in May, the first decline in four months although this is the 18th consecutive month above the key 50 level. Indeed, activity around the world seems to be in a similar state....examples: the Eurozone expanded at a slower pace (52.2%), ditto for the U.K. (57.0%), China picked up a tad (50.8%), and Japan contracted but at a slower pace (49.9%). Similar to April, the number of US industries that reported growth came in at 17 (out of 18 surveyed), albeit last month, none contracted.

US housing price growth slowed to just 0.2% in the first three months of 2014, latest figures show. According to the S&P/Case-Shiller index, the slowdown in growth compared with the previous quarter was partly caused by tighter bank lending regulations. Further compounding the problem is rising student loan debt, which has discouraged first-time buyers. Nationally, US home prices are still up 10.3%, compared with a year earlier.

EU Elections - Eurosceptic parties enjoyed major gains across Europe in a blow to the Brussels establishment. France's Front National and Greece's Golden Dawn are among the parties to triumph in European elections. The French Front National, which wants to leave the euro and the EU, have won 25% of the vote, more than ten points ahead of Francois Hollande's Socialists. In Greece, the extreme right party Golden Dawn have won almost 10% of the vote.

Ukraine - Exit polls show billionaire Petro Poroshenko winning Ukraine's presidential ballot with a mandate to resolve the crisis that's roiled the nation since November. The polls showed the billionaire garnered more than 50% of the vote. Russian

President, Putin, who doesn't recognize the government in Kiev, has said he would work with the winner.

## Financial Conditions

The European Central Bank will eclipse all else in economic terms this week, following heavy hints that monetary policy will be loosened in a variety of ways. Financial markets have been buoyed by the prospect of cheaper money in the euro zone and would react sharply if the central bank does not deliver on Thursday. Its policymakers have done nothing to disabuse investors of the notion of imminent action. A clutch of senior sources told Reuters earlier this month that the ECB was preparing a package of policy options for its June 5 meeting, including cuts in all its interest rates and targeted measures aimed at boosting lending to small- and mid-sized firms. (Source:Reuters).

US - US Federal Reserve policymakers remain determined to flatten the yield curve as much as possible, having indicated they expect 'exceptionally low levels of interest through 2014 with the Federal Reserve carefully calibrating the beginning of unwinding quantitative easing and undertaking that the Federal Reserve will keep rates low until mid 2015. The U.S. 2 year/10 year treasury spread is now 2.13% and the U.K.'s 2 year/10 year treasury spread is 1.92% - meaning investment banks remain constrained from profiting from a steep yield curve and instead are seeking operational efficiencies, including job cuts and lower compensation, to maintain acceptable levels of profit, i.e. above their costs of capital. It seems the top tier 6-9 investment banks will continue to command their market and possibly increase their share - as barriers to entry for newcomers have in our view been raised.

Influenced by the withdrawal of quantitative easing, the U.S. 30 year mortgage market rate has increased to 4.12% - (was 3.31%, end of November 2012 the lowest rate since the Federal Reserve began tracking rates in 1971), as the Federal Reserve effectively continues to give priority to incentivising home ownership. Existing U.S. housing inventory is at 5.2 months supply of existing houses. So the combined effects of low mortgage rates, near record high affordability, a more promising economic recovery, job creation, and low prices are finally supporting the housing market with housing inventory well off its peak of 9.4 months and we believe now in a more normal range of 4-7 months.



The VIX (volatility index) is 11.40 and while, by its characteristics, the VIX will remain volatile, we believe a VIX level below 25 augurs well for quality equities.

## **Mutual Funds**

Portland currently offers 5 mutual funds:

- Portland Advantage Fund
- Portland Canadian Balanced Fund
- Portland Canadian Focused Fund
- Portland Global Banks Fund
- Portland Global Income Fund
- Portland Global Dividend Fund

## **Private/Alternative Products**

Portland also currently offers 3 private/alternative products:

- Portland Focused Plus Fund LP
- Portland Private Income Fund
- Portland GEEREF LP

## **Net Asset Value:**

At the close of business each day we publish the Net Asset Values (NAV) of our mutual funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

## **Closed-End Fund**

Spreads on the closed-end fund remain, in our view, very attractively priced to purchase.

The Portland Investment Counsel's 2013 Fourth Quarter Fund update is now available on the website.

At the close of business each day we publish the Net Asset Values (NAV) of our funds onto our Portland website at <http://www.portlandic.com/prices/default.aspx>

The price details published are replicated here below from which you can see we also highlight whether the funds share prices are trading at a premium or discount to their respective NAV.

# Market Commentary



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Source: Thomson Reuters, Bloomberg, Company reports

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